SCORPIO BULKERS INC.
Form F-1/A
August 29, 2014
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As filed with the Securities and Exchange Commission on August 29, 2014

Registration No. 333-197949

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Amendment No. 1

to

Form F-1

REGISTRATION STATEMENT

UNDER

THE SECURITIES ACT OF 1933

SCORPIO BULKERS INC.

(Exact name of registrant as specified in its charter)

Marshall Islands	**4412**	N/A
(State or other jurisdiction of incorporation or organization)	(Primary Standard Industrial Classification Code Number)	(I.R.S. Employer Identification Number)

Scorpio Bulkers Inc. **9, Boulevard Charles III** **MC 98000 Monaco** **(011) 377 9798 5716** (Address, including zip code, and telephone number, including area code, of registrant s principal executive offices)	**Seward & Kissel LLP** **Attention: Lawrence Rutkowski, Esq.** **Edward S. Horton, Esq.** **One Battery Park Plaza** **New York, New York 10004** **(212) 574-1200** (Name, address and telephone number of agent for service)

Copies to:

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Approximate date of commencement of proposed sale to the public:

As soon as practicable after this Registration Statement becomes effective.

If any of the securities being registered on this Form are being offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act, check the following box. ¨

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities to be Registered	Proposed Maximum Aggregate Offering Price (1)(2)	Amount of Registration Fee (3)
% Senior Notes due	$57,500,000	$7,406

(1) Includes an additional $7,500,000 aggregate principal amount of our % Senior Notes due that the underwriters have an option to purchase.
(2) Estimated solely for the purpose of calculating the registration fee pursuant to Rule 457(o) under the Securities Act of 1933, as amended.
(3) Calculated in accordance with Rule 457(o) under the Securities Act of 1933, as amended. The amount of the registration fee was previously paid on August 7, 2014.

The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933, as amended, or until the Registration Statement shall become effective on such date as the U.S. Securities and Exchange Commission, acting pursuant to said Section 8(a), may determine.

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The information in this Prospectus is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This Prospectus is not an offer to sell these securities and it is not soliciting an offer to buy these securities in any jurisdiction where the offer or sale is not permitted.

SUBJECT TO COMPLETION, DATED AUGUST 29, 2014

PRELIMINARY PROSPECTUS

$50,000,000

% Senior Notes due 2019

Scorpio Bulkers Inc.

We are offering $50,000,000 aggregate principal amount of our % Senior Notes due 2019 (the Notes). We have granted the underwriters the option to purchase, exercisable during the 30-day period beginning on the date of this prospectus, up to an additional $7,500,000 aggregate principal amount of the Notes. The Notes will bear interest from , 2014 at a rate of % per year. The Notes will mature on , 2019. Interest on the Notes will be payable quarterly in arrears on the 15th day of March, June, September and December of each year, commencing on , 2014. We may redeem the Notes at our option, in whole or in part, at any time on or after at a redemption price equal to 100% of the principal amount to be redeemed, plus accrued and unpaid interest to, but excluding, the redemption date, as described in Description of Notes Optional Redemption. In addition, we may redeem the Notes in whole, but not in part, at any time at our option, at a redemption price equal to 100% of the principal amount to be redeemed, plus accrued and unpaid interest to, but excluding, the redemption date, if certain events occur involving changes in taxation, as described in this prospectus under Description of Notes Optional Redemption for Changes in Withholding Taxes.

The Notes will be senior unsecured obligations and will rank equally with all of our existing and future senior unsecured and unsubordinated debt. The Notes will be effectively subordinated to our existing and future secured debt, to the extent of the value of the assets securing such debt, and will be structurally subordinated to all existing and future debt and other liabilities of our subsidiaries. The Notes will be issued in minimum denominations of $25.00 and integral multiples of $25.00 in excess thereof.

Investing in our Notes involves risks. Please read "Risk Factors" beginning on page 22.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or passed upon the adequacy or accuracy of this prospectus. Any representation to the contrary is a criminal offense.

	Per Note	Total
Public offering price	$	$
Underwriting discounts and commissions		
Proceeds, before expenses, to us [1]	$	$

(1) Plus accrued interest from if settlement occurs after that.

We have applied for the listing of the Notes on the New York Stock Exchange under the symbol SLTB. If approved for listing, trading on the New York Stock Exchange is expected to commence within 30 days after the Notes are first issued.

We expect that delivery of the Notes will be made to investors on or about , 2014, through the book-entry system of The Depository Trust Company for the accounts of its participants, including Euroclear Bank S.A./N.V., as operator of the Euroclear system, and Clearstream Banking, *société anonyme*.

Stifel **Deutsche Bank Securities** **Jefferies**

Prospectus dated , 2014

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You should rely only on the information contained in this prospectus or in any free writing prospectus we may authorize to be delivered to you. We have not, and the underwriters have not, authorized any other person to provide you with additional, different or inconsistent information. If anyone provides you with additional, different or inconsistent information, you should not rely on it. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission (the SEC) is effective. We are not, and the underwriters are not, making an offer to sell these securities in any jurisdiction where the offer or sale is not permitted. You should not assume that the information appearing in this prospectus is accurate as of any date other than the date on the front cover of this prospectus unless otherwise specified herein. Our business, financial condition, results of operations and prospects may have changed since that date. Information contained on our website does not constitute part of this prospectus.

We have not taken any action to permit a public offering of these securities outside the United States or to permit the possession or distribution of this prospectus outside the United States. Persons outside the United States who come into possession of this prospectus must inform themselves about and observe any restrictions relating to the offering of these securities and the distribution of this prospectus outside the United States.

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PROSPECTUS SUMMARY

This summary highlights information that appears later in this prospectus and is qualified in its entirety by the more detailed information and financial statements included elsewhere in this prospectus. This summary may not contain all of the information that may be important to you. As an investor or prospective investor, you should carefully review the entire prospectus, including the section of this prospectus entitled Risk Factors and the more detailed information that appears later in this prospectus before making an investment in our Notes. The information presented in this prospectus assumes, unless otherwise indicated, that the underwriters option to purchase up to $ aggregate principal amount of the Notes is not exercised.

Unless otherwise indicated, references to Scorpio Bulkers, the Company, we, our, us or similar terms refer to the registrant, Scorpio Bulkers Inc., and its subsidiaries, except where the context otherwise requires. We use the term deadweight tons, or dwt, expressed in metric tons, each of which is equivalent to 1,000 kilograms, in describing the size of our vessels. Unless otherwise indicated, all references to U.S. dollars, dollars, U.S. $ and $ in this prospectus are to the lawful currency of the United States of America.

Our Business

We are an international shipping company that was incorporated in the Republic of the Marshall Islands on March 20, 2013 for the purpose of acquiring and operating the latest generation of newbuilding drybulk carriers with fuel-efficient specifications and carrying capacities of greater than 30,000 dwt. We believe that it is an opportune time to acquire these vessels because acquisition costs for these vessels are currently near the lowest average levels of the past 10 years. In addition, we believe that recent advances in shipbuilding design and technology should make these latest generation vessels more fuel-efficient than older vessels in the global fleet that compete with us for charters, providing us with a competitive advantage. Our fleet transports a broad range of major and minor bulk commodities, including ores, coal, grains, and fertilizers, along worldwide shipping routes, and are, or are expected to be, employed primarily in the spot market or in spot market-oriented pools of similarly sized vessels. As of the date of this prospectus, our operating fleet consists of 19 drybulk vessels, of which 18 are vessels that we charter-in and one is a recently delivered Kamsarmax vessel from our Newbuilding Program, with an aggregate carrying capacity of approximately 1.5 million dwt, which we refer to as our Operating Fleet. We also have one time charter-in contract that is scheduled to commence during the first half of 2015 and contracts for the construction of 79 newbuilding drybulk vessels at established shipyards in Japan, China, South Korea and Romania, which we have agreed to acquire for an aggregate purchase price of $3,070.8 million, including 29 Ultramax vessels, 22 Kamsarmax vessel and 28 Capesize vessels, each with a carrying capacity of between 60,000 dwt and 180,000 dwt and an aggregate carrying capacity of approximately 8.6 million dwt. We refer to these newbuilding vessels as our Newbuilding Program. We expect to take delivery of the vessels in our Newbuilding Program as follows: one vessel in 2014, 42 vessels in 2015 and 36 vessels in 2016. Until we have taken delivery of a larger number of the vessels in our Newbuilding Program, we do not anticipate earning a material amount of revenues from our operations.

In December 2013, we completed our underwritten initial public offering of 31,300,000 common shares at $9.75 per share, and in January 2014, the underwriters in the initial public offering exercised their option to purchase an additional 4,695,000 common shares. In February 2014, we completed our offer to exchange unregistered common shares that were previously issued in Norwegian equity private placements (other than the common shares owned by affiliates of us) for common shares that were registered under the Securities Act of 1933, as amended, which we refer to as the Exchange Offer. Upon completion of the Exchange Offer, holders of 95,766,779 unregistered common shares validly tendered their shares in exchange for such registered common shares, representing a participation rate of 99.7%. On July 31, 2014, we delisted from the Norwegian OTC. Our common shares currently trade on the New York Stock Exchange under the symbol SALT.

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Following the completion of this offering, we expect to have in excess of $ million of available cash. As of June 30, 2014, we have paid a total of $764.1 million in initial installment payments due under our shipbuilding contracts for our Newbuilding Program. We plan to finance the remaining contractual commitments of $2,338.8 million with the net proceeds received from this offering, cash on hand, cash flows from operations, borrowings under committed and proposed new secured credit facilities, and from capital raised in the public and private debt and equity markets. We cannot assure you that we will be successful in obtaining the financing necessary to fund all of our remaining contractual obligations under our shipbuilding contracts or will be able to take delivery of all the vessels we have agreed to acquire.

In addition, we plan to use all or substantially all of the net proceeds from this offering and the net proceeds from future equity or debt offerings or both, together with the amounts we expect to be available to us under our credit facilities to fund installment payments due under our Newbuilding Program, and the remaining amounts, if any, for general corporate purposes and working capital. Our intention is to acquire additional latest generation drybulk carriers with fuel-efficient vessel specifications and carrying capacities of greater than 30,000 dwt, either directly from shipyards or from owners with existing newbuilding vessel contracts. We may also acquire secondhand vessels that meet our stringent vessel specifications. The timing of these vessel acquisitions will depend on our ability to identify suitable vessels on attractive acquisition terms. Although we may have the capacity to obtain additional financing, we intend to maintain moderate levels of leverage of not more than 60% of the value of our vessels collateralizing our indebtedness on a consolidated basis.

Our Co-Founder, Chairman and Chief Executive Officer, Mr. Emanuele Lauro, is a member of the Lolli-Ghetti family, which in 2009 founded Scorpio Tankers Inc. (NYSE: STNG), or Scorpio Tankers, a large international shipping company engaged in seaborne transportation of refined petroleum products. As of August 28, 2014, it owned or had contracted for the construction of 75 tanker vessels. Mr. Lauro is currently its Chairman and Chief Executive Officer. The Lolli-Ghetti family also owns and controls the Scorpio Group, which includes Scorpio Ship Management S.A.M., or SSM, which provides us with vessel technical management services, Scorpio Commercial Management S.A.M., or SCM, which provides us with vessel commercial management services, and Scorpio Services Holding Limited, or SSH, which provides us and other related entities with administrative services and services related to the acquisition of vessels. Our Co-Founder, President and Director, Mr. Robert Bugbee is also the President and a Director of Scorpio Tankers, has a senior management position at the Scorpio Group, and was formerly the President and Chief Operating Officer of OMI Corporation, or OMI, which was a publicly traded shipping company. SSM and SCM also provide technical and commercial management services to Scorpio Tankers as well as unaffiliated vessel owners.

Our Relationship with the Scorpio Group

We believe that one of our principal strengths is our relationship with Scorpio Tankers and the Scorpio Group of companies. Our vessel operations are managed under the supervision of our board of directors, by our management team and by members of the Scorpio Group of companies. We expect that our relationship with Scorpio Tankers and the Scorpio Group of companies will give us access to their relationships with major international charterers, lenders and shipbuilders. We will have access to Scorpio Group s customer and supplier relationships and their technical, commercial and managerial expertise, which we believe will allow us to compete more effectively and operate our vessels on a cost efficient basis. The Scorpio Group, through SSH, beneficially owns approximately 1.0% of our common shares, excluding the common shares to be issued pursuant to the Administrative Services Agreement. Please see Security Ownership of Certain Beneficial Owners and Management.

In addition to our relationship with Scorpio Tankers, we believe there are opportunities for us to benefit from operational, charterer and shipyard-based synergies due to our broader shared relationship with the Scorpio Group which includes:

- SSM, which provides vessel technical management services for 40 vessels owned by third-parties, including Scorpio Tankers, and provides us with the same services for all of our vessels.

- SCM, which provides vessel commercial management services for 100 vessels owned by third-parties, including Scorpio Tankers, and provides us with the same services for all of our vessels. SCM manages 75 vessels (excluding the vessels in our fleet) through the spot market-oriented Scorpio Group Pools, which currently include the Scorpio LR2 Pool, the Scorpio Panamax Tanker Pool, the Scorpio MR Pool, Scorpio Handymax Tanker Pool, the Scorpio Ultramax Pool, Scorpio Kamsarmax Pool and the Scorpio Capesize Pool.

- SSH, which provides us and related entities with administrative services and services related to the acquisition of vessels.

We can provide no assurance, however, that we will realize any benefits from our relationship with Scorpio Tankers or the Scorpio Group.

Emanuele Lauro, our Co-Founder, Chairman and Chief Executive Officer, is a member of the Lolli-Ghetti family which owns and controls SCM, our commercial manager, and SSM, our technical manager. These relationships, and other relationships between certain of our executive officers and members of the Scorpio Group, may create certain conflicts of interest between us, on the one hand, and other members of the Scorpio Group, including our commercial and technical manager, on the other hand. For example, our Chief Executive Officer, President, and Chief Operating Officer each participate in business activities not associated with us, including serving as members of the management team of Scorpio Tankers, and are not required to work full-time on our affairs. We expect that each of our executive officers devote a substantial portion of his business time to the completion of our Newbuilding Program and management of the Company. Additionally, our executive officers named above serve in similar positions in the Scorpio Group. This may create conflicts of interest in matters involving or affecting us and our customers, including in the chartering, purchase, sale and operation of the vessels in our fleet versus vessels managed by other members of the Scorpio Group. As result of these conflicts, it is not certain that these conflicts of interest will be resolved in our favor, and other members of the Scorpio Group, who have limited contractual duties, may favor their own or other owners interest over our interests. Please see Risk Factors Our Chief Executive Officer, President and Chief Operating Officer will not devote all of their time to our business, which may hinder our ability to operate successfully.

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Our Fleet

The following table summarizes key information about our Newbuilding Program and our Operating Fleet as of the date of this prospectus:

Newbuilding Program

Capesize

Vessel Name		Expected Delivery (1)	DWT	Shipyard
1	Hull H1309 TBN SBI Puro	Q1-15	180,000	Waigaoqiao
2	Hull H1310 TBN SBI Valrico	Q2-15	180,000	Waigaoqiao
3	Hull H1311 TBN SBI Maduro	Q3-15	180,000	Waigaoqiao
4	Hull H1364 TBN SBI Belicoso	Q4-15	180,000	Waigaoqiao
5	Hull H1365 TBN SBI Corona	Q1-16	180,000	Waigaoqiao
6	Hull H1366 TBN SBI Diadema	Q2-16	180,000	Waigaoqiao
7	Hull H1367 TBN SBI Estupendo	Q3-16	180,000	Waigaoqiao
8	Hull S1205 TBN SBI Camacho	Q1-15	180,000	Sungdong
9	Hull S1206 TBN SBI Montesino	Q2-15	180,000	Sungdong
10	Hull S1211 TBN SBI Magnum	Q2-15	180,000	Sungdong
11	Hull S1212 TBN SBI Montecristo	Q3-15	180,000	Sungdong
12	Hull S1213 TBN SBI Aroma	Q3-15	180,000	Sungdong
13	Hull S1214 TBN SBI Cohiba	Q4-15	180,000	Sungdong
14	Hull S1215 TBN SBI Habano	Q4-15	180,000	Sungdong
15	Hull S1216 TBN SBI Lonsdale	Q1-16	180,000	Sungdong
16	Hull S1217 TBN SBI Partagas	Q1-16	180,000	Sungdong
17	Hull S1218 TBN SBI Parejo	Q1-16	180,000	Sungdong
18	Hull S1219 TBN SBI Toro	Q2-16	180,000	Sungdong
19	Hull S1220 TBN SBI Tuscamina	Q2-16	180,000	Sungdong
20	Hull H1059 TBN SBI Churchill	Q4-15	180,000	Daewoo
21	Hull H1060 TBN SBI Perfecto	Q4-15	180,000	Daewoo
22	Hull H1061 TBN SBI Presidente	Q1-16	180,000	Daewoo
23	Hull H1062 TBN SBI Panatela	Q1-16	180,000	Daewoo
24	Hull H1063 TBN SBI Robusto	Q2-16	180,000	Daewoo
25	Hull HN1058 TBN SBI Behike	Q3-15	180,000	Daehan
26	Hull HN1059 TBN SBI Monterrey	Q4-15	180,000	Daehan
27	Hull HN1060 TBN SBI Macanudo	Q4-15	180,000	Daehan
28	Hull HN1061 TBN SBI Cuaba	Q1-16	180,000	Daehan
Aggregate Capesize Newbuilding DWT			**5,040,000**	

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Kamsarmax

Vessel Name		Expected Delivery [1]	DWT	Shipyard
1	Hull H1285 TBN SBI Charleston	Q3-14	82,000	Waigaoqiao
2	Hull S1680 TBN SBI Samba	Q1-15	84,000	Imabari
3	Hull S1681 TBN SBI Rumba	Q3-15	84,000	Imabari
4	Hull 1090 TBN SBI Electra	Q3-15	82,000	Yangzijiang
5	Hull 1091 TBN SBI Flamenco	Q3-15	82,000	Yangzijiang
6	Hull 1092 TBN SBI Rock	Q4-15	82,000	Yangzijiang
7	Hull 1093 TBN SBI Twist	Q1-16	82,000	Yangzijiang
8	Hull SS164 TBN SBI Salsa	Q3-15	81,600	Tsuneishi
9	Hull SS179 TBN SBI Merengue	Q1-16	81,600	Tsuneishi
10	Hull S1228 TBN SBI Capoeira	Q1-15	82,000	Hudong
11	Hull S1722A TBN SBI Conga	Q2-15	82,000	Hudong
12	Hull S1723A TBN SBI Bolero	Q2-15	82,000	Hudong
13	Hull S1229 TBN SBI Carioca	Q2-15	82,000	Hudong
14	Hull S1724A TBN SBI Sousta	Q3-15	82,000	Hudong
15	Hull S1725A TBN SBI Reggae	Q1-16	82,000	Hudong
16	Hull S1726A TBN SBI Zumba	Q1-16	82,000	Hudong
17	Hull S1231 TBN SBI Macarena	Q1-16	82,000	Hudong
18	Hull S1735A TBN SBI Parapara	Q1-16	82,000	Hudong
19	Hull S1736A TBN SBI Mazurka	Q2-16	82,000	Hudong
20	Hull S1230 TBN SBI Lambada	Q3-15	82,000	Hudong
21	Hull S1232 TBN SBI Swing	Q2-16	82,000	Hudong
22	Hull S1233 TBN SBI Jive	Q3-16	82,000	Hudong
Aggregate Kamsarmax Newbuilding DWT			**1,807,200**	

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Ultramax

	Vessel Name	Expected Delivery (1)	DWT	Shipyard
1	Hull 1907 TBN SBI Hera	Q2-16	60,200	Mitsui
2	Hull 1906 TBN SBI Zeus	Q2-16	60,200	Mitsui
3	Hull 1911 TBN SBI Poseidon	Q3-16	60,200	Mitsui
4	Hull 1912 TBN SBI Apollo	Q3-16	60,200	Mitsui
5	Hull S870 TBN SBI Echo	Q3-15	61,000	Imabari
6	Hull S871 TBN SBI Tango	Q3-15	61,000	Imabari
7	Hull S-A098 TBN SBI Achilles	Q1-16	61,000	Imabari
8	Hull S-A089 TBN SBI Cronos	Q1-16	61,000	Imabari
9	Hull S-A090 TBN SBI Hermes	Q1-16	61,000	Imabari
10	Hull NE180 TBN SBI Bravo	Q1-15	61,000	Nacks
11	Hull NE181 TBN SBI Antares	Q1-15	61,000	Nacks
12	Hull NE182 TBN SBI Maia	Q3-15	61,000	Nacks
13	Hull NE183 TBN SBI Hydra	Q3-15	61,000	Nacks
14	Hull NE194 TBN SBI Hyperion	Q2-16	61,000	Nacks
15	Hull NE195 TBN SBI Tethys	Q2-16	61,000	Nacks
16	Hull DE018 TBN SBI Leo	Q1-15	61,000	Dacks
17	Hull DE019 TBN SBI Lyra	Q2-15	61,000	Dacks
18	Hull DE020 TBN SBI Subaru	Q2-15	61,000	Dacks
19	Hull DE021 TBN SBI Ursa	Q3-15	61,000	Dacks
20	Hull CX0610 TBN SBI Athena	Q1-15	64,000	Chengxi
21	Hull CX0651 TBN SBI Pegasus	Q3-15	64,000	Chengxi
22	Hull CX0652 TBN SBI Orion	Q4-15	64,000	Chengxi
23	Hull CX0612 TBN SBI Thalia	Q4-15	64,000	Chengxi
24	Hull CX0653 TBN SBI Hercules	Q1-16	64,000	Chengxi
25	Hull CX0627 TBN SBI Perseus	Q1-16	64,000	Chengxi
26	Hull CX0654 TBN SBI Kratos	Q2-16	64,000	Chengxi
27	Hull CX0655 TBN SBI Samson	Q2-16	64,000	Chengxi
28	Hull CX0613 TBN SBI Phoebe	Q3-16	64,000	Chengxi
29	Hull CX0656 TBN SBI Phoenix	Q3-16	64,000	Chengxi
Ultramax NB DWT			**1,795,800**	
Aggregate Newbuild DWT			**8,643,000**	

* As used in this prospectus, Dacks refers to Dalian COSCO KHI Ship Engineering Co. Ltd., Daehan refers to Daehan Shipbuilding Co., Ltd., Daewoo refers to Daewoo Mangalia Heavy Industries S.A., Chengxi refers to Chengxi Shipyard Co., Ltd., Hudong refers to Hudong-Zhonghua Shipbuilding (Group) Co., Inc., Imabari refers to Imabari Shipbuilding Co. Ltd., Mitsui refers to Mitsui Engineering & Shipbuilding Co. Ltd., Nacks refers to Nantong COSCO KHI Ship Engineering Co., Ltd., Sungdong refers to Sungdong Shipbuilding & Marine Engineering Co., Ltd., Tsuneishi refers to Tsuneishi Group (Zhoushan) Shipbuilding Inc., Waigaoqiao refers to Shanghai Waigaoqiao Shipbuilding Co., Ltd., and Yangzijiang refers to Jiangsu Yangzijiang Shipbuilding Co. Ltd.

(1) Expected Delivery refers to the quarter during which each vessel is currently expected to be delivered from the shipyard.

Operating Fleet

Owned Vessel

Vessel Name	Year Built	DWT	Vessel Type
SBI Cakewalk	2014	82,000	Kamsarmax

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Time Chartered-in Vessels

Vessel Type	Year Built	DWT	Where Built	Daily Base Rate	Earliest Expiry
Post-Panamax	2010	93,000	China	$13,250	23-Oct-14(1)
Post-Panamax	2011	93,000	China	$13,500	24-Oct-14(2)
Post-Panamax	2009	93,000	China	See Note(3)	9-May-15(3)
Kamsarmax	2009	82,500	Japan	$14,500	8-Feb-15(4)
Kamsarmax	2012	82,000	South Korea	$15,500	23-Jul-17(5)
Kamsarmax	2011	81,900	South Korea	$12,750	3-Apr-15(6)
Kamsarmax	2012	81,500	South Korea	$14,500	7-Dec-14(7)
Kamsarmax	2011	81,500	South Korea	$15,000	15-Jan-16(8)
Kamsarmax	2012	81,000	South Korea	$15,000	10-Feb-15(9)
Kamsarmax	2012	79,500	China	$14,000	23-Jan-15(10)
Panamax	2004	77,500	China	$14,000	3-Jan-17(11)
Panamax	2014	77,000	Japan	$16,000	4-Mar-15(12)
Panamax	2009	76,500	Japan	$14,000	1-Dec-14(13)
Panamax	2007	75,500	South Korea	$13,750	14-Feb-15(14)
Ultramax	2010	61,000	Japan	$14,200	1-Apr-17(15)
Supramax	2010	58,000	China	$14,250	12-Dec-16(16)
Supramax	2011	58,000	China	$13,750	18-Jan-15(17)
Supramax	2015	55,000	Japan	$14,000	30-Jun-18(18)
Handymax	2002	48,500	Japan	$12,000	31-Jan-17(19)
Total TC DWT		**1,435,900**			

(1) This vessel has been time chartered-in for eight to 10 months at Company s option at $13,250 per day. The vessel was delivered on February 23, 2014.

(2) This vessel has been time chartered-in for seven to nine months at the Company s option at $13,500 per day. The vessel was delivered on March 24, 2014.

(3) This vessel has been time chartered-in for 10 to 14 months at the Company s option at a rate of 90% of the Baltic Panamax 4TC Index. The Company has the option to extend this time charter for an additional 10 to 14 months at the same rate of hire. The vessel was delivered on July 9, 2014.

(4) This vessel has been time chartered-in for 11 to 13 months at the Company s option at $14,500 per day. The Company has the option to extend this time charter for one year at $15,500 per day. The vessel was delivered on March 8, 2014.

(5) This vessel has been time chartered-in for 39 to 44 months at the Company s option at $15,500 per day. The Company has the option to extend this time charter for one year at $16,300 per day. The vessel was delivered on April 23, 2014.

(6) This vessel has been time chartered-in for 11 to 13 months at the Company s option at $12,750 per day. The Company has the option to extend this time charter for one year at $13,750 per day. The vessel was delivered on May 3, 2014.

(7) This vessel has been time chartered-in for 10 to 12 months at Company s option at $14,500 per day. The vessel was delivered on February 7, 2014.

(8)

This vessel has been time chartered-in for 23 to 28 months at the Company s option at $15,000 per day. The Company has the option to extend the charter for an additional 11 to 13 months at $16,000 per day. This vessel was delivered on February 15, 2014.

(9) This vessel has been time chartered-in for 12 to 14 months at Company s option at $15,000 per day. The vessel was delivered on February 10, 2014.

(10) This vessel has been time chartered-in for 11 to 14 months at the Company s option at $14,000 per day. The Company has the option to extend the charter for an additional 11 to 14 months at $14,750 per day. This vessel was delivered on February 23, 2014.

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(11) This vessel has been time chartered-in for 32 to 38 months at the Company s option at $14,000 per day. The vessel was delivered on May 3, 2014.
(12) This vessel has been time chartered-in for 12 to 13 months at Company s option at $16,000 per day. The vessel was delivered on March 4, 2014.
(13) This vessel has been time chartered-in until December 1, 2014 which may be extended for an additional two months at the Company s option. The charter hire rate is $15,900 per day until June 23, 2014 and $14,000 per day thereafter, including the option period. The vessel was delivered on January 23, 2014.
(14) This vessel has been time chartered-in for 11 to 13 months at the Company s option at $13,750 per day. The Company has the option to extend the charter for an additional year at $14,750 per day. The vessel was delivered on March 14, 2014.
(15) This vessel has been time chartered-in for three years at $14,200 per day. The Company has options to extend the charter for up to three consecutive one year periods at $15,200 per day, $16,200 per day and $17,200 per day, respectively. This vessel was delivered on April 13, 2014.
(16) This vessel has been time chartered-in for 20 to 24 months at the Company s option at $14,250 per day. The Company has the option to extend the charter for an additional 10 to 12 months at $14,850 per day. This vessel was delivered on April 12, 2014.
(17) This vessel has been time chartered-in for ten to 13 months at the Company s option at $13,750 per day. This vessel was delivered on March 18, 2014.
(18) This vessel has been time chartered-in for three years at $14,000 per day. The Company has options to extend the charter for up to two consecutive one year periods at $15,000 per day and $16,000 per day, respectively. This vessel is expected to be delivered during the first half of 2015.
(19) This vessel has been time chartered-in for 34 to 37 months at the Company s option at $12,000 per day. The Company has options to extend the charter for up to three consecutive one year periods at $12,750 per day, $13,600 per day and $14,800 per day, respectively. This vessel was delivered on March 31, 2014.

Employment of Our Fleet

Generally, we intend to operate our vessels in spot market-oriented commercial pools, in the spot market or, under certain circumstances, on time charters. See Business Employment of our Fleet.

Spot Market-Oriented Commercial Pools

To increase vessel utilization and thereby revenues, we intend to participate in commercial pools with other shipowners with similar modern, well-maintained vessels. By operating a large number of vessels as an integrated transportation system, commercial pools offer customers greater flexibility and a higher level of service while achieving scheduling efficiencies. Pools employ experienced commercial managers and operators who have close working relationships with customers and brokers, while technical management is performed by each shipowner. The managers of the pools negotiate charters with customers primarily in the spot market. The size and scope of these pools enable them to enhance vessel utilization rates for pool vessels by securing backhaul voyages, which is when cargo is transported on the return leg of a journey, and contracts of affreightment, or COAs, thus generating higher effective TCE revenues than otherwise might be obtainable in the spot market, while providing a higher level of service offerings to customers.

The pools in which our vessels operate, or are expected to operate, are spot market-oriented commercial pools managed by our commercial manager, which we refer to as the Scorpio Group Pools, which expose us to fluctuations in spot market charter rates. The Scorpio Group Pools have been newly formed or will be formed prior to the delivery of the vessels in our Newbuilding Program and have limited to no operating history. Our vessels are expected to participate in the Scorpio Group Pools under the same contractual terms and conditions as the third party vessels in the pool. Each pool will aggregate the revenues and expenses of all of the pool participants and distribute the net earnings calculated on (i) the number of pool points for the vessel, which are

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based on vessel attributes such as cargo carrying capacity, fuel consumption, and construction characteristics, and (ii) the number of days the vessel operates in the period. SCM, as operator of the Scorpio Group Pools, charges $300 a day for each vessel, whether owned by us or chartered-in, plus a 1.75% commission on the gross revenues per charter fixture. SCM is expected to negotiate voyage charters, short duration time charters, and contracts of affreightment; manages procurement of bunkers, port charges and administrative services; and distributes the cash earnings.

SCM, a Monaco corporation controlled by the Lolli-Ghetti family of which our co-founder, Chairman and Chief Executive Officer is a member, is, or will be, responsible for the administration of the pool and the commercial management of the participating vessels, including the marketing, chartering, operating and bunker (fuel oil) purchases for the vessels. The pool participants will remain responsible for all other costs including the financing, insurance, manning and technical management of their vessels. The earnings of all of the vessels will be aggregated and divided according to the relative performance capabilities of the vessel and the actual earning days each vessel is available.

We currently employ, or expect to employ, all of the vessels in our Operating Fleet in the Scorpio Group Pools.

Spot Market

A spot market voyage charter is generally a contract to carry a specific cargo from a load port to a discharge port for an agreed freight per ton of cargo or a specified total amount. Under spot market voyage charters, we pay specific voyage expenses such as port, canal and bunker costs. Spot charter rates are volatile and fluctuate on a seasonal and year-to-year basis.

Fluctuations derive from imbalances in the availability of cargoes for shipment and the number of vessels available at any given time to transport these cargoes. Vessels operating in the spot market generate revenue that is less predictable, but may enable us to capture increased profit margins during periods of improvements in drybulk vessel charter rates.

Time Charters

Time charters give us a fixed and stable cash flow for a known period of time. Time charters also mitigate in part the seasonality of the spot market business, which is generally weaker in the second and third quarters of the year. In the future, we may opportunistically look to enter our vessels into time charter contracts should rates become more attractive. We may also enter into time charter contracts with profit sharing agreements, which enable us to benefit if the spot market increases.

Management of Our Business

Commercial and Technical Management

Our vessels are commercially managed by SCM and technically managed by SSM pursuant to a Master Agreement, which may be terminated by either party upon 24 months notice. SCM and SSM are companies affiliated with us. The vessels we charter-in are also commercially managed by SCM. We expect that additional vessels that we may acquire in the future, including the vessels in our Newbuilding Program, will also be managed under the Master Agreement or on substantially similar terms.

SCM s services include securing employment for our vessels in the spot market and on time charters. SCM also manages the Scorpio Group Pools in which our vessels are, or are expected to be, employed. For commercial management of any of our vessels that does not operate in one of these pools, we pay SCM a daily fee of $300 per vessel, plus a 1.75% commission on the gross revenues per charter fixture. The Scorpio Group Pool

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participants, including us and third-party owners of similar vessels, are each expected to pay SCM a pool management fee of $300 per vessel per day, plus a 1.75% commission on the gross revenues per charter fixture.

SSM s services include providing technical support, such as arranging the hiring of qualified officers and crew, supervising the maintenance and performance of vessels, purchasing supplies, spare parts and new equipment, arranging and supervising drydocking and repairs, and monitoring regulatory and classification society compliance and customer standards. We will pay SSM an annual fee of $200,000 per vessel to provide technical management services for each of our vessels in the Newbuilding Program upon delivery. In addition, representatives of SSM, including certain subcontractors, provide us with construction supervisory services while our vessels are being constructed in shipyards. For these services, we compensate SSM for its direct expenses, which can vary between $200,000 and $500,000 per vessel. Please see Certain Relationships and Related Party Transactions Commercial and Technical Management Agreements for additional information.

Administrative Services Agreement

We have entered into an Administrative Services Agreement with SSH for the provision of administrative staff, office space and accounting, legal compliance, financial and information technology services. SSH is a company affiliated with us. SSH also arranges acquisitions for us. The services provided to us by SSH may be sub-contracted to other entities within the Scorpio Group. Pursuant to the Administrative Services Agreement, we will reimburse SSH for the reasonable direct or indirect expenses it incurs in providing us with the administrative services described above and a pro-rata portion of the salary incurred by SSH for an internal auditor. We will also pay SSH a fee for arranging vessel acquisitions, including newbuildings, equal to $250,000 per vessel, due upon delivery of the vessel, which is payable in our common shares. We have agreed to issue upon delivery of each vessel in our Newbuilding Program (i) 31,250 common shares to SSH as payment related to each of the first 17 vessels in our Newbuilding Program; (ii) 25,811 common shares to SSH as payment related to each of the next nine vessels in our Newbuilding Program; (iii) 25,633 common shares to SSH as payment related to each of the next ten vessels in our Newbuilding Program; (iv) 26,419 common shares to SSH as payment related to each of the next four Kamsarmax vessels in our Newbuilding Program; (v) 26,185 common shares to SSH as payment related to each of the next three Capesize vessels in our Newbuilding Program; (vi) 26,197 common shares to SSH as payment related to each of the next two vessels in our Newbuilding Program; (vii) 26,394 common shares to SSH as payment related to each of the next seven vessels in our Newbuilding Program; (viii) 26,248 common shares to SSH as payment related to each of the next four vessels in our Newbuilding Program; (ix) 26,111 common shares to SSH as payment related to each of the next four vessels in our Newbuilding Program; (x) 26,050 common shares to SSH as payment related to each of the next three vessels in our Newbuilding Program; (xi) 25,888 common shares to SSH as payment related to each of the next 11 vessels in our Newbuilding Program; (xii) 25,497 common shares to SSH as payment related to each of the next five vessels in our Newbuilding Program and (xiii) 27,640 common shares to SSH as payment related to the next vessel in our Newbuilding Program. For all vessels added to our Newbuilding Program after the first 17 vessels, the number of common shares issuable to SSH as payment is based on the market value of our common shares based on the volume weighted average price of our common shares over the 30 trading day period immediately preceding the contract date of a definitive agreement to acquire any vessel. In addition, SSH has agreed with us not to own any drybulk carriers greater than 30,000 dwt for so long as the Administrative Services Agreement is in full force and effect. This agreement may be terminated by SSH three years following the third anniversary of our initial public offering upon 12 months notice.

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Our Competitive Strengths

We believe that we possess a number of competitive strengths in our industry, including:

Experienced management teams. Our Company s leadership has considerable depth of shipping industry expertise. Since 2003, under the leadership of Mr. Emanuele Lauro, our Co-Founder, Chairman and Chief Executive Officer, the Scorpio Group, together with Scorpio Tankers, has grown from an owner of three vessels in 2003 to an owner of 75 vessels, and an operator or manager of approximately 100 vessels, as of August 28, 2014. Mr. Robert Bugbee, our Co-Founder, President and Director, also holds a senior management position within the Scorpio Group and is the President and a Director of Scorpio Tankers, has more than 27 years of experience in the shipping industry and was formerly the President and Chief Operating Officer of OMI, which was a publicly traded shipping company until its sale in 2007. Messrs. Lauro and Bugbee are supported by Mr. Cameron Mackey, Mr. Hugh Baker and Mr. Luca Forgione, who serve as our Chief Operating Officer, our Chief Financial Officer, and our General Counsel, respectively, of whom, Messrs. Mackey and Forgione also serve as members of the management team of Scorpio Tankers. Mr. Mackey is also a director of Scorpio Tankers. Messrs. Mackey, Baker and Forgione serve in similar positions in the Scorpio Group and have 20, 22 and 11 years of experience, respectively, in the shipping industry, and, with Messrs. Lauro and Bugbee, collectively have over 80 years of combined shipping experience, and have developed industry relationships with charterers, lenders, shipbuilders, insurers and other industry participants. In addition, our Chief Executive Officer has experience in the ownership and operation of dry bulk carriers, through the Scorpio Group, which has owned and operated several dry bulk carriers, and in the upstream and downstream supply chain of dry bulk commodities, as founder, Chief Executive Officer and Chairman of Scorpio Logistics Ltd. Our executive officers are not required to work full-time on our affairs and also perform services for other companies, including Scorpio Tankers. Initially, we expect that our executive officers will devote a substantial portion of their business time to the completion of our drybulk carrier acquisition program and management of the Company.

Attractive Fleet. The 79 drybulk carriers in our Newbuilding Program, including 29 Ultramax vessels, 22 Kamsarmax vessels and 28 Capesize vessels, are scheduled to be delivered to us between the third quarter of 2014 and the third quarter of 2016. In addition, we own one Kamsarmax vessel that was recently delivered to us from the shipyard. We believe that owning a modern, well-maintained fleet with fuel efficient specifications reduces operating costs, improves the quality of service we deliver and provides us with a competitive advantage in securing favorable time and spot charters with high-quality counterparties. We believe that it is an opportune time to acquire these latest generation, fuel-efficient drybulk vessels because acquisition costs for these vessels are currently near the lowest average levels of the past 10 years. In addition, we believe that recent advances in shipbuilding design and technology should make these latest generation vessels more fuel-efficient than older vessels in the global fleet that compete with us for charters, providing us with a competitive advantage.

Significant available liquidity to pursue acquisition and expansion opportunities. Following the completion of this offering, we expect to have at least $ million of available cash, including $346.0 million which is a portion of the net proceeds from the Equity Private Placements and our Initial Public Offering. We intend to use the substantial majority of our available cash, and borrowing capacity under the secured credit facilities we intend to enter, to pursue vessel acquisitions, including the vessels in our Newbuilding Program, consistent with our business strategy. We believe that our strong balance sheet, financing capacity and future access to capital will allow us to make opportunistic acquisitions at attractive prices.

Access to attractive acquisition and chartering opportunities. Scorpio Group, including Scorpio Tankers, has established strong global relationships with shipping companies, charterers, shipyards, brokers and commercial shipping lenders. We believe that the Scorpio Group s relationships with these counterparties and its strong sale and purchase track record and reputation as a creditworthy counterparty should provide us, as a member of the Scorpio

Group, with access to attractive asset acquisitions, chartering and vessel financing opportunities.

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High quality, cost efficient vessel opportunities. We believe that Scorpio Group s experience with the commercial and technical management of vessels and its reputation in the industry as an operator with high safety and quality operating standards will be important in establishing and retaining high quality charterers that are looking for reliable and responsible operators to meet their exacting standards for vessel chartering and day-to-day operation.

Our Business Strategies

Our primary objectives are to profitably grow our business and emerge as a successful owner and operator of drybulk vessels. The key elements of our strategy are:

Expanding our fleet through opportunistic acquisitions of high-quality vessels at attractive prices. We intend to acquire latest generation drybulk carriers with fuel-efficient specifications and carrying capacities of greater than 30,000 dwt through timely and selective acquisitions. We currently view this vessel class as providing attractive return characteristics given the relatively low vessel price levels. A key element to our acquisition strategy will be to acquire high-quality vessels at attractive prices. When evaluating acquisitions, we will consider and analyze, among other things, our expectation of fundamental developments in the drybulk shipping industry sector, the level of liquidity in the resale and charter market, the cash flow earned by the vessel in relation to its value, its condition and technical specifications with particular regard to fuel consumption, expected remaining useful life, the credit quality of the charterer and duration and terms of charter contracts for vessels acquired with charters attached, as well as the overall diversification of our fleet and customers. We believe that these circumstances combined with our management s knowledge of the shipping industry present an opportunity for us to grow our fleet at favorable prices.

Optimizing vessel revenues primarily through spot market exposure. The Baltic Dry Index, or the BDI, a daily average of charter rates for key drybulk routes published by the Baltic Exchange Limited, which has long been viewed as the main benchmark to monitor the movements of the drybulk vessel charter market and the performance of the entire drybulk shipping market, has recently increased from the record low levels of 647 in February 2012 to 755 on July 31, 2014. We intend to employ a chartering strategy to capture upside opportunities in the spot market. We may also use fixed-rate time charters as the charter market improves to reduce downside risks. There can be no assurance that the drybulk charter market will increase and the market could decline.

Focusing on drybulk carriers based on the experience and expertise of the Scorpio Group and our management team in the international shipping industry. We believe that major international commodity companies seek transportation partners that are financially stable and have a reputation for reliability, safety, and high environmental and quality standards. We intend to leverage the operational expertise and customer base of the Scorpio Group and the members of our management team in order to further expand these relationships with consistent delivery of superior customer service.

Minimizing operating and corporate expenses. Pursuant to the Master Agreement, SSM and SCM coordinates and oversees the technical and commercial management of our fleet, respectively. We believe that SSM and SCM will be able to provide these services at costs that are lower than what we could achieve by performing these functions in-house.

Maintain a strong balance sheet through moderate use of leverage. We plan to finance the remaining contractual commitments due under our Newbuilding Program and future vessel acquisitions with a mix of debt and equity, but intend to maintain moderate levels of leverage over time, even though we may have the capacity to obtain additional financing. By maintaining moderate levels of leverage of not more than 60% of the value of the vessels collateralizing our indebtedness, we expect to retain greater flexibility than our more leveraged competitors to operate our vessels under shorter spot or period charters. Charterers have increasingly favored

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financially solid vessel owners, and we believe that our expected balance sheet strength will enable us to access more favorable chartering opportunities, as well as give us a competitive advantage in pursuing vessel acquisitions from commercial banks and shipyards, which have also recently displayed a preference for contracting with well capitalized counterparties.

Recent Developments

On July 21, 2014, we received a commitment from two leading European financial institutions for a $540 million senior secured loan facility. The proceeds of this facility are expected to finance up to 55% of the contract price for 24 of the vessels in our Newbuilding Program (six Ultramax, nine Kamsarmax, and nine Capesize vessels) with expected deliveries in 2015 and 2016. This facility is expected to have a six year term with customary financial and restrictive covenants, and interest at LIBOR plus a margin. The closing of this loan facility, which is expected within 2014, is subject to usual and customary conditions precedent, including the negotiation and execution of final documentation. Please see Description of Other Indebtedness.

On July 29, 2014, we entered a $330.0 million senior secured credit facility with Credit Agricole Corporate and Investment Bank and Deutsche Bank AG London to fund a portion of the purchase price of 22 of the vessels in our Newbuilding Program. Please see Description of Other Indebtedness.

On July 30, 2014, we entered into a $67.5 million senior secured credit facility with NIBC Bank N.V. to fund a portion of the purchase price of four vessels in our Newbuilding Program. See Description of Other Indebtedness.

On July 31, 2014, we delisted our common shares from the Norwegian OTC List. Our common shares will continue to trade on the NYSE under the symbol SALT.

Risk Factors

We face a number of risks associated with our business and industry and must overcome a variety of challenges to utilize our strengths and implement our business strategies. These risks relate to, among others, changes in the international shipping industry, including supply and demand, charter hire rates, commodity prices, a downturn in the global economy, hazards inherent in our industry and operations resulting in liability for damage to or destruction of property and equipment, pollution or environmental damage, inability to comply with covenants in the credit facilities we may enter into, inability to finance capital projects, and inability to successfully employ our drybulk carriers.

You should carefully consider the following risks, those risks described in Risk Factors and the other information in this prospectus before deciding whether to invest in our Notes.

Implications of Being an Emerging Growth Company

We had less than $1.0 billion in revenue during our last fiscal year, which means that we qualify as an emerging growth company as defined in the Jumpstart Our Business Startups Act, or JOBS Act. An emerging growth company may take advantage of specified reduced reporting and other burdens that are otherwise applicable generally to public companies. These provisions include:

- the ability to present only two years of audited financial statements and only two years of related Management s Discussion and Analysis of Financial Condition and Results of Operations in the registration statement for our initial public offering;

- exemption from the auditor attestation requirement in the assessment of the emerging growth company s internal controls over financial reporting;

- exemption from new or revised financial accounting standards applicable to public companies until such standards are also applicable to private companies; and

- exemption from compliance with any new requirements adopted by the Public Company Accounting Oversight Board, or the PCAOB, requiring mandatory audit firm rotation or a supplement to our auditor s report in which the auditor would be required to provide additional information about the audit and our financial statements.

We may take advantage of these provisions until the end of the fiscal year following the fifth anniversary of our initial public offering or such earlier time that we are no longer an emerging growth company. We will cease to be an emerging growth company if we have more than $1.0 billion in total annual gross revenues during our most recently completed fiscal year, if we become a large accelerated filer with market capitalization of more than $700 million, or as of any date on which we have issued more than $1.0 billion in non-convertible debt over the three year period to such date. We will become a large accelerated filer as of December 31, 2014, and, as a result we will cease to be an emerging growth company. For as long as we qualify as an emerging growth company and take advantage of the reduced reporting obligations, the information that we provide shareholders may be different from information provided by other public companies. We are choosing to opt out of the extended transition period relating to the exemption from new or revised financial accounting standards and as a result, we will comply with new or revised accounting standards on the relevant dates on which adoption of such standards is required for non-emerging growth companies. Section 107 of the JOBS Act provides that our decision to opt out of the extended transition period for complying with new or revised accounting standards is irrevocable.

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Corporate Structure

The following diagram depicts our simplified organizational structure:

Corporate Information

Our principal executive offices are located at 9, Boulevard Charles III, MC 98000 Monaco. Our telephone number at that address is (011) 377 9798 5716. We expect to own our vessels through separate wholly-owned subsidiaries that will be incorporated in the Republic of the Marshall Islands, the Republic of Malta or other jurisdictions generally acceptable to lenders in the shipping industry. Our website is www.scorpiobulkers.com. The information contained in or connected to our website is not part of this prospectus.

Other Information

Because we are incorporated under the laws of the Republic of the Marshall Islands, you may encounter difficulty protecting your interests as shareholders, and your ability to protect your rights through the U.S. federal court system may be limited. Please refer to the sections entitled Risk Factors and Service of Process and Enforcement of Civil Liabilities for more information.

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THE OFFERING

The summary below describes the principal terms of the Notes. Certain of the terms and conditions described below are subject to important limitations and exceptions. See Description of Notes for a more detailed description of the terms and conditions of the Notes.

Issuer	Scorpio Bulkers Inc., a Marshall Islands corporation
Securities Offered	$ million aggregate principal amount (plus up to an additional $ million aggregate principal amount pursuant to an option granted to the underwriters) of our % Senior Notes due 2019 issued in minimum denominations of $25 and integral multiples of $25 in excess thereof.
Issue Date	, 2014
Maturity Date	The Notes will mature on , 2019.
Interest	The Notes will bear interest from the date of original issue until maturity at a rate of % per year, payable quarterly in arrears on March 15, June 15, September 15 and December 15, commencing on .
Use of Proceeds	We intend to use all or substantially all of the net proceeds of the sale of our Notes, which are expected to total approximately $ million after deducting underwriting discounts and commission and estimated offering expenses (or approximately $ million if the underwriters exercise their option to purchase additional Notes in full), to fund installment payments due under our Newbuilding Program, and the remaining amount, if any, for general corporate purposes and working capital. Please read Use of Proceeds.
Ranking	The Notes will be our senior unsecured obligations and will rank senior to any of our future subordinated debt and rank equally in right of payment with all of our existing and future senior unsecured debt. Our Notes will effectively rank junior to our existing and future secured debt, to the extent of the value of the assets securing such debt, as well as to existing and future debt of our subsidiaries. As of June 30, 2014, we had no outstanding indebtedness.
No Security or Guarantees	None of our obligations under our Notes will be secured by collateral or guaranteed by any of our subsidiaries, affiliates or any other persons.
Change of Control	Upon the occurrence of certain change of control events (as defined in the indenture governing the

Notes), you will have the right, as a holder of the Notes, to require us to repurchase some or all of your Notes at 101% of the principal amount, plus

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	accrued and unpaid interest to, but excluding, the repurchase date. For additional information, please read Description of Notes Change of Control Permits Holders to Require us to Purchase Notes.
Covenants	The indenture governing our Notes contains certain restrictive covenants, including covenants that require us to limit the amount of debt we incur, maintain a certain minimum net worth, and provide certain reports. These covenants are subject to important exceptions and qualifications. For additional information, please read Description of Notes.
Additional Notes	We may reopen our Notes at any time without the consent of the holders of our Notes and issue additional notes with the same terms as our Notes (except the issue price, issue date and initial interest payment date), which will thereafter constitute a single fungible series with our Notes, provided that if the additional notes are not fungible with our Notes for U.S. federal income tax purposes, such additional notes will have a separate CUSIP number.
Ratings	The Notes will not be rated by any nationally recognized statistical rating organization.
Listing	We have applied to list our Notes on the New York Stock Exchange, or NYSE under the symbol SLTB. If the application is approved, trading of our Notes on NYSE is expected to begin within 30 days after the original issue date of our Notes. The underwriters have advised us that they intend to make a market in our Notes prior to commencement of any trading on NYSE. However, the underwriters will have no obligation to do so, and no assurance can be given that a market for our Notes will develop prior to commencement of trading on NYSE or, if developed, will be maintained.
Form	Our Notes will be represented by one or more permanent global notes, which will be deposited with the trustee as custodian for The Depository Trust Company, or DTC, and registered in the name of a nominee designated by DTC. Holders of Notes may elect to hold interests in a global Note only in the manner described in this prospectus. Any such interest may not be exchanged for certificated securities except in limited circumstances described in this prospectus. For additional information, please read Description of Notes Book-entry System; Delivery and Form in this prospectus.

Additional Amounts; Tax Redemption	Any payments made by us with respect to the Notes will be made without withholding or deduction for or on account of taxes unless required by law. If we are required by law to withhold or deduct amounts for or on account of tax imposed by a taxing authority of a jurisdiction where we are a resident or certain other jurisdictions with respect to a payment to the holders of Notes, we will, subject to certain exceptions, pay the additional amounts necessary so that the net amount received by the holders of the Notes after the withholding or deduction is not less than the amount that they would have received in the absence of the withholding or deduction. See Description of Notes Additional Amounts.
	In the event of certain changes of law or official positions of certain taxing authorities that trigger requirements discussed immediately above that we pay additional amounts, we may redeem the Notes in whole, but not in part, at any time, upon not less than 30 nor more than 60 days notice at a redemption price of 100% of the principal amount, plus accrued and unpaid interest, if any, and additional amounts, if any, to, but excluding, the date of redemption. See Description of Notes Optional Redemption for Changes in Withholding Taxes.
Settlement	Delivery of our Notes offered hereby will be made against payment therefor on or about , 2014.
Risk Factors	An investment in our Notes involves risks. You should consider carefully the factors set forth in the section of this prospectus entitled Risk Factors beginning on page 22 of this prospectus to determine whether an investment in our Notes is appropriate for you.

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SUMMARY CONSOLIDATED FINANCIAL AND OTHER DATA

We were formed on March 20, 2013 for the purpose of acquiring and operating the latest generation of newbuilding drybulk carriers with fuel-efficient specifications and carrying capacities of greater than 30,000 dwt in the international shipping markets. The following table summarizes our summary consolidated financial and other operating data at the dates and for the periods indicated.

Our summary consolidated financial and other data as of and for the six month period ended June 30, 2014 has been derived from our unaudited interim consolidated financial statements and related notes thereto, appearing elsewhere in this prospectus. Our summary consolidated financial data as of December 31, 2013 and for the period from March 20, 2013 (date of inception) to December 31, 2013 has been derived from our audited consolidated financial statements and related notes thereto, which are incorporated by reference herein. Our consolidated financial statements have been prepared in accordance with U.S. GAAP. The following financial data should be read in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations, and our consolidated financial statements and related notes included elsewhere in this prospectus.

	Six Months Ended June 30, 2014	Period from March 20, 2013 (date of inception) to December 31, 2013
	(Dollars in Thousands)	
Statement of Operations		
Revenue:		
Vessel revenue	$ 18,647	$ -
Operating expenses:		
Voyage expenses	3,180	-
Charterhire expenses	26,562	-
General and administrative expenses	15,351	5,505
Total operating expenses	45,093	5,505
Operating loss	(26,446)	(5,505)
Other income and (expense):		
Interest income	793	341
Foreign exchange loss	(5)	(1,135)
Other expense, net	-	(8)
Total other income and expense	788	(802)
Net loss	$ (25,658)	$ (6,307)

	As of June 30, 2014	As of December 31, 2013
	(Dollars in Thousands)	
Balance Sheet		

Cash and cash equivalents	$ 345,956	$ 733,896
Vessels under construction	842,845	371,692
Total assets	1,211,283	1,105,684
Current liabilities	79,091	1,472
Total liabilities	79,091	1,472
Shareholders equity	1,132,192	1,104,212

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	Six Months Ended June 30, 2014	Period from March 20, 2013 (date of inception) to December 31, 2013
	(Dollars in Thousands)	
Cash Flow		
Net cash inflow (outflow)		
Operating activities	$ (32,203)	$ (2,237)
Investing activities	(397,000)	(371,692)
Financing activities	41,263	1,107,825

(Dollars in Thousands, Except Per Day Data)	Six Months Ended June 30, 2014
Other Financial Data (1)	
Time Charter Equivalent Revenue (2):	
Vessel revenue	$ 18,647
Voyage expenses	3,180
Time charter equivalent revenue	$ 15,467
Time charter equivalent revenue attributable to:	
Kamsarmax	$ 12,027
Ultramax	3,440
	$ 15,467
Revenue days (2):	
Kamsarmax	1,560
Ultramax	335
Combined	1,895
TCE per revenue day (2):	
Kamsarmax	$ 7,712
Ultramax	$ 10,262
Combined	$ 8,163

(1) We had no revenue prior to 2014 and, accordingly, there are no other financial data for any period in 2013.

(2) We define Time Charter Equivalent (TCE) revenue as voyage revenues less voyage expenses. Such TCE revenue, divided by the number of our available days during the period, or revenue days, is TCE per revenue day, which is consistent with industry standards. TCE per revenue day is a common shipping industry performance measure used primarily to compare daily earnings generated by vessels on time charters with daily earnings generated by vessels on voyage charters, because charter hire rates for vessels on voyage charters are generally not expressed in per-day amounts while charter hire rates for vessels on time charters generally are expressed in such amounts.

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CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This prospectus includes forward-looking statements, as defined by U.S. federal securities laws, with respect to our financial condition, results of operations and business and our expectations or beliefs concerning future events. Words such as, but not limited to, believe, expect, anticipate, estimate, intend, plan, targets, projects, likely, could and similar expressions or phrases may identify forward-looking statements.

All forward-looking statements involve risks and uncertainties. The occurrence of the events described, and the achievement of the expected results, depend on many events, some or all of which are not predictable or within our control. Actual results may differ materially from expected results.

In addition, important factors that, in our view, could cause actual results to differ materially from those discussed in the forward-looking statements include:

- the strength of world economies;
- fluctuations in interest rates;
- general drybulk market conditions, including fluctuations in charter hire rates and vessel values;
- changes in demand in the drybulk shipping industry, including the market for our vessels;
- changes in our operating expenses, including bunker prices, dry docking and insurance costs;
- changes in governmental rules and regulations or actions taken by regulatory authorities;
- potential liability from pending or future litigation;
- general domestic and international political conditions;
- potential disruption of shipping routes due to accidents or political events;
- the availability of financing and refinancing;
- vessel breakdowns and instances of off-hire; and

other important factors described in Risk Factors beginning on page 22.

We have based these statements on assumptions and analyses formed by applying our experience and perception of historical trends, current conditions, expected future developments and other factors we believe are appropriate in the circumstances. All future written and verbal forward-looking statements attributable to us or any person acting on our behalf are expressly qualified in their entirety by the cautionary statements contained or referred to in this section. We undertake no obligation, and specifically decline any obligation, except as required by law, to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. In light of these risks, uncertainties and assumptions, the forward-looking events discussed in this prospectus might not occur.

See the sections entitled Risk Factors, beginning on page 22 of this prospectus for a more complete discussion of these risks and uncertainties and for other risks and uncertainties. These factors and the other risk factors described in this prospectus are not necessarily all of the important factors that could cause actual results or developments to differ materially from those expressed in any of our forward-looking statements. Other unknown or unpredictable factors also could harm our results. Consequently, there can be no assurance that actual results or developments anticipated by us will be realized or, even if substantially realized, that they will have the expected consequences to, or effects on, us. Given these uncertainties, prospective investors are cautioned not to place undue reliance on such forward-looking statements.

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RISK FACTORS

An investment in our Notes involves substantial risks. You should carefully consider the risks described below, as well as the other information included in this prospectus, before making an investment in our Notes. We operate in an intensely competitive industry. Some of the following risks relate principally to the industry in which we operate and our business in general. Other risks relate principally to the securities market, national and global economic conditions and the ownership of our Notes. The occurrence of any of the events described in this section could cause our results to differ materially from those contained in the forward-looking statements made in this prospectus, and could significantly and negatively affect our business, financial condition or operating results.

Risks of Investing in our Notes and Risks Related to our Other Indebtedness

Your investment in our Notes is subject to our credit risk.

Our Notes are unsubordinated unsecured general obligations of ours and are not, either directly or indirectly, an obligation of any third party. Our Notes will rank equally with all of our other unsecured and unsubordinated debt obligations, except as such obligations may be preferred by operation of law. Any payment to be made on our Notes, including the return of the principal amount at maturity or any redemption date, as applicable, depends on our ability to satisfy our obligations as they come due. As a result, our actual and perceived creditworthiness may affect the market value of our Notes and, in the event we were to default on our obligations, you may not receive the amounts owed to you under the terms of our Notes.

Our debt levels may limit our flexibility in obtaining additional financing and in pursuing other business opportunities.

As of June 30, 2014, we had no outstanding indebtedness. As of the same date, we received bank commitments for up to $977.1 million in aggregate proposed future borrowings, consisting of our $330.0 Million Senior Secured Credit Facility, our $67.5 Million Senior Secured Credit Facility, our $39.6 Million Senior Secured Credit Facility, and our Proposed $540.0 Million Senior Secured Credit Facility, which is subject to the negotiation and execution of final documentation. The amount of our outstanding borrowings under our debt facilities is expected to increase in connection with the completion of our acquisition of the 80 vessels in our Newbuilding Program that we have contracted to purchase. In addition, we may enter into other new debt arrangements or issue additional debt securities in the future. So long as our net borrowings do not equal or exceed 70% of our total assets, the indenture under which the Notes will be issued will permit us to incur additional indebtedness without limitation. Our level of debt could have important consequences to us, including the following:

- our ability to obtain additional financing, if necessary, for working capital, capital expenditures, acquisitions or other purposes may be impaired or such financing may not be available on favorable terms;

- we may need to use a substantial portion of our cash from operations to make charter hire payments or principal and interest payments relating to our debt obligations, reducing the funds that would otherwise be available for operations and future business opportunities;

- our debt level could make us more vulnerable than our competitors with less debt to competitive pressures or a downturn in our business or the economy generally; and

- our debt level may limit our flexibility in responding to changing business and economic conditions.

Our ability to service our debt and charter hire obligations will depend upon, among other things, our financial and operating performance, which will be affected by prevailing economic conditions and financial, business, regulatory and other factors, some of which are beyond our control. If our results of operations are not sufficient to service our current or future indebtedness and charter hire obligations, we will be forced to take actions such as reducing dividends, reducing or delaying our business activities, acquisitions, investments or capital expenditures, selling assets, restructuring or refinancing our debt, or seeking additional equity capital or bankruptcy protection. We may not be able to effect any of these remedies on satisfactory terms, or at all.

Our subsidiaries conduct the substantial majority of our operations and own our operating assets, and your right to receive payments on our Notes is structurally subordinated to the rights of the lenders of our subsidiaries.

Our subsidiaries conduct the substantial majority of our operations and own our operating assets. As a result, our ability to make required payments on our Notes depends in part on the operations of our subsidiaries and our subsidiaries ability to distribute funds to us. To the extent our subsidiaries are unable to distribute, or are restricted from distributing, funds to us, we may be unable to fulfill our obligations under our Notes. Our subsidiaries are separate and distinct legal entities and have no obligation, contingent or otherwise, to pay amounts due on our Notes or to make funds available for that purpose. Our Notes will not be guaranteed by any of our subsidiaries or any other person.

The rights of holders of our Notes will be structurally subordinated to the rights of our subsidiaries lenders. A default by a subsidiary under its debt obligations would result in a block on distributions from the affected subsidiary to us. Our Notes will be effectively junior to all existing and future liabilities of our subsidiaries. In the event of a bankruptcy, liquidation or reorganization of any of our subsidiaries, creditors of our subsidiaries will generally be entitled to payment of their claims from the assets of those subsidiaries before any assets are made available for distribution to us. As of June 30, 2014, we had no outstanding indebtedness and vessels under construction with a net book value of $842.8 billion. In addition, the indenture under which our Notes will be issued will permit our subsidiaries to incur additional debt without any limitation.

Our Notes will be unsecured obligations and will be effectively subordinated to our secured debt.

Our Notes are unsecured and therefore will be effectively subordinated to any secured debt we maintain or may incur to the extent of the value of the assets securing the debt. In the event of a bankruptcy or similar proceeding involving us, the assets that serve as collateral will be available to satisfy the obligations under any secured debt before any payments are made on our Notes. As of June 30, 2014, we had no outstanding indebtedness. As of the same date, we received bank commitments for up to $977.1 million in aggregate proposed future borrowings (all of which will be secured indebtedness), consisting of our $330.0 Million Senior Secured Credit Facility, $67.5 Million Senior Secured Credit Facility, $39.6 Million Senior Secured Credit Facility as well as our Proposed $540.0 Million Senior Secured Credit Facility, which is subject to credit approval, satisfaction of conditions precedent, and the negotiation and execution of final documentation. Please read Description of Other Indebtedness. We will continue to have the ability to incur, and intend to incur, significant additional secured debt, subject to limitations in our credit facilities and the indenture relating to our Notes.

We may not have the ability to raise the funds necessary to purchase our Notes as required upon a change of control, and our existing and future debt may contain limitations on our ability to purchase our Notes.

Following a change of control as described under Description of Notes Change of Control Permits Holders to Require us to Purchase Notes, holders of Notes will have the right to require us to purchase their Notes for cash. A change of control may also constitute an event of default or prepayment under, and result in the acceleration of the maturity of, our then existing indebtedness. We cannot assure you that we will have sufficient financial resources, or will be able to arrange financing, to pay the change of control purchase price in cash with respect to any Notes surrendered by holders for purchase upon a change of control. In addition, restrictions in our then existing credit facilities or other indebtedness, if any, may not allow us to purchase the Notes upon a change of control. Our failure to purchase the Notes upon a change of control when required would result in an event of default with respect to the Notes which could, in turn, constitute a default under the terms of our other indebtedness, if any. If the repayment of the related indebtedness were to be accelerated after any applicable notice or grace periods, we may not have sufficient funds to repay the indebtedness and purchase the Notes.

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Some significant restructuring transactions may not constitute a change of control, in which case we would not be obligated to offer to purchase the Notes.

Upon the occurrence of a change of control, you have the right to require us to purchase your Notes. However, the change of control provisions will not afford protection to holders of Notes in the event of certain transactions that could adversely affect the Notes. For example, transactions such as leveraged recapitalizations, refinancings or certain restructurings would not constitute a change of control requiring us to repurchase the Notes. In the event of any such transaction, holders of the Notes would not have the right to require us to purchase their Notes, even though each of these transactions could increase the amount of our indebtedness, or otherwise adversely affect our capital structure or any credit ratings, thereby adversely affecting holders of the Notes.

Our Notes do not have an established trading market, which may negatively affect their market value and your ability to transfer or sell your Notes.

Our Notes are a new issuance of securities with no established trading market. We have applied to list our Notes on the NYSE, but there can be no assurance that the NYSE will accept our Notes for listing. Even if our Notes are approved for listing by the NYSE, an active trading market on the NYSE for our Notes may not develop or, even if it develops, may not last, in which case the trading price of our Notes could be adversely affected and your ability to transfer your Notes will be limited. If an active trading market does develop on the NYSE, our Notes may trade at prices lower than the offering price. The trading price of our Notes will depend on many factors, including:

- prevailing interest rates;
- the market for similar securities;
- general economic and financial market conditions;
- our issuance of debt or preferred equity securities; and
- our financial condition, results of operations and prospects.

We have been advised by the underwriters that they intend to make a market in our Notes pending any listing of the Notes on the NYSE, but they are not obligated to do so and may discontinue market-making at any time without notice.

Our Notes have not been rated, and ratings of any of our other securities may affect the trading price of our Notes.

We have not sought to obtain a rating for our Notes, and our Notes may never be rated. It is possible, however, that one or more credit rating agencies might independently determine to assign a rating to our Notes or that we may elect to obtain a rating of our Notes in the future. In addition, we may elect to issue other securities for which we may seek to obtain a rating. If any ratings are assigned to our Notes in the future or if we issue other securities with a rating, such ratings, if they are lower than market expectations or are subsequently lowered or withdrawn, or if ratings for such other securities would imply a lower relative value for our Notes, could adversely affect the market for, or the market value of, our Notes. Ratings only reflect the views of the issuing rating agency or agencies and such ratings could at any time be revised downward or withdrawn entirely at the discretion of the issuing rating agency. A rating is not a recommendation to purchase, sell or hold any particular security, including our Notes. Ratings do not reflect market prices or suitability of a security for a particular investor and any future rating of our Notes may not reflect all risks related to us and our business, or the structure or market value of our Notes.

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Our management will have broad discretion over the use of the proceeds to us from this offering and might not apply the proceeds of this offering in ways that increase the value of your investment.

Our management will have broad discretion to use the net proceeds from this offering, and you will be relying on the judgment of our management regarding the application of these proceeds. They may not apply the net proceeds of this offering in ways that increase the value of your investment. Our management might not be able to yield a significant return, if any, on any investment of these net proceeds. We currently expect to use all or substantially all of the net proceeds from this offering to fund installment payments due under our Newbuilding Program, and the remaining amount, if any, for general corporate purposes and working capital. Please read Use of Proceeds.

Servicing our current or future indebtedness limits funds available for other purposes and if we cannot service our debt, we may lose our vessels.

Borrowing under our credit facilities requires us to dedicate a part of our cash flow from operations to paying interest on our indebtedness under such facilities. These payments limit funds available for working capital, capital expenditures and other purposes, including further equity or debt financing in the future. Amounts borrowed under our credit facilities bear interest at variable rates. Increases in prevailing rates could increase the amounts that we would have to pay to our lenders, even though the outstanding principal amount remains the same, and our net income and cash flows would decrease. We expect our earnings and cash flow to vary from year to year due to the cyclical nature of the drybulk industry. If we do not generate or reserve enough cash flow from operations to satisfy our debt obligations, we may have to undertake alternative financing plans, such as:

- seeking to raise additional capital;
- refinancing or restructuring our debt;
- selling vessels; or
- reducing or delaying capital investments.

However, these alternative financing plans, if necessary, may not be sufficient to allow us to meet our debt obligations. If we are unable to meet our debt obligations or if some other default occurs under our credit facilities, our lenders could elect to declare that debt, together with accrued interest and fees, to be immediately due and payable and proceed against the collateral vessels securing that debt even though the majority of the proceeds used to purchase the collateral vessels did not come from our credit facilities.

Our credit facilities contain restrictive covenants which limit the amount of cash that we may use for other corporate activities, which could negatively affect our growth and cause our financial performance to suffer.

Our credit facilities may impose operating and financial restrictions on us that limit our ability, or the ability of our subsidiaries party thereto, to:

pay dividends and make capital expenditures if we do not repay amounts drawn under our credit facilities or if there is another default under our credit facilities;

incur additional indebtedness, including the issuance of guarantees;

create liens on our assets;

change the flag, class or management of our vessels or terminate or materially amend the management agreement relating to each vessel;

sell our vessels;

merge or consolidate with, or transfer all or substantially all our assets to, another person; or

enter into a new line of business.

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Therefore, we may need to seek permission from our lenders in order to engage in some corporate actions. Our lenders interests may be different from ours and we may not be able to obtain our lenders permission when needed. This may limit our ability to pay dividends on our common shares, if we determine to do so in the future, and interest on our Notes, finance our future operations or capital requirements, make acquisitions or pursue business opportunities.

In addition, our secured credit facilities, including our $330.0 Million Senior Secured Credit Facility, our $67.5 Million Senior Secured Credit Facility, our $39.6 Million Senior Secured Credit Facility requires, and our Proposed $540.0 Million Senior Secured Credit Facility require, or is expected to require, us to maintain specified financial ratios and satisfy financial covenants, including ratios and covenants based on the market value of the vessels in our fleet. Should our charter rates or vessel values materially decline in the future, we may be required to take action to reduce our debt or to act in a manner contrary to our business objectives to meet any such financial ratios and satisfy any such financial covenants. Events beyond our control, including changes in the economic and business conditions in the shipping markets in which we operate, may affect our ability to comply with these covenants. We cannot assure you that we will meet these ratios or satisfy these covenants or that our lenders will waive any failure to do so. A breach of any of the covenants in, or our inability to maintain the required financial ratios under, our credit facilities would prevent us from borrowing additional money under our credit facilities and could result in a default under our credit facilities. If a default occurs under our credit facilities, the lenders could elect to declare the outstanding debt, together with accrued interest and other fees, to be immediately due and payable and foreclose on the collateral securing that debt, which could constitute all or substantially all of our assets. Please see Description of Other Indebtedness.

Servicing our current or future indebtedness limits funds available for other purposes and if we cannot service our debt, we may lose our vessels.

Borrowing under credit facilities requires us to dedicate a part of our cash flow from operations to paying interest on our indebtedness. These payments limit funds available for working capital, capital expenditures and other purposes, including further equity or debt financing in the future. Amounts borrowed under our credit facilities will bear interest at variable rates. Increases in prevailing rates could increase the amounts that we would have to pay to our lenders, even though the outstanding principal amount remains the same, and our net income and cash flows would decrease. We expect our earnings and cash flow to vary from year to year due to the cyclical nature of the drybulk carrier industry. If we do not generate or reserve enough cash flow from operations to satisfy our debt obligations, we may have to undertake alternative financing plans, such as:

- seeking to raise additional capital;
- refinancing or restructuring our debt;
- selling drybulk carriers; or
- reducing or delaying capital investments.

However, these alternative financing plans, if necessary, may not be sufficient to allow us to meet our debt obligations. If we are unable to meet our debt obligations or if some other default occurs under the credit facilities that we intend to enter, our lenders could elect to declare that debt, together with accrued interest and fees, to be immediately due and payable and proceed against the collateral vessels securing that debt.

We expect to be exposed to volatility in the London Interbank Offered Rate, or LIBOR, and intend to selectively enter into derivative contracts, which can result in higher than market interest rates and charges against our income.

We expect the loans under our secured credit facilities to be generally advanced at a floating interest rate based on LIBOR, which has been stable, but was volatile in prior years, which can affect the amount of interest payable on our debt, and which, in turn, could have an adverse effect on our earnings and cash flow. In addition, in recent years, LIBOR has been at relatively low levels, and may rise in the future as the current low interest rate

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environment comes to an end. Our financial condition could be materially adversely affected at any time that we have not entered into interest rate hedging arrangements to hedge our exposure to the interest rates applicable to our credit facilities and any other financing arrangements we may enter into in the future, including those we enter into to finance a portion of the amounts payable with respect to newbuildings. Moreover, even if we have entered into interest rate swaps or other derivative instruments for purposes of managing our interest rate exposure, our hedging strategies may not be effective and we may incur substantial losses.

We intend to selectively enter into derivative contracts to hedge our overall exposure to interest rate risk exposure. Entering into swaps and derivatives transactions is inherently risky and presents various possibilities for incurring significant expenses. The derivatives strategies that we employ in the future may not be successful or effective, and we could, as a result, incur substantial additional interest costs. See Management s Discussion and Analysis of Financial Condition and Results of Operations for a description of our expected interest rate swap arrangements.

Industry Specific Risk Factors

Charter hire rates for drybulk vessels are volatile and have declined significantly since their historic highs and may remain at low levels or decrease in the future, which may adversely affect our earnings, revenue and profitability and our ability to comply with our loan covenants.

The drybulk shipping industry is cyclical with high volatility in charter hire rates and profitability. The degree of charter hire rate volatility among different types of drybulk vessels has varied widely; however, the continued downturn in the drybulk charter market has severely affected the entire drybulk shipping industry and charter hire rates for drybulk vessels have declined significantly from historically high levels. The Baltic Dry Index, or the BDI, a daily average of charter rates for key drybulk routes published by the Baltic Exchange Limited, which has long been viewed as the main benchmark to monitor the movements of the drybulk vessel charter market and the performance of the entire drybulk shipping market, declined 94% in 2008 from a peak of 11,793 in May 2008 to a low of 663 in December 2008 and has remained volatile since then. The BDI recorded a record low of 647 in February 2012. During 2013, the BDI remained volatile, ranging from a low of 698 in January to a high of 2,337 in December, before ending the year at 2,277. The BDI has since decreased to 755 as of July 31, 2014.

Fluctuations in charter rates result from changes in the supply of and demand for vessel capacity and changes in the supply of and demand for the major commodities carried by water internationally. Because the factors affecting the supply of and demand for vessels are outside of our control and are unpredictable, the nature, timing, direction and degree of changes in industry conditions are also unpredictable. Since we intend to charter all our vessels principally in the spot market we will be exposed to the cyclicality and volatility of the spot market. We may be unable to keep our vessels fully employed in these short-term markets or charter rates available in the spot market may be insufficient to enable our vessels to be operated profitably. A significant decrease in charter rates would affect asset values and adversely affect our profitability, cash flows and ability to pay dividends, if any, in the future, on our common shares, and interest on our Notes.

Factors that influence demand for drybulk vessel capacity include:

- supply of and demand for energy resources, commodities and industrial products;

- changes in the exploration or production of energy resources, commodities, consumer and industrial products;

the location of regional and global exploration, production and manufacturing facilities;

the location of consuming regions for energy resources, commodities, consumer and industrial products;

the globalization of production and manufacturing;

global and regional economic and political conditions, including armed conflicts and terrorist activities; embargoes and strikes;

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- developments in international trade;
- changes in seaborne and other transportation patterns, including the distance cargo is transported by sea;
- environmental and other regulatory developments;
- currency exchange rates; and
- weather.

Factors that influence the supply of vessel capacity include:

- the number of newbuilding deliveries;
- port and canal congestion;
- the scrapping of older vessels;
- vessel casualties; and
- the number of vessels that are out of service, namely those that are laid-up, drydocked, awaiting repairs or otherwise not available for hire.

In addition to the prevailing and anticipated freight rates, factors that affect the rate of newbuilding, scrapping and laying-up include newbuilding prices, secondhand vessel values in relation to scrap prices, costs of bunkers and other operating costs, costs associated with classification society surveys, normal maintenance and insurance coverage, the efficiency and age profile of the existing drybulk fleet in the market and government and industry regulation of maritime transportation practices, particularly environmental protection laws and regulations. These factors influencing the supply of and demand for shipping capacity are outside of our control, and we may not be able to correctly assess the nature, timing and degree of changes in industry conditions.

We anticipate that the future demand for our drybulk vessels will be dependent upon economic growth in the world s economies, including China and India, seasonal and regional changes in demand, changes in the capacity of the global drybulk fleet and the sources and supply of drybulk cargo to be transported by sea. Given the number of new drybulk carriers currently on order with the shipyards, the capacity of the global drybulk carrier fleet seems likely to increase and there can be no assurance as to the timing or extent of future economic growth. Adverse economic, political, social or other developments could have a material adverse effect on our business and operating results.

Global economic conditions may continue to negatively impact the drybulk shipping industry.

In the current global economy, operating businesses have recently faced tightening credit, weakening demand for goods and services, weak international liquidity conditions, and declining markets. Lower demand for drybulk cargoes as well as diminished trade credit available for the delivery of such cargoes have led to decreased demand for drybulk carriers, creating downward pressure on charter rates and vessel values. The relatively weak global economic conditions have and may continue to have a number of adverse consequences for drybulk and other shipping sectors, including, among other things:

- low charter rates, particularly for vessels employed on short-term time charters or in the spot market;
- decreases in the market value of drybulk vessels and limited second-hand market for the sale of vessels;
- limited financing for vessels;
- widespread loan covenant defaults; and
- declaration of bankruptcy by certain vessel operators, vessel owners, shipyards and charterers.

The occurrence of one or more of these events could have a material adverse effect on our business, results of operations, cash flows and financial condition.

The current state of global financial markets and current economic conditions may adversely impact our ability to obtain financing or refinance our future credit facilities on acceptable terms, which may hinder or prevent us from operating or expanding our business.

Global financial markets and economic conditions have been, and continue to be, volatile. These issues, along with significant write-offs in the financial services sector, the re-pricing of credit risk and the current weak economic conditions, have made, and will likely continue to make, it difficult to obtain additional financing. The current state of global financial markets and current economic conditions might adversely impact our ability to issue additional equity at prices which will not be dilutive to our existing shareholders or preclude us from issuing equity at all.

Also, as a result of concerns about the stability of financial markets generally and the solvency of counterparties specifically, the cost of obtaining money from the credit markets has increased as many lenders have increased interest rates, enacted tighter lending standards, refused to refinance existing debt at all or on terms similar to current debt and reduced, and in some cases ceased, to provide funding to borrowers. Due to these factors, we cannot be certain that financing will be available to the extent required, or that we will be able to refinance our future credit facilities, on acceptable terms or at all. If financing or refinancing is not available when needed, or is available only on unfavorable terms, we may be unable to meet our obligations as they come due or we may be unable to enhance our existing business, complete the acquisition of our newbuildings and additional vessel acquisitions or otherwise take advantage of business opportunities as they arise.

If economic conditions throughout the world do not improve, it may impede our results of operations, financial condition and cash flows.

Negative trends in the global economy that emerged in 2008 continue to adversely affect global economic conditions. In addition, the world economy is currently facing a number of new challenges, recent turmoil and hostilities in the Ukraine, the Middle East, including Syria, North Korea, North Africa and other geographic areas and countries. The weakness in the global economy has caused, and may continue to cause, a decrease in worldwide demand for certain goods and, thus, shipping. Continuing economic instability could have a material adverse effect on our ability to implement our business strategy.

We face risks attendant to changes in economic environments, changes in interest rates, and instability in the banking and securities markets around the world, among other factors. Major market disruptions and the current adverse changes in market conditions and regulatory climate in the United States and worldwide may adversely affect our business or impair our ability to borrow amounts under credit facilities or any future financial arrangements. The recent and developing economic and governmental factors, together with the possible further declines in charter rates and vessel values, may have a material adverse effect on our results of operations, financial condition or cash flows.

Continued economic slowdown in the Asia Pacific region, particularly in China, may exacerbate the effect on us, as we anticipate a significant number of the port calls made by our vessels will continue to involve the loading or discharging of drybulk commodities in ports in the Asia Pacific region. Before the global economic financial crisis that began in 2008, China had one of the world s fastest growing economies in terms of gross domestic product, GDP, which had a significant impact on shipping demand. The growth rate of China s GDP is estimated to have remained stable year over year at approximately 7.7% for the year ended December 31, 2013 and continues to remain below pre-2008 levels. China has recently imposed measures to restrain lending, which may further contribute to a slowdown in its economic growth. It is possible that China and other countries in the Asia Pacific region will continue to experience slowed or even negative economic growth in the near future. Moreover, the current economic slowdown in the economies of the United States, the European Union and other Asian countries may further adversely affect economic growth in China and elsewhere. Our business, financial condition and results of operations, ability to pay dividends, if any, in the future, on our common shares, and interest on our Notes, as well as our future prospects, will likely be materially and adversely affected by a further economic downturn in any of these countries.

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The market values of our vessels may decline, which could limit the amount of funds that we can borrow, cause us to breach certain financial covenants in our future credit facilities, or result in an impairment charge, and we may incur a loss if we sell vessels following a decline in their market value.

The fair market values of drybulk vessels have generally experienced high volatility and have recently declined significantly. Although we believe that we have contracted to purchase the vessels in our Newbuilding Program, at attractive times in the cycle, the fair market value of our vessels may continue to fluctuate depending on a number of factors, including:

- prevailing level of charter rates;
- general economic and market conditions affecting the shipping industry;
- types, sizes and ages of vessels;
- supply of and demand for vessels;
- other modes of transportation;
- cost of newbuildings;
- governmental or other regulations;
- the need to upgrade vessels as a result of charterer requirements, technological advances in vessel design or equipment or otherwise; and
- technological advances.

If the fair market values of our vessels decline, the amount of funds we may draw down under our secured credit facilities may be limited and we may not be in compliance with certain covenants contained in those secured credit facilities, which may result in an event of default. In such circumstances, we may not be able to refinance our debt or obtain additional financing. If we are not able to comply with the covenants in our secured credit facilities, and are unable to remedy the relevant breach, our lenders could accelerate our debt and foreclose on our fleet. In addition, if we sell one or more of our vessels at a time when vessel prices have fallen and before we have recorded an impairment adjustment to our consolidated financial statements, the sale may be less than the vessel s carrying value on our consolidated financial statements, resulting in a loss and a reduction in earnings. Furthermore, if vessel values decline, we may have to record an impairment charge in our consolidated financial statements which could adversely affect our financial results.

Conversely, if vessel values are elevated at a time when we wish to acquire additional vessels, the cost of such acquisitions may increase and this could adversely affect our business, results of operations, cash flow and financial condition.

Please see Description of Other Indebtedness.

Compliance with safety and other vessel requirements imposed by classification societies may be very costly and may adversely affect our business.

The hull and machinery of every commercial vessel must be classed by a classification society authorized by its country of registry. The classification society certifies that a vessel is safe and seaworthy in accordance with the applicable rules and regulations of the country of registry of the vessel and the Safety of Life at Sea Convention.

A vessel must undergo annual surveys, intermediate surveys and special surveys. In lieu of a special survey, a vessel s machinery may be on a continuous survey cycle under which the machinery would be surveyed periodically over a five-year period. Every vessel is also required to be drydocked every two and a half to five years for inspection of its underwater parts.

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Compliance with the above requirements following the delivery of vessels may result in significant expense. If any vessel does not maintain its class or fails any annual, intermediate or special survey, the vessel will be unable to trade between ports and will be unemployable and uninsurable, which could negatively impact our results of operations and financial condition.

We are subject to complex laws and regulations, including environmental regulations that can adversely affect the cost, manner or feasibility of doing business.

Our operations are subject to numerous international, national, state and local laws, regulations, treaties and conventions in force in international waters and the jurisdictions in which our vessels operate or are registered, which can significantly affect the ownership and operation of our vessels. These laws and regulations include, but are not limited to, the U.S. Oil Pollution Act of 1990, or OPA, the Comprehensive Environmental Response, Compensation and Liability Act, or CERCLA, the U.S. Clean Air Act, the U.S. Clean Water Act and the U.S. Maritime Transportation Security Act of 2002, or the MTSA, and regulations of the International Maritime Organization, or IMO, including the International Convention for the Prevention of Pollution from Ships of 1973 (as from time to time amended and generally referred to as MARPOL), the International Convention for the Safety of Life at Sea of 1974 (as from time to time amended and generally referred to as SOLAS), the International Convention on Civil Liability for Bunker Oil Pollution Damage, and the International Convention on Load Lines of 1966 (as from time to time amended). Compliance with such laws, regulations and standards, where applicable, may require installation of costly equipment or implementation of operational changes and may affect the resale value or useful lives of our vessels. These costs could have a material adverse effect on our business, results of operations, cash flows and financial condition. A failure to comply with applicable laws and regulations may result in administrative and civil penalties, criminal sanctions or the suspension or termination of our operations. Because such conventions, laws, and regulations are often revised, we cannot predict the ultimate cost of complying with them or the impact thereof on the resale prices or useful lives of our vessels. Additional conventions, laws and regulations may be adopted which could limit our ability to do business or increase the cost of our doing business and which may materially adversely affect our operations.

Environmental laws often impose strict liability for remediation of spills and releases of oil and hazardous substances, which could subject us to liability without regard to whether we were negligent or at fault. Under OPA, for example, owners, operators and bareboat charterers are jointly and severally strictly liable for the discharge of oil within the 200-mile exclusive economic zone around the United States. Furthermore, the 2010 explosion of the Deepwater Horizon well and the subsequent release of oil into the Gulf of Mexico, or other similar events, may result in further regulation of the shipping industry, and modifications to statutory liability schemes, which could have a material adverse effect on our business, financial condition, results of operations and cash flows. An oil spill could result in significant liability, including fines, penalties and criminal liability and remediation costs for natural resource damages under other federal, state and local laws, as well as third-party damages.

We are required by various governmental and quasi-governmental agencies to obtain certain permits, licenses, and certificates with respect to our operations, and satisfy insurance and financial responsibility requirements for potential oil (including marine fuel) spills and other pollution incidents. Although we will, when available, arrange insurance to cover certain environmental risks, there can be no assurance that such insurance will be sufficient to cover all such risks or that any claims will not have a material adverse effect on our business, results of operations, cash flows and financial condition and our ability to pay dividends, if any, in the future, on our common shares, and interest on our Notes.

An over-supply of drybulk carrier capacity may prolong or further depress the current low charter rates, which may limit our ability to operate our drybulk carriers profitably.

The supply of drybulk vessels has increased significantly since the beginning of 2006. As of September 2013, newbuilding orders have been placed for approximately 15.7% of the existing fleet capacity. Vessel supply growth has been outpacing vessel demand growth over the past few years causing downward pressure on charter rates. Until the new supply is fully absorbed by the market, charter rates may continue to be under pressure due to vessel supply in the near to medium term. The Scorpio Group Pools in which our vessels operate, or are expected to operate, are spot market-oriented commercial pools managed by our commercial manager, which expose us to fluctuations in spot market charter rates.

World events could affect our results of operations and financial condition.

Past terrorist attacks, as well as the threat of future terrorist attacks around the world, continue to cause uncertainty in the world s financial markets and may affect our business, operating results and financial condition. Continuing conflicts and recent developments in Russia, Ukraine, the Korean Peninsula, the Middle East, including Egypt and North Africa, and the presence of U.S. or other armed forces in the Middle East, may lead to additional acts of terrorism and armed conflict around the world, which may contribute to further economic instability in the global financial markets. These uncertainties could also adversely affect our ability to obtain additional financing on terms acceptable to us or at all. In the past, political conflicts have also resulted in attacks on vessels, mining of waterways and other efforts to disrupt international shipping, particularly in the Arabian Gulf region. Acts of terrorism and piracy have also affected vessels trading in regions such as the South China Sea and the Gulf of Aden off the coast of Somalia. Any of these occurrences could have a material adverse impact on our operating results, revenues and costs.

Acts of piracy on ocean-going vessels have had and may continue to have an adverse effect on our business.

Acts of piracy have historically affected ocean-going vessels trading in regions of the world such as the South China Sea, the Indian Ocean and in the Gulf of Aden off the coast of Somalia. Although the frequency of sea piracy worldwide decreased during 2012 and 2013 to its lowest level since 2009, sea piracy incidents continue to occur, particularly in the Gulf of Aden off the coast of Somalia and increasingly in the Gulf of Guinea and the West Coast of Africa, with drybulk vessels particularly vulnerable to such attacks. If these piracy attacks result in regions in which our vessels are deployed being characterized as war risk zones by insurers, as the Gulf of Aden temporarily was in May 2008, or Joint War Committee war and strikes listed areas, premiums payable for such coverage could increase significantly and such insurance coverage may be more difficult to obtain. In addition, crew costs, including due to employing onboard security guards, could increase in such circumstances. Furthermore, while we believe the charterer remains liable for charter payments when a vessel is seized by pirates, the charterer may dispute this and withhold charter hire until the vessel is released. A charterer may also claim that a vessel seized by pirates was not on-hire for a certain number of days and is therefore entitled to cancel the charter party, a claim that we would dispute. We may not be adequately insured to cover losses from these incidents, which could have a material adverse effect on us. In addition, any detention hijacking as a result of an act of piracy against our vessels, or an increase in cost, or unavailability, of insurance for our vessels, could have a material adverse impact on our business, financial condition and results of operations.

Our vessels may call on ports located in countries that are subject to restrictions imposed by the U.S. or other governments, that could adversely affect our reputation.

Although we do not expect our vessels will call on ports located in countries subject to sanctions and embargoes imposed by the U.S. government and other authorities or countries identified by the U.S. government or other authorities as state sponsors of terrorism, such as Cuba, Iran, Sudan and Syria, from time to time on charterers instructions, our vessels may call on ports located in such countries in the future. The U.S. sanctions and embargo laws and regulations vary in their application, as they do not all apply to the same covered persons or proscribe the same activities, and such sanctions and embargo laws and regulations may be amended or strengthened over time. In 2010, the U.S. enacted the Comprehensive Iran Sanctions Accountability and Divestment Act, or CISADA, which amended the Iran Sanctions Act. Among other things, CISADA introduced limits on the ability of companies and persons to do business or trade with Iran when such activities relate to the investment, supply or export of refined petroleum or petroleum products. In 2012, President Obama signed Executive Order 13608 which prohibits foreign persons from violating or attempting to violate, or causing a violation of any sanctions in effect against Iran or facilitating any deceptive transactions for or on behalf of any person subject to U.S. sanctions. Any persons found to be in violation of Executive Order 13608 will be deemed a foreign sanctions evader and will be banned from all contacts with the United States, including conducting business in U.S. dollars. Also in 2012, President Obama signed into law the Iran Threat Reduction and Syria Human Rights Act of 2012, or the Iran Threat Reduction Act, which created new sanctions and strengthened existing sanctions. Among other things, the Iran Threat Reduction Act intensifies existing sanctions regarding the provision of goods, services, infrastructure or technology to Iran s petroleum or petrochemical sector. The Iran Threat Reduction Act also includes a provision requiring the President of the United States to impose five or more sanctions from Section 6(a) of the Iran Sanctions Act, as amended, on a person the President determines is a controlling beneficial owner of, or otherwise owns, operates, or controls or insures a vessel that was used to transport crude oil from Iran to another country and (1) if the person is a controlling beneficial owner of the vessel, the person had actual knowledge the vessel was so used or (2) if the person otherwise owns, operates, or controls, or insures the vessel, the person knew or should have known the vessel was so used. Such a person could be subject to a variety of sanctions, including exclusion from U.S. capital markets, exclusion from financial transactions subject to U.S. jurisdiction, and exclusion of that person s vessels from U.S. ports for up to two years.

On November 24, 2013, the P5+1 (the United States, United Kingdom, Germany, France, Russia and China) entered into an interim agreement with Iran entitled the Joint Plan of Action (JPOA). Under the JPOA it was agreed that, in exchange for Iran taking certain voluntary measures to ensure that its nuclear program is used only for peaceful purposes, the U.S. and EU would voluntarily suspend certain sanctions for a period of six months. On January 20, 2014, the U.S. and E.U. indicated that they would begin implementing the temporary relief measures provided for under the JPOA. These measures include, among other things, the suspension of certain sanctions on the Iranian petrochemicals, precious metals, and automotive industries from January 20, 2014 until July 20, 2014. The U.S. has since extended the JPOA until November 24, 2014. Although it is our intention to comply with the provisions of the JPOA, there can be no assurance that we will be in compliance in the future as such regulations and U.S. sanctions may be amended over time, and the U.S. retains the authority to revoke the aforementioned relief if Iran fails to meet its commitments under the JPOA.

Although we believe that we are in compliance with all applicable sanctions and embargo laws and regulations, and intend to maintain such compliance, there can be no assurance that we will be in compliance in the future, particularly as the scope of certain laws may be unclear and may be subject to changing interpretations. Any such violation could result in fines or other penalties and could severely impact our ability to access U.S. capital markets and conduct our business, and could result in some investors deciding, or being required, to divest their interest, or not to invest, in us. In addition, certain institutional investors may have investment policies or restrictions that prevent them from holding securities of companies that have contracts with countries identified by the U.S. government as state sponsors of terrorism. The determination by these investors not to invest in, or to divest from, our securities may adversely affect the price at which our securities trade. Moreover, our charterers may violate applicable sanctions and embargo laws and regulations as a result of actions that do not involve us or our vessels, and those violations could in turn negatively affect our reputation. In addition, our reputation and the market for our securities may be adversely affected if we engage in certain other activities, such as entering into charters with individuals or entities in countries subject to U.S. sanctions and embargo laws that are not controlled by the governments of those countries, or engaging in operations associated with those countries pursuant to contracts with third parties that are unrelated to those countries or entities controlled by their governments. Investor perception of the value of our securities may be adversely affected by the consequences of war, the effects of terrorism, civil unrest and governmental actions in these and surrounding countries.

Our operating results will be subject to seasonal fluctuations, which could affect our operating results.

We operate our vessels in markets that have historically exhibited seasonal variations in demand and, as a result, in charter hire rates. This seasonality may result in volatility in our operating results to the extent that we enter into new charter agreements or renew existing agreements during a time when charter rates are weaker or we operate our vessels on the spot market or index based time charters, which may result in quarter-to-quarter volatility in our operating results. The drybulk sector is typically stronger in the fall and winter months in anticipation of increased consumption of coal and other raw materials in the northern hemisphere. In addition, unpredictable weather patterns in these months tend to disrupt vessel scheduling and supplies of certain commodities. As a result, our revenues from our drybulk carriers may be weaker during the fiscal quarters ended June 30 and September 30, and, conversely, our revenues from our drybulk carriers may be stronger in fiscal quarters ended December 31 and March 31.

We are subject to international safety regulations and the failure to comply with these regulations may subject us to increased liability, may adversely affect our insurance coverage and may result in a denial of access to, or detention in, certain ports.

The operation of our vessels is affected by the requirements set forth in the ISM Code. The ISM Code requires ship owners, ship managers and bareboat charterers to develop and maintain an extensive Safety Management System that includes the adoption of a safety and environmental protection policy setting forth instructions and procedures for safe operation of vessels and describing procedures for dealing with emergencies. In addition, vessel classification societies impose significant safety and other requirements on our vessels.

The failure of a shipowner or bareboat charterer to comply with the ISM Code may subject it to increased liability, may invalidate existing insurance or decrease available insurance coverage for the affected vessels and may result in a denial of access to, or detention in, certain ports. Each of the vessels that we have agreed to acquire will be ISM Code-certified when delivered to us. However, if we are subject to increased liability for non-compliance or if our insurance coverage is adversely impacted as a result of non-compliance, it may negatively affect our ability to pay dividends, if any, in the future, on our common shares and interest on our Notes. If any of our vessels are denied access to, or are detained in, certain ports as a result of non-compliance with the ISM Code, our revenues may be adversely impacted.

Increased inspection procedures and tighter import and export controls could increase costs and disrupt our business.

International shipping is subject to various security and customs inspection and related procedures in countries of origin and destination and trans-shipment points. Inspection procedures may result in the seizure of contents of our vessels, delays in the loading, offloading, trans-shipment or delivery and the levying of customs duties, fines or other penalties against us.

It is possible that changes to inspection procedures could impose additional financial and legal obligations on us. Changes to inspection procedures could also impose additional costs and obligations on our customers and may, in certain cases, render the shipment of certain types of cargo uneconomical or impractical. Any such changes or developments may have a material adverse effect on our business, financial condition and results of operations.

The operation of drybulk carriers has certain unique operational risks which could affect our earnings and cash flow.

The operation of certain vessel types, such as drybulk carriers, has certain unique risks. With a drybulk carrier, the cargo itself and its interaction with the vessel can be an operational risk. By their nature, drybulk cargoes are often heavy, dense, easily shifted, and react badly to water exposure. In addition, drybulk carriers are often subjected to battering treatment during unloading operations with grabs, jackhammers (to pry encrusted cargoes out of the hold) and small bulldozers. This treatment may cause damage to the vessel. Vessels damaged due to treatment during unloading procedures may be more susceptible to breach at sea. Hull breaches in drybulk carriers may lead to the flooding of the vessels holds. If a drybulk carrier suffers flooding in its forward holds, the bulk cargo may become so dense and waterlogged that its pressure may buckle the vessel s bulkheads, leading to the loss of a vessel. If we are unable to adequately maintain our vessels, we may be unable to prevent these events. Any of these circumstances or events may have a material adverse effect on our business, results of operations, cash flows, financial condition and ability to pay dividends, if any, in the future, on our common shares and interest on our Notes. In addition, the loss of any of our vessels could harm our reputation as a safe and reliable vessel owner and operator.

Rising fuel, or bunker, prices may adversely affect our profits.

Since we primarily employ our vessels in the spot market or in spot market-oriented pools, we expect that fuel, or bunkers, will be typically the largest expense in our shipping operations for our vessels. While we believe that we will experience a competitive advantage as a result of increased bunker prices due to the greater fuel efficiency of our vessels compared to the average global fleet, changes in the price of fuel may adversely affect our profitability. The price and supply of fuel is unpredictable and fluctuates based on events outside our control, including geopolitical developments, supply and demand for oil and gas, actions by the Organization of the Petroleum Exporting Countries, or OPEC, and other oil and gas producers, war and unrest in oil producing countries and regions, regional production patterns and environmental concerns. Further, fuel may become much more expensive in the future, which may reduce our profitability.

Our business has inherent operational risks, which may not be adequately covered by insurance.

Our vessels and their cargoes are at risk of being damaged or lost because of events such as marine disasters, bad weather, mechanical failures, human error, environmental accidents, war, terrorism, piracy and other circumstances or events. In addition, transporting cargoes across a wide variety of international jurisdictions creates a risk of business interruptions due to political circumstances in foreign countries, hostilities, labor strikes and boycotts, the potential for changes in tax rates or policies, and the potential for government expropriation of our vessels. Any of these events may result in loss of revenues, increased costs and decreased cash flows to our customers, which could impair their ability to make payments to us under our charters.

In the event of a casualty to a vessel or other catastrophic event, we will rely on our insurance to pay the insured value of the vessel or the damages incurred. We procure insurance for the vessels in our fleet against those risks that we believe the shipping industry commonly insures against. These insurances include marine hull and machinery insurance, protection and indemnity insurance, which include pollution risks and crew insurances, and war risk insurance. Currently, the amount of coverage for liability for pollution, spillage and leakage available to us on commercially reasonable terms through protection and indemnity associations and providers of excess coverage is $1 billion per vessel per occurrence.

We will procure hull and machinery insurance, protection and indemnity insurance, which includes environmental damage and pollution insurance coverage and war risk insurance for our fleet. We do not maintain, for our vessels, insurance against loss of hire, which covers business interruptions that result from the loss of use of a vessel. We may not be adequately insured against all risks. We may not be able to obtain adequate insurance coverage for our fleet in the future, and we may not be able to obtain certain insurance coverages. The insurers may not pay particular claims. Our insurance policies may contain deductibles for which we will be responsible and limitations and exclusions which may increase our costs or lower our revenue. Moreover, insurers may default on claims they are required to pay.

We cannot assure you that we will be adequately insured against all risks or that we will be able to obtain adequate insurance coverage at reasonable rates for our vessels in the future. For example, in the past more stringent environmental regulations have led to increased costs for, and in the future may result in the lack of availability of, insurance against risks of environmental damage or pollution. Additionally, our insurers may refuse to pay particular claims. Any significant loss or liability for which we are not insured could have a material adverse effect on our financial condition.

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Maritime claimants could arrest one or more of our vessels, which could interrupt our cash flow.

Crew members, suppliers of goods and services to a vessel, shippers of cargo and other parties may be entitled to a maritime lien against a vessel for unsatisfied debts, claims or damages. In many jurisdictions, a claimant may seek to obtain security for its claim by arresting a vessel through foreclosure proceedings. The arrest or attachment of one or more of our vessels could interrupt our cash flow and require us to pay large sums of money to have the arrest or attachment lifted. In addition, in some jurisdictions, such as South Africa, under the sister ship theory of liability, a claimant may arrest both the vessel which is subject to the claimant s maritime lien and any associated vessel, which is any vessel owned or controlled by the same owner. Claimants could attempt to assert sister ship liability against one vessel in our fleet for claims relating to another of our vessels.

Governments could requisition our vessels during a period of war or emergency, resulting in a loss of earnings.

A government could requisition one or more of our vessels for title or for hire. Requisition for title occurs when a government takes control of a vessel and becomes her owner, while requisition for hire occurs when a government takes control of a vessel and effectively becomes her charterer at dictated charter rates. Generally, requisitions occur during periods of war or emergency, although governments may elect to requisition vessels in other circumstances. Although we would be entitled to compensation in the event of a requisition of one or more of our vessels, the amount and timing of payment would be uncertain. Government requisition of one or more of our vessels may negatively impact our revenues.

Failure to comply with the U.S. Foreign Corrupt Practices Act could result in fines, criminal penalties, charter terminations and an adverse effect on our business.

We may operate in a number of countries throughout the world, including countries known to have a reputation for corruption. We are committed to doing business in accordance with applicable anti-corruption laws and have adopted a code of business conduct and ethics which is consistent and in full compliance with the U.S. Foreign Corrupt Practices Act of 1977, or the FCPA. We are subject, however, to the risk that we, our affiliated entities or our or their respective officers, directors, employees and agents may take actions determined to be in violation of such anti-corruption laws, including the FCPA. Any such violation could result in substantial fines, sanctions, civil and/or criminal penalties and curtailment of operations in certain jurisdictions, and might adversely affect our business, results of operations or financial condition. In addition, actual or alleged violations could damage our reputation and ability to do business. Furthermore, detecting, investigating, and resolving actual or alleged violations is expensive and can consume significant time and attention of our senior management.

Company Specific Risk Factors

We are a recently formed company with a limited history of operations.

We are a recently formed company and have a limited performance record, operating history and historical financial statements upon which you can evaluate our operations or our ability to implement and achieve our business strategy. We cannot assure you that we will be successful in implementing our business strategy. In addition, while our Chief Executive Officer and the management teams of our commercial and technical managers have experience operating drybulk carriers, other members of our senior management, who have experience operating tanker and other classes of vessels, have limited experience operating drybulk carriers. We believe that the experience of our senior management in the ownership and operation of tanker vessels, which require significant technical expertise to operate and are subject to heightened regulatory oversight and more rigorous vetting procedures from charterers than drybulk carriers, provides our management team with the expertise and qualifications to manage drybulk carriers, however we cannot assure you that they will be able to successfully operate our fleet.

The Scorpio Group Pools in which our vessels operate, or are expected to operate, are or will be newly formed and will have limited or no prior operating history. We cannot assure you that these pools will be successful in finding employment for all of our vessels.

The Scorpio Group Pools in which our vessels operate, or are expected to operate, are or will be newly formed and will have limited or no prior operating history. We will own a large number of vessels that will enter these pools in a relatively short period of time without having previously secured employment. We cannot assure you that these pools will be successful in finding employment for all such vessels in the volatile spot market immediately upon their deliveries to us or whether any such employment will be at profitable rates. We cannot assure you that our vessels will be profitably operated by such pools. In addition, vessels owned by our affiliates, including members of the Scorpio Group, which includes Scorpio Ship Management S.A.M., or SSM, which provides us with vessel technical management services, Scorpio Commercial Management S.A.M., or SCM, which provides us with vessel commercial management services, and Scorpio Services Holding Limited, or SSH, which provides us and other related entities with administrative services and services related to the acquisition of vessels, as well as by unaffiliated third-parties, may participate in such pools. Such vessels may not be of the comparable design or quality to our vessels, negatively impacting the profitability of such pools, while diluting our interest in such profits.

Newbuilding projects are subject to risks that could cause delays, cost overruns or cancellation of our newbuilding contracts.

We have entered into shipbuilding contracts with established shipyards in Japan, China, South Korea and Romania for the construction of 79 newbuilding vessels for an aggregate purchase price of $3,070.8 million. These vessels are expected to be delivered to us between the third quarter of 2014 and the third quarter of 2016. These construction projects are subject to risks of delay or cost overruns inherent in any large construction project from numerous factors, including shortages of equipment, materials or skilled labor, unscheduled delays in the delivery of ordered materials and equipment or shipyard construction, failure of equipment to meet quality and/or performance standards, financial or operating difficulties experienced by equipment vendors or the shipyard, unanticipated actual or purported change orders, inability to obtain required permits or approvals, unanticipated cost increases between order and delivery, design or engineering changes and work stoppages and other labor disputes, adverse weather conditions or any other events of force majeure. Significant cost overruns or delays could adversely affect our financial position, results of operations and cash flows. Additionally, failure to complete a project on time may result in the delay of revenue from that vessel.

As of June 30, 2014, we had made total yard payments in the amount of $764.1 million and we have remaining yard installments in the amount of $2,338.8 million before we take possession of the vessels. We had, as of June 30, 2014, a cash balance of $346.0 million to fund future newbuilding commitments, however, a significant portion of our remaining commitments are currently unfunded. If we are not able to borrow additional funds, raise other capital or utilize available cash on hand, we may not be able to acquire these newbuilding vessels, which could have a material adverse effect on our business, financial condition, results of operations and cash flows. We have executed and signed loan documentation for our $330.0 Million Senior Secured Credit Facility that will be secured by 22 of the vessels in our Newbuilding Program, executed and signed loan documentation for our $39.6 Million Senior Secured Credit Facility that will be secured by two of the vessels in our Newbuilding Program, executed and signed loan documentation for our $67.5 Million Senior Secured Credit Facility that will be secured by four of the vessels in our Newbuilding Program, and received a commitment letter for our $540.0 Million Senior Secured Credit Facility that will be secured by 24 vessels in our Newbuilding Program, however, such credit facilities are subject to important conditions, including the negotiation and execution of definitive documentation. We cannot assure you that we will be able to enter into either such proposed senior secured credit facility. If for any reason we fail to make a payment when due, which may result in a default under our newbuilding contracts, or otherwise fail to take delivery of our newbuild vessels, we would be prevented from realizing potential revenues from these vessels, we could also lose all or a portion of our yard payments that were paid by us and we could be liable for penalties and damages under such contracts.

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In addition, in the event the shipyards do not perform under their contracts and we are unable to enforce certain refund guarantees with third party banks for any reason, we may lose all or part of our investment, which would have a material adverse effect on our results of operations, financial condition and cash flows.

We are subject to certain risks with respect to our counterparties on contracts, and failure of such counterparties to meet their obligations could cause us to suffer losses or negatively impact our results of operations and cash flows.

We have entered into, and may enter into the future, various contracts, including pooling arrangements, charter agreements, shipbuilding contracts and credit facilities. Such agreements subject us to counterparty risks. The ability of each of our counterparties to perform its obligations under a contract with us will depend on a number of factors that are beyond our control and may include, among other things, general economic conditions, the condition of the maritime and offshore industries, the overall financial condition of the counterparty, charter rates received for specific types of vessels, and various expenses. For example, the combination of a reduction of cash flow resulting from declines in world trade, a reduction in borrowing bases under reserve-based credit facilities and the lack of availability of debt or equity financing may result in a significant reduction in the ability of our charterers to make charter payments to us. In addition, in depressed market conditions, our charterers and customers may no longer need a vessel that is then under charter or contract or may be able to obtain a comparable vessel at lower rates. As a result, charterers and customers may seek to renegotiate the terms of their existing charter agreements or avoid their obligations under those contracts. Should a counterparty fail to honor its obligations under agreements with us, we could sustain significant losses which could have a material adverse effect on our business, financial condition, results of operations and cash flows.

We are, and expect to continue to be, dependent on spot market-oriented pools and spot charters and any decrease in spot charter rates in the future may adversely affect our earnings.

The Scorpio Group Pools in which our vessels operate, or are expected to operate, are spot market-oriented commercial pools managed by our commercial manager, which expose us to fluctuations in spot market charter rates. The spot charter market may fluctuate significantly based upon drybulk carrier supply and demand. The successful operation of our vessels in the competitive spot charter market, including within the Scorpio Group Pools, depends on, among other things, obtaining profitable spot charters and minimizing, to the extent possible, time spent waiting for charters and time spent traveling unladen to pick up cargo. The spot market is very volatile, and, in the recent past, there have been periods when spot charter rates have declined below the operating cost of vessels and for some vessel classes are currently only slightly above operating costs. If future spot charter rates decline, then we may be unable to operate our vessels trading in the spot market profitably, meet our obligations, including payments on indebtedness, or pay dividends in the future. Furthermore, as charter rates for spot charters are fixed for a single voyage which may last up to several weeks, during periods in which spot charter rates are rising, we will generally experience delays in realizing the benefits from such increases.

Our ability to renew expiring charters or obtain new charters will depend on the prevailing market conditions at the time. If we are not able to obtain new charters in direct continuation with previous charters, or if new charters are entered into at charter rates substantially below the existing charter rates or on terms otherwise less favorable compared to previous charter terms, our revenues and profitability could be adversely affected.

The failure of our charterers to meet their obligations under our charter agreements, on which we depend for our revenues, could cause us to suffer losses or otherwise adversely affect our business.

We do not expect to employ any of our vessels under a long-term time charter agreement but we may enter into such agreements in the future. The ability and willingness of each of our counterparties to perform their obligations under a time charter, spot voyage or other agreement with us, directly or through our pooling arrangements, will depend on a number of factors that are beyond our control and may include, among other things, general economic conditions, the condition of the drybulk shipping industry and the overall financial condition of the counterparties. In addition, in depressed market conditions, there have been reports of charterers renegotiating their charters or defaulting on their obligations under charters. Our customers may fail to pay charterhire or attempt to renegotiate charter rates. Should a counterparty fail to honor its obligations under agreements with us, it may be difficult to secure substitute employment for such vessel, and any new charter arrangements we secure in the spot market or on time charters may be at lower rates given currently decreased drybulk carrier charter rate levels. When we employ a vessel in the spot charter market, we intend to place such vessel in a drybulk carrier pool managed by our commercial manager that pertains to that vessel s size class. If our charterers fail to meet their obligations to us or attempt to renegotiate our charter agreements, we could sustain significant losses which could have a material adverse effect on our business, financial condition, results of operations and cash flows, as well as our ability to pay dividends, if any, in the future, on our common shares and interest on our Notes, and comply with covenants in our credit facilities.

We may have difficulty managing our planned growth properly.

We have entered into shipbuilding contracts with established shipyards in Japan, China, South Korea and Romania for the construction of 80 latest generation drybulk vessels and chartered in 19 vessels, of which 18 vessels have been delivered to us, that we employ in the Scorpio Group Pools. One of our principal strategies is to continue to grow by expanding our operations and adding to our fleet. Our future growth will primarily depend upon a number of factors, some of which may not be within our control. These factors include our ability to:

- identify suitable drybulk carriers, including newbuilding slots at shipyards and/or shipping companies for acquisitions at attractive prices;
- obtain required financing for our existing and new operations;
- identify businesses engaged in managing, operating or owning drybulk carriers for acquisitions or joint ventures;
- integrate any acquired drybulk carriers or businesses successfully with our existing operations, including obtaining any approvals and qualifications necessary to operate vessels that we acquire;
- hire, train and retain qualified personnel and crew to manage and operate our growing business and fleet;
- identify additional new markets;
- enhance our customer base; and
- improve our operating, financial and accounting systems and controls.

Our failure to effectively identify, acquire, develop and integrate any drybulk carriers or businesses could adversely affect our business, financial condition and results of operations. The number of employees that perform services for us and our current operating and financial systems may not be adequate as we implement our plan to expand the size of our fleet in the drybulk sector, and we may not be able to effectively hire more employees or adequately improve those systems. Finally, acquisitions may require additional equity issuances, which may dilute our common shareholders if issued at lower prices than the price they acquired their shares, or debt issuances (with amortization payments), both of which could lower our available cash. If any such events occur, our financial condition may be adversely affected.

Growing any business by acquisition presents numerous risks such as undisclosed liabilities and obligations, difficulty in obtaining additional qualified personnel and managing relationships with customers and suppliers and integrating newly acquired operations into existing infrastructures. The expansion of our fleet may impose significant additional responsibilities on our management and staff, and the management and staff of our commercial and technical managers, and may necessitate that we, and they, increase the number of personnel. We cannot give any assurance that we will be successful in executing our growth plans or that we will not incur significant expenses and losses in connection with our future growth.

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As we expand our business, we may need to improve our operating and financial systems and will need to recruit suitable employees and crew for our vessels.

Our current operating and financial systems may not be adequate as we implement our plan to take delivery of 80 newbuilding vessels between the third quarter of 2014 and the third quarter of 2016 and to expand the size of our fleet through acquiring and chartering in additional vessels and our attempts to improve those systems may be ineffective. In addition, if we further expand our fleet, we will need to recruit suitable additional seafarers and shore side administrative and management personnel. We cannot guarantee that we will be able to hire suitable employees as we expand our fleet. If we or our crewing agent encounters business or financial difficulties, we may not be able to adequately staff our vessels. If we are unable to grow our financial and operating systems or to recruit suitable employees as we expand our fleet, our financial performance may be adversely affected and, among other things, the amount of cash available for distribution as dividends to our shareholders may be reduced.

If we acquire and operate secondhand vessels, we will be exposed to increased operating costs which could adversely affect our earnings and, as our fleet ages, the risks associated with older vessels could adversely affect our ability to obtain profitable charters.

Our current business strategy includes additional growth which may, in addition to the acquisition of newbuilding vessels, include the acquisition of modern secondhand vessels. While we expect that we would typically inspect secondhand vessels prior to acquisition, this does not provide us with the same knowledge about their condition that we would have had if these vessels had been built for and operated exclusively by us. Generally, purchasers of secondhand vessels do not receive the benefit of warranties from the builders for the secondhand vessels that they acquire.

Governmental regulations, safety or other equipment standards related to the age of vessels may require expenditures for alterations, or the addition of new equipment, to our vessels and may restrict the type of activities in which the vessels may engage. As our vessels age, market conditions may not justify those expenditures or enable us to operate our vessels profitably during the remainder of their useful lives.

The aging of our fleet may result in increased operating costs in the future, which could adversely affect our earnings.

In general, the cost of maintaining a vessel in good operating condition increases with the age of the vessel. While all of the vessels in our owned fleet will be newbuildings, as our vessels age typically they will become less fuel-efficient and more costly to maintain than more recently constructed vessels due to improvements in engine technology. Cargo insurance rates increase with the age of a vessel, making older vessels less desirable to charterers. Governmental regulations and safety or other equipment standards related to the age of vessels may also require expenditures for alterations or the addition of new equipment, to our vessels and may restrict the type of activities in which our vessels may engage. We cannot assure you that, as our vessels age, market conditions will justify those expenditures or enable us to operate our vessels profitably during the remainder of their useful lives.

Technological innovation could reduce our charter hire income and the value of our vessels.

The charter hire rates and the value and operational life of a vessel are determined by a number of factors including the vessel s efficiency, operational flexibility and physical life. Efficiency includes speed, fuel economy and the ability to load and discharge cargo quickly. Flexibility includes the ability to enter harbors, utilize related docking facilities and pass through canals and straits. The length of a vessel s physical life is related to its original design and construction, its maintenance and the impact of the stress of operations. If new drybulk carriers are built that are more efficient or more flexible or have longer physical lives than our vessels, competition from these more technologically advanced vessels could adversely affect the amount of charterhire payments we receive for our vessels once their initial charters expire and the resale value of our vessels could significantly decrease. As a result, our business, results of operations, cash flows and financial condition could be adversely affected.

In the highly competitive international shipping industry, we may not be able to compete for charters with new entrants or established companies with greater resources, and as a result, we may be unable to employ our vessels profitably.

Our vessels will be employed in a highly competitive market that is capital intensive and highly fragmented. Competition arises primarily from other vessel owners, some of whom have substantially greater resources than we do. Competition for the transportation of drybulk cargo by sea is intense and depends on price, location, size, age, condition and the acceptability of the vessel and its operators to the charterers. Due in part to the highly fragmented market, competitors with greater resources could enter the drybulk shipping industry and operate larger fleets through consolidations or acquisitions and may be able to offer lower charter rates and higher quality vessels than we are able to offer. If we are unable to successfully compete with other drybulk shipping companies, our results of operations would be adversely impacted.

We may be subject to litigation that, if not resolved in our favor and not sufficiently insured against, could have a material adverse effect on us.

We may be, from time to time, involved in various litigation matters. These matters may include, among other things, contract disputes, personal injury claims, environmental claims or proceedings, asbestos and other toxic tort claims, employment matters, governmental claims for taxes or duties, and other litigation that arises in the ordinary course of our business. Although we intend to defend these matters vigorously, we cannot predict with certainty the outcome or effect of any claim or other litigation matter, and the ultimate outcome of any litigation or the potential costs to resolve them may have a material adverse effect on us. Insurance may not be applicable or sufficient in all cases and/or insurers may not remain solvent which may have a material adverse effect on our financial condition.

We are a holding company, and we depend on the ability of our subsidiaries to distribute funds to us in order to satisfy our financial obligations and to make dividend payments.

We are a holding company and our subsidiaries conduct all of our operations and own all of our operating assets. We have no significant assets other than the equity interests in our subsidiaries. As a result, our ability to satisfy our financial obligations and to make dividend payments in the future depends on our subsidiaries and their ability to distribute funds to us. If we are unable to obtain funds from our subsidiaries, our board of directors may exercise its discretion not to declare or pay dividends. We do not intend to obtain funds from other sources to pay dividends.

Because we are organized under the laws of the Marshall Islands, it may be difficult to serve us with legal process or enforce judgments against us, our directors or our management.

We are organized under the laws of the Marshall Islands, and substantially all of our assets are located outside of the United States. In addition, the majority of our directors and officers are or will be non-residents of the United States, and all or a substantial portion of the assets of these non-residents are located outside the United States. As a result, it may be difficult or impossible for you to bring an action against us or against these individuals in the United States if you believe that your rights have been infringed under securities laws or otherwise. Even if you are successful in bringing an action of this kind, the laws of the Marshall Islands and of other jurisdictions may prevent or restrict you from enforcing a judgment against our assets or the assets of our directors or officers. For more information regarding the relevant laws of the Marshall Islands, see Service of Process and Enforcement of Civil Liabilities.

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We are incorporated in the Marshall Islands, which does not have a well-developed body of corporate law.

Our corporate affairs are governed by our amended and restated articles of incorporation and bylaws and by the Marshall Islands Business Corporations Act, or the BCA. The provisions of the BCA resemble provisions of the corporation laws of a number of states in the United States. However, there have been few judicial cases in the Marshall Islands interpreting the BCA. The rights and fiduciary responsibilities of directors under the laws of the Marshall Islands are not as clearly established as the rights and fiduciary responsibilities of directors under statutes or judicial precedent in existence in the United States. The rights of shareholders of companies incorporated in the Marshall Islands may differ from the rights of shareholders of companies incorporated in the United States. While the BCA provides that it is to be interpreted according to the laws of the State of Delaware and other states with substantially similar legislative provisions, there have been few, if any, court cases interpreting the BCA in the Marshall Islands and we can t predict whether Marshall Islands courts would reach the same conclusions as United States courts. Thus, you may have more difficulty in protecting your interests in the face of actions by the management, directors or controlling shareholders than would shareholders of a corporation incorporated in a United States jurisdiction which has developed a relatively more substantial body of case law.

The international nature of our operations may make the outcome of any bankruptcy proceedings difficult to predict.

We are incorporated under the laws of the Republic of The Marshall Islands and we conduct operations in countries around the world. Consequently, in the event of any bankruptcy, insolvency, liquidation, dissolution, reorganization or similar proceeding involving us or any of our subsidiaries, bankruptcy laws other than those of the United States could apply. If we become a debtor under U.S. bankruptcy law, bankruptcy courts in the United States may seek to assert jurisdiction over all of our assets, wherever located, including property situated in other countries. There can be no assurance, however, that we would become a debtor in the United States, or that a U.S. bankruptcy court would be entitled to, or accept, jurisdiction over such a bankruptcy case, or that courts in other countries that have jurisdiction over us and our operations would recognize a U.S. bankruptcy court s jurisdiction if any other bankruptcy court would determine it had jurisdiction.

We may have to pay tax on United States source income, which would reduce our earnings and cash flow.

Under the United States Internal Revenue Code of 1986, as amended, or the Code, 50% of the gross shipping income of a vessel owning or chartering corporation, such as ourselves and our subsidiaries, that is attributable to transportation that begins or ends, but that does not both begin and end, in the United States is characterized as United States source shipping income and such income is subject to a 4% United States federal income tax without allowance for any deductions, unless that corporation qualifies for exemption from tax under Section 883 of the Code and the Treasury regulations promulgated thereunder.

We have taken the position that we qualified for this statutory exemption for U.S. federal income tax return reporting purposes for our 2013 taxable year and we intend to so qualify for future taxable years. However, there are factual circumstances beyond our control that could cause us to lose the benefit of this tax exemption and thereby cause us to become subject to United States federal income tax on our United States source shipping income. For example, there is a risk that we could no longer qualify for exemption under Section 883 of the Code for a particular taxable year if non-qualified shareholders with a five percent or greater interest in our stock were, in combination with each other, to own 50% or more of the outstanding shares of our stock on more than half the days during the taxable year. Due to the factual nature of the issues involved, we can give no assurances on our tax-exempt status or that of any of our subsidiaries.

If we are not entitled to this exemption under Section 883 of the Code for any taxable year, we would be subject for such taxable year to a 4% United States federal income tax on our United States source shipping income on a gross basis. The imposition of this taxation could have a negative effect on our business and would result in decreased earnings and cash available to pay amounts due on the Notes.

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United States tax authorities could treat us as a passive foreign investment company, which could have adverse United States federal income tax consequences to United States shareholders.

A foreign corporation will be treated as a passive foreign investment company, or PFIC, for United States federal income tax purposes if either (1) at least 75% of its gross income for any taxable year consists of certain types of passive income or (2) at least 50% of the average value of the corporation s assets produce or are held for the production of those types of passive income, including cash. For purposes of these tests, passive income includes dividends, interest, and gains from the sale or exchange of investment property and rents and royalties other than rents and royalties which are received from unrelated parties in connection with the active conduct of a trade or business. For purposes of these tests, income derived from the performance of services does not constitute passive income. United States shareholders of a PFIC are subject to a disadvantageous United States federal income tax regime with respect to the income derived by the PFIC, the distributions they receive from the PFIC and the gain, if any, they derive from the sale or other disposition of their shares in the PFIC.

There is a significant risk that we will be treated as a PFIC for our 2013, 2014 and 2015 taxable years. Whether we are treated as a PFIC will depend, in part, upon whether the deposits that we make on newbuilding contracts are treated as being held for the production of passive income and on the amount of passive income that we derive for such years.

Thereafter, whether we will be treated as a PFIC will depend upon the nature and extent of our operations. In this regard, we intend to treat the gross income we derive or are deemed to derive from our time chartering activities as services income, rather than rental income. Accordingly, we believe that our income from our time chartering activities does not constitute passive income, and the assets that we own and operate in connection with the production of that income do not constitute passive assets. There is, however, no direct legal authority under the PFIC rules addressing our method of operation. Accordingly, no assurance can be given that the United States Internal Revenue Service, or IRS, or a court of law will accept our position, and there is a risk that the IRS or a court of law could determine that we are a PFIC. Moreover, no assurance can be given that we would not constitute a PFIC for any taxable year if there were to be changes in the nature and extent of our operations.

If we were treated as a PFIC for any taxable year, our United States shareholders may face adverse United States federal income tax consequences and information reporting obligations. As a result, it may be difficult for us to raise capital through sales of our common stock.

We are an emerging growth company and we cannot be certain if the reduced disclosure requirements applicable to emerging growth companies will make our common shares and Notes less attractive to investors.

We are an emerging growth company, as defined in the JOBS Act, and we may take advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not emerging growth companies as described under Summary Implications of Being an Emerging Growth Company. We cannot predict if investors will find our common shares and Notes less attractive because we may rely on these exemptions. If some investors find our common shares and Notes less attractive as a result, there may be a less active trading market for our common shares and Notes and our share price and Note price may be more volatile.

In addition, under the JOBS Act, our independent registered public accounting firm will not be required to attest to the effectiveness of our internal control over financial reporting pursuant to Section 404 of the Sarbanes-Oxley Act of 2002 for so long as we are an emerging growth company. For as long as we take advantage of the reduced reporting obligations, the information that we provide shareholders may be different from information provided by other public companies.

Our costs of operating as a public company will be significant, and our management will be required to devote substantial time to complying with public company regulations.

We recently became subject to the reporting requirements of the Securities Exchange Act of 1934, as amended, or the Exchange Act, and the other rules and regulations of the SEC, including the Sarbanes-Oxley Act of 2002, or the Sarbanes-Oxley Act, and as such, we will have significant legal, accounting and other expenses that we did not incur as a private company. These reporting obligations impose various requirements on public companies, including changes in corporate governance practices, and these requirements may continue to evolve. We and our management personnel, and other personnel, if any, will need to devote a substantial amount of time to comply with these requirements. Moreover, these rules and regulations increase our legal and financial compliance costs and make some activities more time-consuming and costly.

Sarbanes-Oxley requires, among other things, that we maintain and periodically evaluate our internal control over financial reporting and disclosure controls and procedures. In particular, we need to perform system and process evaluation and testing of our internal control over financial reporting to allow management and our independent registered public accounting firm to report on the effectiveness of our internal control over financial reporting, as required by Section 404 of Sarbanes-Oxley, subject to the reduced disclosure requirements for emerging growth companies set forth above. Our compliance with Section 404 may require that we incur substantial accounting expenses and expend significant management efforts.

Risks Related to Our Relationship with Scorpio Group and its Affiliates

We are dependent on our managers and their ability to hire and retain key personnel, and there may be conflicts of interest between us and our managers that may not be resolved in our favor.

Our success depends to a significant extent upon the abilities and efforts of our technical manager, SSM, our commercial manager, SCM, and our management team. Our success will depend upon our and our managers ability to hire and retain key members of our management team. The loss of any of these individuals could adversely affect our business prospects and financial condition.

Difficulty in hiring and retaining personnel could adversely affect our results of operations. We do not maintain key man life insurance on any of our officers.

Our technical and commercial managers are affiliates of the Scorpio Group, which is owned and controlled by the Lolli-Ghetti family, of which our founder, Chairman and Chief Executive Officer, Mr. Emanuele Lauro, is a member. Conflicts of interest may arise between us, on the one hand, and our commercial and technical managers, on the other hand. As a result of these conflicts, our commercial and technical managers, who have limited contractual duties, may favor their own or their owner s interests over our interests. These conflicts may have unfavorable results for us.

Our Co-Founder, Chairman and Chief Executive Officer, has affiliations with our commercial and technical managers which may create conflicts of interest.

Emanuele Lauro, our Co-Founder, Chairman and Chief Executive Officer, is a member of the Lolli-Ghetti family which owns and controls our commercial and technical managers. These relationships could create conflicts of interest between us, on the one hand, and our commercial and technical managers, on the other hand. These conflicts may arise in connection with the chartering, purchase, sale and operation of the vessels in our fleet versus vessels managed by other companies affiliated with our commercial or technical managers. In particular, as of the date of this prospectus, our commercial and technical managers provide commercial and technical management services to approximately 100 and 40 vessels, respectively, other than the vessels in our fleet, that are operated by entities affiliated with Mr. Lauro, and such entities may operate additional vessels that will compete with our vessels in the future. Such conflicts may have an adverse effect on our results of operations.

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Our Chief Executive Officer, President, and Chief Operating Officer will not devote all of their time to our business, which may hinder our ability to operate successfully.

Our Chief Executive Officer, President, Chief Operating Officer, Vice President, Vessel Operations, General Counsel and Secretary participate in business activities not associated with us, including serving as members of the management team of Scorpio Tankers and are not required to work full-time on our affairs. Initially, we expect that each of our executive officers will devote a substantial portion of his business time to the completion of our Newbuilding Program and management of the Company. Additionally, our Chief Executive Officer, President, Chief Operating Officer, Vice President, Vessel Operations, General Counsel and Secretary serve in similar positions in the Scorpio Group. As a result, such officers may devote less time to us than if they were not engaged in other business activities and may owe fiduciary duties to the shareholders of both us as well as shareholders of other companies which they may be affiliated with, including Scorpio Tankers and Scorpio Group companies. This may create conflicts of interest in matters involving or affecting us and our customers and it is not certain that any of these conflicts of interest will be resolved in our favor. This could have a material adverse effect on our business, financial condition, results of operations and cash flows.

Our commercial and technical managers are each privately held companies and there is little or no publicly available information about them.

Our vessels are, or are expected to be upon their delivery to us, commercially managed by SCM and technically managed by SSM. SCM s and SSM s ability to render management services will depend in part on their own financial strength. Circumstances beyond our control could impair our commercial manager s or technical manager s financial strength, and because each is a privately held company, information about the financial strength of our commercial manager and technical manager is not available. As a result, we and our shareholders might have little advance warning of financial or other problems affecting our commercial manager or technical manager even though their financial or other problems could have a material adverse effect on us.

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RATIO OF EARNINGS TO FIXED CHARGES

The following table sets forth our ratio of earnings to fixed charges for the period from March 20, 2013 (date of inception) to December 31, 2013 and the six months ended June 30, 2014.

(Dollars in Thousands)	Six Months Ended June 30, 2014		Period from March 20, 2013 (date of inception) to December 31, 2013	
Earnings:				
Net loss	$	(25,658)	$	(6,307)
Plus: Fixed charges (calculated below)		8,854		-
Earnings Available to Cover Fixed Charges	$	(16,804)	$	(6,307)
Fixed charges:				
Interest component of rent (1)	$	8,854	$	-
Fixed charges	$	8,854	$	-
Ratio of earnings to fixed charges		*		*

(1) Represents one-third of charterhire expense, which is the proportion deemed representative of the interest factor.

* For the six months ended June 30, 2014 and for the period March 20, 2013 (date of inception) to December 31, 2013, earnings were inadequate to cover fixed charges by $25,658 and $6,307, respectively.

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USE OF PROCEEDS

We intend to use all or substantially all of the net proceeds of the sale of our Notes, which are expected to total approximately $ after deducting underwriting discounts and commissions and estimated offering expenses (or approximately $ if the underwriters exercise their option to purchase additional Notes in full), to fund installment payments due under our Newbuilding Program, and the remaining amount, if any, for general corporate purposes and working capital.

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CAPITALIZATION

The following table sets forth our capitalization at June 30, 2014, on:

- an actual basis;
- an as adjusted basis to give effect to installment payments of $114.8 million on vessels under construction during the period from July 1, 2014 to August 28, 2014; and
- an as further adjusted basis to give effect to the $50.0 million proceeds of this Notes offering.

There have been no other significant adjustments to our capitalization since June 30, 2014, as so adjusted. The following should be read in conjunction with the consolidated financial statements and the related notes thereto in this prospectus as well as Management s Discussion and Analysis of Financial Condition and Results of Operations.

	As of June 30, 2014		
In thousands of U.S. dollars	**Actual**	**As Adjusted**	**As Further Adjusted**
Cash and Cash Equivalents	$ 345,956	$ 231,173	$ 281,172
Total Cash and Cash Equivalents	345,596	231,173	281,172
Current debt:			
Bank loans	-	-	-
Non-current debt:			
Bank loans	-	-	-
Senior Notes	-	-	50,000
Total debt	$ -	$ -	$ 50,000
Shareholders equity:			
Common Stock	$ 1,402	$ 1,402	$ 1,402
Paid-in capital	1,162,755	1,162,755	1,162,755
Accumulated deficit	(31,965)	(31,965)	(31,965)
Total shareholders equity	$ 1,132,192	$ 1,132,192	$ 1,132,192
Total capitalization	$ 1,132,192	$ 1,132,192	$ 1,182,192

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SELECTED CONSOLIDATED FINANCIAL AND OTHER DATA

We were formed on March 20, 2013 for the purpose of acquiring and operating the latest generation of newbuilding drybulk carriers with fuel-efficient specifications and carrying capacities of greater than 30,000 dwt in the international shipping markets. The following table summarizes our selected consolidated financial and other operating data at the dates and for the periods indicated.

Our selected consolidated financial and other data as of and for the six month period ended June 30, 2014 has been derived from our unaudited interim consolidated financial statements and related notes thereto, appearing elsewhere in this prospectus. Our selected consolidated financial data as of December 31, 2013 and for the period from March 20, 2013 (date of inception) to December 31, 2013 has been derived from our audited consolidated financial statements and related notes thereto, which are incorporated by reference herein. Our consolidated financial statements have been prepared in accordance with U.S. GAAP. The following financial data should be read in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations, and our consolidated financial statements and related notes included elsewhere in this prospectus.

	Six Months Ended June 30, 2014	Period from March 20, 2013 (date of inception) to December 31, 2013
	(Dollars in Thousands)	
Statement of Operations		
Revenue:		
Vessel revenue	$ 18,647	$ -
Operating expenses:		
Voyage expenses	3,180	-
Charterhire expenses	26,562	-
General and administrative expenses	15,351	5,505
Total operating expenses	45,093	5,505
Operating loss	(26,446)	(5,505)
Other income and (expense):		
Interest income	793	341
Foreign exchange loss	(5)	(1,135)
Other expense, net	-	(8)
Total other income and expense	788	(802)
Net loss	$ (25,658)	$ (6,307)

	As of June 30, 2014	As of December 31, 2013
	(Dollars in Thousands)	
Balance Sheet		

Cash and cash equivalents	$ 345,956	$ 733,896
Vessels under construction	842,845	371,692
Total assets	1,211,283	1,105,684
Current liabilities	79,091	1,472
Total liabilities	79,091	1,472
Shareholders equity	1,132,192	1,104,212

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	Six Months Ended June 30, 2014	Period from March 20, 2013 (date of inception) to December 31, 2013
	(Dollars in Thousands)	
Cash Flow		
Net cash inflow (outflow)		
Operating activities	$ (32,203)	$ (2,237)
Investing activities	(397,000)	(371,692)
Financing activities	41,263	1,107,825

(Dollars in Thousands, Except Per Day Data)	Six Months Ended June 30, 2014
Other Financial Data (1)	
Time Charter Equivalent Revenue (2):	
Vessel revenue	$ 18,647
Voyage expenses	3,180
Time charter equivalent revenue	$ 15,467
Time charter equivalent revenue attributable to:	
Kamsarmax	$ 12,027
Ultramax	3,440
	$ 15,467
Revenue days (2):	
Kamsarmax	1,560
Ultramax	335
Combined	1,895
TCE per revenue day (2):	
Kamsarmax	$ 7,712
Ultramax	$ 10,262
Combined	$ 8,163

(1) We had no revenue prior to 2014 and, accordingly, there are no other financial data for any period in 2013.

(2) We define Time Charter Equivalent (TCE) revenue as voyage revenues less voyage expenses. Such TCE revenue, divided by the number of our available days during the period, or revenue days, is TCE per revenue day, which is consistent with industry standards. TCE per revenue day is a common shipping industry performance measure used primarily to compare daily earnings generated by vessels on time charters with daily earnings generated by vessels on voyage charters, because charter hire rates for vessels on voyage charters are generally not expressed in per-day amounts while charter hire rates for vessels on time charters generally are expressed in such amounts.

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MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following presentation of management s discussion and analysis of results of operations and financial condition should be read in conjunction with the Selected Consolidated Financial and Other Data and our consolidated financial statements and related notes thereto, included elsewhere in this prospectus. The following discussion contains forward-looking statements that reflect our future plans, estimates, beliefs and expected performance. The forward-looking statements are dependent upon events, risks and uncertainties that may be outside our control. Our actual results could differ materially from those discussed in these forward-looking statements. Please read Risk Factors and Forward-Looking Statements. In light of these risks, uncertainties and assumptions, the forward-looking events discussed may not occur. Our audited consolidated financial statements as of December 31, 2013 and for the period from March 20, 2013 (date of inception) to December 31, 2013, and our unaudited interim consolidated financial statements as of and for the six month period ended June 30, 2014, have been prepared in accordance with accounting principles generally accepted in the United States of America, or U.S. GAAP. We reported in our December 31, 2013 financial statements that we were a development stage company. The consolidated financial statements are presented in U.S. dollars ($) unless otherwise indicated. Any amounts converted from another non-U.S. currency to U.S. dollars in this prospectus are at the rate applicable at the relevant date, or the average rate during the applicable period.

We are an international shipping company that was incorporated in the Republic of the Marshall Islands on March 20, 2013 for the purpose of acquiring and operating the latest generation of newbuilding drybulk carriers with fuel-efficient specifications and carrying capacities of greater than 30,000 dwt. We believe that it is an opportune time to acquire these vessels because acquisition costs for these vessels are currently near the lowest average levels of the past 10 years. In addition, we believe that recent advances in shipbuilding design and technology should make these latest generation vessels more fuel-efficient than older vessels in the global fleet that compete with us for charters, providing us with a competitive advantage. Our fleet transports a broad range of major and minor bulk commodities, including ores, coal, grains, and fertilizers, along worldwide shipping routes, and are, or are expected to be, employed primarily in the spot market or in spot market-oriented pools of similarly sized vessels. As of the date of this prospectus, our operating fleet consists of 19 drybulk vessels, of which 18 are vessels that we charter-in and one is a recently delivered Kamsarmax vessel from our Newbuilding Program, with an aggregate carrying capacity of approximately 1.5 million dwt, which we refer to as our Operating Fleet. We also have one time charter-in contract that is scheduled to commence during the first half of 2015 and contracts for the construction of 79 newbuilding drybulk vessels at established shipyards in Japan, China, South Korea and Romania, which we have agreed to acquire for an aggregate purchase price of $3,070.8 million, including 29 Ultramax vessels, 22 Kamsarmax vessels and 28 Capesize vessels, each with a carrying capacity of between 60,000 dwt and 180,000 dwt and an aggregate carrying capacity of approximately 8.6 million dwt. We refer to these newbuilding vessels as our Newbuilding Program. We expect to take delivery of the vessels in our Newbuilding Program as follows: one vessel in 2014, 42 vessels in 2015 and 36 vessels in 2016. Until we have taken delivery of a larger number of the vessels in our Newbuilding Program, we do not anticipate earning a material amount of revenues from our operations.

In December 2013, we completed our underwritten initial public offering of 31,300,000 common shares at $9.75 per share, and in January 2014, the underwriters in the initial public offering exercised their option to purchase an additional 4,695,000 common shares. In February 2014, we completed our offer to exchange unregistered common shares that were previously issued in Norwegian equity private placements (other than the common shares owned by affiliates of us) for common shares that were registered under the Securities Act of 1933, as amended, which we refer to as the Exchange Offer. Upon completion of the Exchange Offer, holders of 95,766,779 unregistered common shares validly tendered their shares in exchange for such registered common shares, representing a participation rate of 99.7%. On July 31, 2014, we delisted from the Norwegian OTC. Our common shares currently trade on the New York

Stock Exchange under the symbol SALT.

Following the completion of this offering, we expect to have in excess of $ million of available cash. As of June 30, 2014, we have paid a total of $764.1 million in initial installment payments due under our shipbuilding contracts for our Newbuilding Program. We plan to finance the remaining contractual commitments of $2,338.8 million with the net proceeds received from this offering, cash on hand, cash flows from operations, borrowings under committed and proposed new secured credit facilities, and from capital raised in the public and private debt and equity capital markets. As of July 30, 2014, we have signed three loan agreements (our $330.0 Senior Secured Credit Facility, our $67.5 Million Senior Secured Credit Facility, and our $39.6 Million Senior Secured Credit Facility) which will provide up to $437.1 million in available borrowings, which will be used to finance a portion of the contract price of 28 vessels in our Newbuilding Program (18 Ultramax and 10 Kamsarmax vessels). In addition, on July 21, 2014, we received a commitment from two leading European financial institutions for a $540.0 million senior secured credit facility, which we refer to as our Proposed $540.0 Million Senior Secured Credit Facility, which we expect to use to finance up to 55% of the contract price of six Ultramax, nine Kamsarmax, and nine Capesize vessels currently under construction for delivery in 2015 and 2016.

With respect to the remaining 28 unfinanced vessels in our Newbuilding Program (five Ultramax, four Kamsarmax and 19 Capesize vessels), we received proposals from leading European and Asian financial institutions to finance between 55% of the contract price and 60% of the market value of the remaining unfinanced vessels currently under construction. The terms and conditions of these proposals, for which commitments are expected within 2014, are expected to be consistent with those of the our existing credit facilities. Our entry into any loan facility that may result from these proposals remains subject to credit approval and customary conditions precedent, including negotiation and execution of final documentation. We cannot assure you that we will be successful in obtaining the financing necessary to fund all of our remaining contractual obligations under our shipbuilding contracts or will be able to take delivery of all the vessels we have agreed to acquire.

In addition, we plan to use all or substantially all of the net proceeds from this offering and the net proceeds from future equity or debt offerings or both, together with the amounts we expect to be available to us under our credit facilities, to fund installment payments due under our Newbuilding Program, and the remaining amounts, if any, for general corporate purposes and working capital. Our intention is to acquire additional latest generation drybulk carriers with fuel-efficient vessel specifications and carrying capacities of greater than 30,000 dwt, either directly from shipyards or from owners with existing newbuilding vessel contracts. We may also acquire secondhand vessels that meet our stringent vessel specifications. The timing of these vessel acquisitions will depend on our ability to identify suitable vessels on attractive acquisition terms. Although we may have the capacity to obtain additional financing, we intend to maintain moderate levels of leverage of not more than 60% of the value of our vessels collateralizing our indebtedness on a consolidated basis.

Results for the six month period ended June 30, 2014

For the six months ended June 30, 2014, the Company recorded a net loss of $25.7 million.

Time charter equivalent, or TCE revenue, a non-GAAP measure, is vessel revenues less voyage expenses (including bunkers and port charges). TCE revenue is included herein because it is a standard shipping industry performance measure used primarily to compare period-to-period changes in a shipping company s performance irrespective of changes in the mix of charter types (i.e., spot charters, time charters, and pool charters), and it provides useful information to investors and management.

Time Charter Equivalent Revenue: (in thousands of U.S. dollars):

Vessel revenue	$ 18,647
Voyage expenses	3,180
Time charter equivalent revenue	$ 15,467

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TCE revenue was $15.5 million for the six months ended June 30, 2014, associated with chartering in 18 vessels, for which the time charter equivalent revenue per day was $8,163 overall, $7,712 per day for our Kamsarmax vessels and $10,262 per day for our Ultramax vessels (see the breakdown of daily TCE averages in the section Summary Consolidated Financial and Other data). Time charter equivalent revenue per day, was adversely affected, especially as it relates to the Kamsarmax vessels, by the integration of the time chartered-in vessels into our fleet which required significant time and fuel as they had to be repositioned for their first voyages as well as a depressed rate environment for dry bulk carriers.

Our revenue has been generated from spot market voyage charters, by either deploying our vessels in the spot market or from revenue we derive from the Scorpio Kamsarmax Pool and Scorpio Ultramax Pool deploying our vessels in the spot market. The spot market is extremely volatile. In 2014, the Baltic Dry Index, or the BDI, a daily average of charter rates for key drybulk routes published by the Baltic Exchange Limited, which has long been viewed as the main benchmark to monitor the movements of the drybulk vessel charter market and the performance of the entire drybulk shipping market, started off at 2,113 on January 2, 2014 and has since decreased to 1,362 as of March 31, 2014 and to 850 as of June 30, 2014.

Charterhire expense was $26.6 million for the six months ended June 30, 2014 relating to the time chartered-in vessels described above. See the Company s Fleet List below for the terms of these agreements.

General and administrative expense was $15.4 million for the six months ended June 30, 2014. Such amount included $11.3 million of restricted stock amortization (noncash) and the balance primarily related to payroll, directors fees, professional fees and insurance.

Results for the Period from March 20, 2013 (date of inception) to December 31, 2013

For the period from March 20, 2013 (date of inception) to December 31, 2013, we had a net loss of $6.3 million, or $0.16 basic and diluted loss per share. During this period, we had no vessels in operation. As such, we had no revenues, voyage expenses or vessel related expenses. General and administrative expense was $5.5 million for the period from March 20, 2013 (date of inception) to December 31, 2013, the majority of which relates to amortization of stock-based compensation and salaries of New York and Monaco based personnel, including our officers. Amortization of stock-based compensation was $3.4 million for the period from March 20, 2013 (date of inception) to December 31, 2013.

Also contributing to our net loss for the period from March 20, 2013 (date of inception) to December 31, 2013 was a $1.1 million foreign exchange loss. Such loss relates to the issuance and sale on September 24, 2013 of 33,400,000 common shares for net proceeds that were denominated in Norwegian kroner (NOK), in Norwegian private placement transactions exempt from registration under the Securities Act which was not settled in U.S. dollars until October 2013.

Critical Accounting Policies

This discussion and analysis of our financial condition and results of operations is based upon our condensed consolidated financial statements, which have been prepared in accordance with U.S. GAAP. The preparation of those financial statements requires us to make estimates and judgments that affect the reported amount of assets and liabilities, revenues and expenses and related disclosure of contingent assets and liabilities at the date of our financial statements. Actual results may differ from these estimates under different assumptions or conditions.

Critical accounting policies are those that reflect significant judgments or uncertainties, and potentially result in materially different results under different assumptions and conditions. We have described below what we believe are our most critical accounting policies.

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Revenue recognition

Vessel Revenue. Vessel revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for services provided in the normal course of business, net of discounts, and other sales-related or value added taxes. Vessel revenue is comprised of time charter revenue, voyage revenue and pool revenue.

Time Charter Revenue. Time charter revenue is recognized as services are performed based on the daily rates specified in the time charter contract.

Voyage Charter Revenue. Voyage charter agreements are charter hires, where a contract is made in the spot market for the use of a vessel for a specific voyage for a specified charter rate. Revenue from voyage charter agreements is recognized on a pro rata basis based on the relative transit time in each period. The period over which voyage revenues are recognized commences at the time the vessel departs from its last discharge port and ends at the time the discharge of cargo at the next discharge port is completed. We do not begin recognizing revenue until a charter has been agreed to by the customer and us, even if the vessel has discharged its cargo and is sailing to the anticipated load port on its next voyage. We do not recognize revenue when a vessel is off hire. Estimated losses on voyages are provided for in full at the time such losses become evident. In the application of this policy, we do not begin recognizing revenue until (i) the amount of revenue can be measured reliably, (ii) it is probable that the economic benefits associated with the transaction will flow to the entity, (iii) the transactions stage of completion at the balance sheet date can be measured reliably and (iv) the costs incurred and the costs to complete the transaction can be measured reliably.

Pool Revenue. Pool revenue for each vessel is determined in accordance with the profit sharing terms specified within each pool agreement. In particular, the pool manager aggregates the revenues and expenses of all of the pool participants and distributes the net earnings to participants based on:

- the pool points (vessel attributes such as cargo carrying capacity, fuel consumption, and construction characteristics are taken into consideration); and

- the number of days the vessel participated in the pool in the period.

We recognize pool revenue on a monthly basis, when the vessel has participated in a pool during the period and the amount of pool revenue for the month can be estimated reliably. We receive estimated vessel earnings based on the known number of days the vessel has participated in the pool, the contract terms, and the estimated monthly pool revenue. On a quarterly basis, we receive a report from the pool which identifies the number of days the vessel participated in the pool, the total pool points for the period, the total pool revenue for the period, and the calculated share of pool revenue for the vessel. We review the quarterly report for consistency with each vessel s pool agreement and vessel management records. The estimated pool revenue is reconciled quarterly, coinciding with our external reporting periods, to the actual pool revenue earned, per the pool report. Consequently, in our financial statements, reported revenues represent actual pooled revenues. While differences do arise in the performance of these quarterly reconciliations, such differences are not material to total reported revenues.

The following are accounting policies we plan to adopt going forward.

Vessels and depreciation

We record the value of our vessels at their cost (which includes acquisition costs directly attributable to the vessel and expenditures made to prepare the vessel for its initial voyage) less accumulated depreciation. We depreciate our vessels on a straight-line basis over their estimated useful lives, estimated to be 25 years from date of initial delivery from the shipyard. Depreciation is based on cost less the estimated residual value which is the lightweight tonnage of each vessel multiplied by scrap value per ton. The scrap value per ton is estimated taking into consideration the historical four year average scrap market rates at the balance sheet date with changes accounted for in the period of change and in future periods. We believe that a 25-year depreciable life for our vessels is consistent with that of other ship owners and with its economic useful life. An increase in the useful life of the vessel or in its residual value would have the effect of decreasing the annual depreciation charge and extending it into later periods. A decrease in the useful life of the vessel or in its residual value would have the effect of increasing the annual depreciation charge. However, when regulations place limitations over the ability of a vessel to trade on a worldwide basis, or when the cost of complying with such regulations is not expected to be recovered, we will adjust the vessel s useful life to end at the date such regulations preclude such vessel s further commercial use. The carrying value of our vessels does not represent the fair market value of such vessels or the amount we could obtain if we were to sell any of our vessels, which could be more or less.

Impairment of long-lived assets

We follow Accounting Standards Codification (ASC) Subtopic 360-10, Property, Plant and Equipment (ASC 360-10), which requires impairment losses to be recorded on long-lived assets used in operations when indicators of impairment are present and the undiscounted cash flows estimated to be generated by those assets are less than their carrying amounts. If indicators of impairment are present, the Company performs an analysis of the anticipated undiscounted future net cash flows of the related long-lived assets. If the carrying value of the related asset exceeds the undiscounted cash flows, the carrying value is reduced to its fair value. Various factors including anticipated future charter rates, estimated scrap values, future drydocking costs and estimated vessel operating costs are included in this analysis.

Liquidity and Capital Resources

We were formed for the purpose acquiring and operating latest generation of newbuilding drybulk carriers with fuel-efficient specifications and carrying capacities of greater than 30,000 dwt. As of the date of this prospectus, our Operating Fleet consists of 19 drybulk vessels (of which 18 are vessels that we charter-in and one is a recently delivered Kamsarmax vessel from our Newbuilding Program) and our Newbuilding Program consists contracts for the construction of 79 drybulk vessels with established shipyards in Japan, China, South Korea and Romania, which we have agreed to acquire for an aggregate purchase price of $3,070.8 million, including 29 Ultramax vessels, 22 Kamsarmax vessels and 28 Capesize vessels. We also have one time charter-in contract that is scheduled to commence during the first half of 2015. In addition, as part of our growth strategy we may also acquire modern secondhand vessels, or charter in additional vessels. Our business is capital intensive and we intend to pay for these vessels with a combination of proceeds from the issuance of bonds, cash generated from operations, equity capital, and borrowings from commercial banks under one or more secured credit facilities. We anticipate that such credit agreements will bear interest based on LIBOR. We expect to rely on operating cash flows as well as equity offerings and long-term borrowings under secured credit facilities to implement our growth plan and dividend policy. We believe that our current cash balance as well as operating cash flows and available borrowings under our credit facilities, including our $67.5 Million Senior Secured Credit Facility, our $330.0 Million Senior Secured Credit Facility, our $39.6 Million Senior Secured Credit Facility and our Proposed $540.0 Million Senior Secured Credit Facility, will be sufficient to meet our liquidity needs for the next 12 months.

The vessels in our Newbuilding Program are expected to be delivered to us between the third quarter of 2014 and the third quarter of 2016. These construction projects are subject to risks of delay or cost overruns inherent in any large construction project from numerous factors, including shortages of equipment, materials or skilled labor, unscheduled delays in the delivery of ordered materials and equipment or shipyard construction, failure of equipment to meet quality and/or performance standards, financial or operating difficulties experienced by equipment vendors or the shipyard, unanticipated actual or purported change orders, inability to obtain required permits or approvals, unanticipated cost increases between order and delivery, design or engineering changes and work stoppages and other labor disputes, adverse weather conditions or any other events of force majeure. Significant cost overruns or delays could adversely affect our financial position, results of operations and cash flows. Additionally, failure to complete a project on time may result in the delay of revenue from that vessel.

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As of June 30, 2014, we have made total yard payments in the amount of $764.1 million and we have remaining yard installments in the amount of $2,338.8 million before we take delivery of the vessels. We had, as of June 30, 2014, a cash balance of $346.0 million to fund future newbuilding commitments, however, a significant portion of our remaining commitments are currently unfunded. If we are not able to borrow additional funds, raise other capital or utilize available cash on hand, we may not be able to acquire these newbuilding vessels, which could have a material adverse effect on our business, financial condition, results of operations and cash flows. If for any reason we fail to make a payment when due, which may result in a default under our newbuilding contracts, or otherwise fail to take delivery of our newbuild vessels, we would be prevented from realizing potential revenues from these vessels, we could also lose all or a portion of our yard payments that were paid by us and we could be liable for penalties and damages under such contracts.

In addition, in the event the shipyards do not perform under their contracts and we are unable to enforce certain refund guarantees with third party banks for any reason, we may lose all or part of our investment, which would have a material adverse effect on our results of operations, financial condition and cash flows.

Equity Private Placements

Upon our formation in March 2013, we issued 1,500 common shares to SSH. Between July 1, 2013 and July 16, 2013, we issued and sold 31,250,000 common shares, par value $0.01 per share, for net proceeds of $242.8 million; on September 24, 2013, we issued and sold an additional 33,400,000 common shares for net proceeds of $290.5 million; and on October 31, 2013, we issued and sold an additional 32,590,411 common shares for net proceeds of $291.0 million, in Norwegian private placement transactions exempt from registration under the Securities Act.

Initial Public Offering

In December 2013, we completed our underwritten initial public offering of 31,300,000 common shares at $9.75 per share, and in January 2014, the underwriters in the initial public offering exercised their option to purchase an additional 4,695,000 common shares. We received net proceeds of $326 million, in aggregate, which was used to fund newbuilding vessel capital expenditures.

Credit Facilities

For a description of our $67.5 Million Senior Secured Credit Facility, our $330.0 Million Senior Secured Credit Facility, our $39.6 Million Senior Secured Credit Facility, and our Proposed $540.0 Million Senior Secured Credit Facility, including the loan covenants thereto, please see the section herein entitled Description of Other Indebtedness.

Dividend Policy

Initially, we do not intend to pay dividends to the holders of our common shares but rather to invest our available cash in the growth of our fleet and development of our business. We will continue to assess our dividend policy and our board of directors may determine it is in the best interest of the Company to pay dividends in the future. Upon the delivery of a larger number of the vessels in our Newbuilding Program and depending on prevailing charter market conditions, our operating results and capital requirements and other relevant factors, our board of directors will re-evaluate our dividend policy. Please see the section of this prospectus entitled Dividend Policy.

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Contractual Obligations

The following table sets forth our estimated current contractual obligations as of June 30, 2014, for our newbuilding commitments through the expected delivery dates of the vessels and vessels that we have time chartered-in.

(in millions of U.S. dollars)	Less than 1 year	1 to 3 years	3 to 5 years	More than 5 years
Vessels Under Construction (1)	$ 785.0	$ 1,553.7	$ -	$ -
Time Charter-in Commitments (2)	61.2	55.9	5.5	-

(1) These are estimates only and are subject to change as construction progresses.
(2) Excludes option periods and time charters-in that are based on floating rates.

This table does not include (i) vessel management fees and expenses, which will be incurred starting with the delivery of the first vessel we time chartered-in and (ii) payments that we expect to make under our credit facilities on which we have not yet drawn down.

Off-Balance Sheet Arrangements

We are committed to make payments for our vessels that we time charter-in. The future minimum rental payments under these vessels that we have time chartered-in are disclosed above in the table under Contractual Obligations.

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THE DRY BULK SHIPPING INDUSTRY

Except as otherwise indicated, the statistical information and industry and market data contained in this section (the DATA) is based on or derived from statistical information and industry and market data collated and prepared by SSY Consultancy & Research Ltd (SSY). The data is based on SSY s review of such statistical information and market data available at the time (including internal surveys and sources, independent financial information, independent external industry publications, reports or other publicly available information). Due to the incomplete nature of the statistical information and market data available, SSY has had to make some estimates where necessary when preparing the data. The data is subject to change and may differ from similar assessments obtained from other analysts of shipping markets. Whilst reasonable care has been taken in the preparation of the data, SSY has not undertaken any independent verification of the information and market data obtained from published sources.

Industry Overview

Dry bulk shipping mainly comprises the shipment of minerals (such as iron ore and coal), other industrial raw materials and various agricultural products. Of these, the major cargoes are iron ore, coal and grain. The remaining minor bulk cargoes include steel products, bauxite/alumina, nickel ore, cement, petroleum coke, forest products, fertilizers and non-grain agricultural products (e.g. sugar).

Charterers in the dry bulk shipping industry range from cargo owners (such as mining companies and grain houses) to end-users (such as steel producers and power utilities) and also include a number of different trading companies and ship operators.

In 2013 total international seaborne dry bulk trade reached an estimated new annual record of 3.97 billion tonnes. This was up by an estimated 7.1% from 2012 and above the compound annual average growth rate (CAGR) from 2009 to 2013, during which time total annual trade rose by an estimated 33.0%. With the exception of 2009, when the global economy was in recession, seaborne dry bulk trade has recorded positive annual growth in every year since 1998.

World Seaborne Dry Bulk Trade

(million tonnes)

Cargo/Year	2008	2009	2010	2011	2012	2013	2008-13% Growth	CAGR
Major Bulks	**1998**	**2109**	**2326**	**2464**	**2607**	**2803**	**40%**	**7%**
Iron Ore	847	939	1036	1107	1138	1240	46%	8%
Coal	829	849	958	1020	1117	1197	44%	8%
Grains	321	321	332	338	352	366	14%	3%
Minor Bulks	**985**	**868**	**977**	**1058**	**1096**	**1162**	**18%**	**3%**
Total	**2983**	**2977**	**3303**	**3523**	**3703**	**3965**	**33%**	**6%**

Totals may not add due to rounding

While only partial dry bulk trade data are available for the first half of 2014, when aggregated they show further positive year-on-year growth, albeit unevenly distributed between the various dry bulk cargo types, as described below.

Cargo Types

Iron ore: The key raw material for steelmaking, iron ore trade has surged in recent years on the back of unprecedented Chinese import demand to be the single largest seaborne dry bulk cargo, totalling an estimated

1,240 million tonnes (Mt) in 2013. This was up by 9% on the 2012 total, 46% higher than in 2008 and 132% above the corresponding total in 2003. In addition to China, which as described elsewhere in this section has become the dominant importer accounting for approximately two-thirds of seaborne imports in 2013, the main import markets for iron ore are Japan, Western Europe and South Korea. Exports are dominated by Australia and Brazil, which together account for over 75% of the seaborne market. Other exporters include Canada, India, South and West Africa. A majority of iron ore cargoes are carried by Capesize vessels given the favourable unit economics, but such is the diversity of iron ore supply sources to China with 17 different countries supplying five Mt or more of iron ore to China in 2013, according to PRC customs statistics that there are also employment opportunities in the smaller vessel sizes.

Trade growth in the first half of 2014 was, however, focused on the key Capesize load areas of Australia and Brazil, with their exports approximately 20% higher than in the same period of 2013, according to government data.

Coal: At an estimated 1,197 million tonnes in 2013, global seaborne coal trade has expanded at a CAGR of 8% between 2008 and 2013. It is comprised of two main categories: (1) steam coal (which is chiefly used for electricity generation, but also by industrial users, such as the cement industry) and (2) coking coal (a key input for blast furnace steelmaking). Traditionally dominated by import demand from Japan and Western Europe, the past five years have seen China and India emerge as key drivers of incremental world import growth. The leading exporter of coking coal is Australia, followed by the US and Canada.

Indonesia is the largest exporter of steam coal, ahead of Australia, the former Soviet Union, Colombia, South Africa and the US. Within the past ten years, China has been transformed from one of the world s major steam coal exporting nations to the single largest importer, such has been the strength of the country s domestic demand for power generation. Indian imports have also grown rapidly during the past five to ten years to surpass those of Taiwan, South Korea and Japan. Western Europe remains a major import market, while Latin America has grown in importance as a coal import generator. Although investments in new port facilities have enabled the participation of Capesize vessels in the Asia-led coal trade growth in recent years, it has chiefly benefitted demand for Panamax and Handymax type vessels.

Available export data for the first half of 2014 indicate a year-on-year decline of approximately 2% in global seaborne coal trade, chiefly due to some softening in import demand from China and several European countries.

Grains: Seaborne grain trade, which totalled approximately 366 Mt in 2013, is comprised of wheat, coarse grains (corn, barley, oats, rye and sorghum) and soyabeans/meal. Compared with the mineral cargoes, grains have generated slower, but still positive rates of annual trade growth over the past five years with an estimated CAGR of 3%. The grain trades do, however, remain an important source of freight market volatility due to both the seasonality of export flows and year-on-year variations in crop surpluses and deficits. For example, improved harvests in the US and Black Sea region were key to the estimated 21% year-on-year growth in combined shipments from the main grain exporting areas in the first half of 2014.

Soya is the largest of the three main categories of grain trade with the US, Brazil and Argentina the leading export countries. The principal markets are in Europe and Far East Asia with China the world s single largest soyabean importer. Shipments are dominated by Panamax and Handymax vessels. Wheat and coarse grains are also primarily carried by mid-size vessels with the US, Canada, Russia, Ukraine, Argentina, Australia and the EU the main exporting regions. In addition to Far East Asia and Europe, the Middle East, Africa and Latin America are all significant import markets.

Minor Bulks: A diversity of cargo types are covered under this heading with different sets of demand drivers. Nevertheless, together at more than 1 billion tonnes per annum these trades represent a major source of employment for the smaller Handysize and Handymax vessels. Several minor bulk cargoes, including steel products and cement suffered an especially severe decline in trade volumes during the global financial crisis. The subsequent recovery in overall minor bulk trade volumes to an estimated all-time high in 2013 has been shaped by some different drivers than during the pre-2008 period, with a greater emphasis on Chinese imports of industrial raw materials, such as bauxite and nickel ore. The estimated CAGR for minor bulk volumes for the period from 2008 to 2013 was 3%.

A key development for the minor bulk trades in 2014 has been the implementation of export restrictions on unprocessed mineral ores by the Indonesian government in January, which have effectively banned the country s exports of bauxite and nickel ore (which totalled a combined 121 Mt in 2013). In contrast, the first half of 2014 saw a positive contribution to minor bulk trade from steel products, where the combined exports from China, Japan, South Korea, Brazil and the EU were 15% higher than during the same period in 2013.

Demand for Dry Bulk Shipping

Dry bulk trade is a function of levels of a) economic activity, b) the industrialization/urbanization of developing countries, c) population growth (plus changes in dietary habits) and d) regional shifts in cargo supply/demand balances (e.g. due to the development of new export/import capacity or depletion/development of mineral reserves). The distances shipped chiefly reflect regional commodity surpluses and deficits. Generally, the more concentrated the sources of cargo supply, the greater the average distance shipped.

Ship demand is determined by the overall volumes of cargo moved and the distance that these are shipped (i.e. tonne-mile demand), as well as changes in vessel efficiency. These changes may be caused by such factors as (1) vessel speed (in the high fuel cost/low freight rate environment of recent years, there has been an incentive for shipowners to reduce speed and so lower fuel consumption); (2) port delays (which have been a common occurrence in the last ten years as inland and port logistics in several key export areas have struggled to meet surging global demand) and (3) laden to ballast ratios - i.e. how much time vessels spend sailing empty on re-positioning voyages (ballasting has also been on the increase over the last ten years due to the widening imbalance in cargo flows between the Atlantic and Pacific Basins).

World seaborne dry bulk trade followed a steady underlying upward trend during the 1980s and 1990s. Compound annual average growth in the major dry bulk cargoes over this period was an estimated 2.5%, before accelerating sharply to 6.3% in the decade from 2000-09 and to an estimated 7.4% in 2010-13.

Both the growth in dry bulk trade volumes since the global financial crisis of 2008/09 and the preceding acceleration in the underlying rate of expansion in cargo movements were primarily due to the rapid industrialization and urbanization of China. From approximately 130 Mt in 2000, Chinese dry bulk imports had increased more than ten-fold by 2013, as illustrated in the accompanying chart. Such an expansion has been facilitated by investments in new mining and port facilities in key exporting areas around the world in response to Chinese-driven rises in commodity prices.

Chinese customs data show that the country s dry bulk imports increased by 169 Mt in 2013 to a new annual record of 1,473 Mt. Corresponding import statistics for the period January-July 2014 annualize at 1,528 Mt, or 3.7% above last year s total.

The table below provides a more detailed comparison of China s dry bulk imports between 2008 and 2013, together with annualized data for 2014. It confirms iron ore s role as the leading source of import growth. This reflects not only increases in domestic steel production (and, therefore, iron ore consumption) to meet the needs of an industrializing and urbanizing economy, but also the substitution of higher-quality imported iron ore for lower-quality domestic supplies. This growth has mainly been to the benefit of Capesize vessels, hauling cargoes from West Australia and Brazil.

The table also highlights high rates of growth across a range of other cargoes between 2008 and 2013, such as coal, grains and some of the key minor bulks. Indonesia and Australia are the primary sources of Chinese coal imports, while in the grain trades increased Chinese demand for soyabeans from Latin America and the US has boosted tonne-mile demand for Panamax and Supramax vessels.

Indonesia had been the dominant supplier of bauxite and nickel ore to China until January 2014 s export restrictions. With Chinese buyers struggling to find alternative supplies from elsewhere and drawing on inventories accumulated over the course of 2013, the country s total imports of both bauxite and nickel ore have fallen sharply. This is illustrated in the table s final column, which highlights how this year s growth in China s dry bulk imports has been dominated by iron ore and, to a lesser extent, grains.

Chinese Dry Bulk Imports (Million Tonnes)

	2008	*2013*	*CAGR*	*2014a*
Iron Ore	444.0	820.3	+13%	929.5
Steel Products	15.7	14.6	-1%	14.8
Coal*	45.8	327.1	+48%	315.5
Bauxite/alumina	30.6	75.4	+20%	44.8
Grains	39.4	78.0	+15%	91.2
Fertilizer	6.3	7.9	+5%	9.5
Other**	47.1	149.5	+26%	122.9
Total of above	**628.9**	**1472.8**	+19%	**1528.2**

* Includes lignite

** Includes mineral ores (e.g. nickel), pulp/woodchip and petroleum coke.

Source: Chinese Customs

Outside of China, most of the additional growth in dry bulk cargo import demand during the past five to six years has been generated by other Asian economies. For example, Indian coal imports are estimated to have risen from 62 Mt in 2008 to 183 Mt in 2013, reflecting the strength of demand from electricity generators and the cement and steel industries. Although India has added several Capesize coal import terminals in recent years, a majority of the coal cargoes arriving in the country are shipped by Supramax, Panamax and Kamsarmax vessels. More established Asian import markets, such as South Korea, have also contributed to the region s import growth with the increase in Korean imports of coal and iron ore between 2008 and 2013 (of 41 Mt) more than offsetting the corresponding decrease in Japanese imports (of approximately 5 Mt).

In contrast, European mineral imports have staged only a partial recovery from their cyclical lows in 2009 and have remained below their 2007 totals, partly due to the ongoing financial crisis in the Eurozone. Consequently, Far East Asia s share of world seaborne major bulk imports is estimated to have climbed above 75% by 2013 from approximately 60% in the middle of the last decade and 50-55% in 2000.

As a result, fastest dry bulk trade growth has been seen within the Pacific Basin, which has been supplemented by increases in fronthaul trade from the Atlantic to the Pacific (chiefly iron ore on Capesize vessels and grains on Panamaxes and Supramaxes).

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Fleet

The cargoes outlined above are predominantly carried by dry bulk carriers of more than 10,000 dwt. Dry bulk carriers are single-decked ships that transport dry cargoes in bulk form (i.e. loose within cargo holds, rather than in bags, crates or on pallets). As of mid-August 2014, the total fleet of 10,000+ dwt dry bulk carriers numbered approximately 9,956 vessels of 737.9 million deadweight (Mdwt).

This fleet is divided into four principal size segments: Handysize (10-39,999 dwt), Handymax (40-64,999 dwt), Panamax (65-99,999 dwt) and Capesize (100,000+dwt). Aside from size, the main distinction between dry bulk vessel types is whether they are geared (i.e. equipped with cranes for loading/discharge) or gearless. The main characteristics of these four vessel types are summarized below, while the accompanying table summarizes the current structure of the fleet by age and size. It shows that in terms of deadweight capacity, the Capesize sector is the largest with 41.0% of the mid-August 2014 total, followed by Panamaxes at 25.7%, Handymaxes at 21.9% and Handys at 11.4%.

Handysize (10,000-39,999dwt): These ships carry the widest range of cargoes of any dry bulk size segment and are the most dependent on the minor bulks for employment. They are usually equipped with cargo-handling gear (cranes or derricks) and are widely used on routes to and from draft-restricted ports that a) cannot receive larger ships and b) often lack their own land-based cargo-handling equipment. Many such loading or discharge facilities are located in developing nations. Due to the limited scale economies that these vessels offer, compared to larger tonnage, many of these ships are extensively employed on intra-regional, shorter-haul trades. Special designs of ship are associated with the carriage of such cargoes as steel products and logs (i.e open-hatch and log-fitted vessels); while some variation also exists in terms of cargo-handling equipment, e.g. grab-fitted tonnage possessing scoops that facilitate easier unloading of certain cargo types.

Handymax (40,000-64,999dwt): This segment of the dry bulk carrier fleet contains three distinct sub-categories the traditional Handymax size (40-49,999dwt), the Supramax size (50-59,999dwt) and the Ultramax size (60-64,999 dwt). There are some Ultramax newbuilding designs of above 65,000 dwt, but as these are much fewer in number than existing gearless vessels of 65-69.9 kdwt, they currently fall in SSY s Panamax size range. Despite their increased size, these vessels retain a high degree of trading flexibility as their cargo gear enables them to load and/or discharge at ports with limited facilities. They are more widely deployed on longer-haul routes than Handysizes (due to the greater scale economies that they offer). Whereas the traditional Handymax types have gained market share from the sub-40,000 dwt fleet of Handysizes over the past twenty years, the new generation of Supramax and Ultramax vessels are also competing for business on Panamax routes (e.g. grains from Latin America).

Panamax (65-99,999 dwt): The strict definition of a Panamax bulk carrier is a ship able to transit the Panama Canal fully laden. However, in recent years this definition has become blurred as (1) only a minority of the vessels in this size range pass through the Panama Canal in any twelve-month period and (2) shipyards have developed new designs in anticipation of the Panama Canal s expanded dimensions from late 2015/early 2016 onwards. At present, the Panama Canal can accommodate ships of maximum beam (i.e. extreme vessel breadth) of 32.3 metres, maximum length overall (LOA) of 294.1m and maximum draft of 12m tropical fresh water (TFW). Post-enlargement, these limits will increase to 49m beam, 366m LOA and 15.2m TFW draft. For the aforementioned reasons our fleet definition stretches from 65,000 to 99,999 dwt, encompassing three main sub-types: traditional Panamaxes (70-79,999 dwt), Kamsarmaxes (82/83,000dwt, which are currently the largest bulk carrier to transit the Panama Canal fully laden) and post-Panamaxes (85-99,999 dwt). The baseload demand for these vessel types is provided by coal and grain cargoes, although they also participate in a number of other trades (including iron ore, bauxite and fertilizers). Only a small minority of vessels in this size range are equipped with cargo gear as most of the ports served have well developed cargo loading or discharge terminals.

Capesize (100,000+dwt): These ships are almost exclusively deployed on the iron ore and coal trades, which benefit most from their scale economies. There are three main sub-types: small Capes (100-119,999 dwt), standard Capes (160-209,999 dwt, which are mainly concentrated between 170,000 dwt and 180,000 dwt, but also include Newcastlemaxes of 200-209,999 dwt) and Very Large Ore Carriers (220,000 dwt and above).

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Dry Bulk Carrier Fleet by Size/Age (Million Dwt):

As at mid-August 2014

Built/Dwt	*10-39,999*	*40-64,999*	*65-99,999*	*100,000+*	*Total*
Pre-1990	12.1	7.9	4.9	3.4	28.3
1990-94	3.3	5.7	9.3	25.4	43.8
1995-99	9.7	15.8	22.1	27.5	75.1
2000-04	7.8	19.3	25.4	26.4	78.9
2005-4-09-	13.8	33.4	34.6	59.5	141.2
2010-14	37.7	79.2	93.4	160.4	370.7
Total Fleet	**84.4**	**161.3**	**189.7**	**302.5**	**737.9**
Avg Age	**11 Yrs**	**8 Yrs**	**8 Yrs**	**8 Yrs**	**8 Yrs**

Totals may not add due to rounding

Ownership

Unlike other specialist areas of the world shipping fleet, ownership in the dry bulk segment is highly fragmented, with SSY s database showing approximately 2,000 different owners. The largest 50 owners account for approximately 36-37% of the total dry bulk carrier fleet in terms of deadweight carrying capacity, but this includes a large number of Chinese-flagged vessels that will trade on domestic, as well as international, routes.

While such analysis tends to understate levels of market concentration, due to the operation of vessel pools and chartered in fleets, the dry bulk segment is sufficiently competitive to ensure that vessel spot market earnings are extremely responsive to fluctuations in the supply/demand balance both globally and regionally.

Supply of Dry Bulk Shipping

The supply of dry bulk carriers is fundamentally determined by the delivery of new vessels from the world s shipbuilding industry and the removal of older vessels, mainly through demolition.

Newbuilding deliveries not only reflect the demand from shipowners for new tonnage, but also available shipyard capacity. Following a sharp upswing in demand for new vessels in all of the main sectors of the commercial shipping industry during the last decade, and an accompanying rise in shipbuilding prices to record levels in 2007/8, there was a massive China-led expansion in world shipbuilding capacity. In the case of the dry bulk sector, annual newbuilding deliveries surged from 24.4 Mdwt in 2008 (and an average of 19.1 Mdwt p.a. in 2000-07 inclusive) to 44.2 Mdwt in 2009, 79.7 Mdwt in 2010 and a peak of 99.4 Mdwt in 2012.

The resulting impact on freight market balances and vessel earnings, as described elsewhere in this section, led to sharply reduced levels of dry bulk carrier ordering in 2011 and 2012, which started to be reflected in a slower pace of newbuilding deliveries in 2013. At 61.2 Mdwt, last year s annual total for newbuilding deliveries was the lowest since 2009, with the slowdown maintained into 2014 as deliveries of 31.6 Mdwt from January-July were 22% below the same period in 2013.

There was, however, a revival in dry bulk carrier newbuilding investments during 2013, which has continued in 2014 and reversed the downward trend in the newbuilding orderbook. These orders have been focussed on new, more fuel efficient ship designs, where shipyard descriptions offer significantly lower fuel consumption compared with existing vessels through a combination of new technology main engines and refinements of hull forms.

The rising costs of bunker fuels over the past five to ten years are illustrated in the accompanying chart, which is based on the Supramax vessel specifications used by the Baltic Exchange (30 tonnes per day at 14.0 knots

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laden/14.5 knots ballast) and estimated bunker prices in Singapore. This shows an increase at sea, at full speed, from approximately $5,000/day in 2003 to approximately $20,000/day in 2012. There has been some moderation in bunker prices since 2012, but vessel fuel costs remain at historically high levels. Furthermore, we would stress that (1) there is a wide variance in individual vessel fuel consumptions, even within the same size segments, and (2) that, as described earlier in this section, vessels have been operating at slower speeds in order to lower their daily fuel consumption and costs.

The accompanying table summarizes the confirmed dry bulk carrier orderbook as of mid-August 2014, by vessel size and scheduled year of delivery. These delivery dates can be subject to delay, with actual deliveries in recent years significantly lagging scheduled totals. For example, 2013 deliveries were an estimated 35% below the scheduled total as at 1st January 2013. At an estimated 156.4 Mdwt, the total tonnage on order represents approximately 21.2% of the existing fleet. This compares with 18.7% at the end of 2013, but remains far below the end-year highs of 56.0% in 2007, 57.2% in 2009 and 67.5% in 2008, as illustrated in the accompanying chart.

Dry Bulk Carrier Newbuilding Orderbook by Size Range (Million Dwt):

As at mid-August 2014

Delivery	**10-39,999**	**40-64,999**	**65-99,999**	**100,000+**	**Total**
2014	3.0	7.3	5.9	9.9	26.0
2015	8.0	19.7	14.1	26.5	68.2
2016	3.1	12.2	8.7	27.1	51.1
2017+	1.0	2.6	2.1	5.6	11.2
Total	**15.0**	**41.7**	**30.7**	**69.0**	**156.4**
% of Fleet	**17.8%**	**25.9%**	**16.2%**	**22.8%**	**21.2%**

Totals may not add due to rounding

Typically dry bulk carriers are scrapped between the ages of 25 and 30 years. Since the beginning of 2013, the average age of Handysize vessels scrapped has been 30 years, for Handymax 27 years, for Panamax 24-25 years and for Capes 23-24 years. However, demolition is not simply a function of the fleet s age profile. Several factors will influence an owners decision on whether to scrap older vessels, notably (1) actual and anticipated returns from the charter market, (2) the relative running costs of the vessel and (3) prospective expenditure at classification society surveys. For much of the decade 2000-09, returns from the dry bulk charter markets supported continued investment in vessel life extension and scrapping volumes fell to minimal levels. This, however, ensured an accumulation of older tonnage in the fleet and, as a result, demolition proved extremely responsive to a deterioration in freight market conditions. For instance, deletions from the dry bulk fleet rose from 3.5 Mdwt in 2008 to 14.7 Mdwt in 2009 and a new annual record of 35.1 Mdwt in 2012. Deletions in 2013 dropped to an estimated annual total of 21.7 Mdwt (which was still the third highest year on record) and were running at an annualized rate of 14.5 Mdwt in January-July 2014.

As the accompanying chart illustrates, record volumes of ship demolition did not prevent a marked acceleration in the rate of dry bulk carrier fleet supply growth. From 6-7% p.a. in 2005-08, net fleet growth leapt to 9.1% in 2009 and 16.6% in 2010 with further years of double-digit percentage growth following in 2011 and 2012, before slowing to approximately 5.8% in 2013 and an annualized 5.5% in the first seven months of 2014.

Demolition did, however, contribute to the uneven development of dry bulk carrier fleet supply over the past five to six years. In particular, the removal of elderly Handysize vessels, combined with the relatively modest newbuilding program in this sector compared with the other sizes, ensured that the 10-39,999 dwt fleet grew at an estimated CAGR of just 1.9% between 2008 and 2013, compared with 10.3% for 40-64,999 dwt Handymaxes, 11.9% for 65-99,999 dwt Panamaxes and 15.1% for 100,000+ dwt Capes. By comparison, in the first seven months of 2014, the annualized rate of growth in the Capesize fleet was 5.3%, behind Panamaxes at 7.7%, while the Handymax and Handysize fleets grew at 5.0% and 2.5%, respectively.

Since the end of 2008, the Handysize sector s share of total dwt capacity has fallen from an estimated 18% to 11.4% in mid-August 2014. By contrast, the share accounted for by 100,000+ dwt Capes has risen from 34.6% to 41.0% over the same period. The 65-99,999 dwt Panamax sector recorded a modest increase in its share, from 24.6% to 25.7%, and the 40-64,999 dwt Handymax sector recorded modest decline, from 22.8% to 21.9%.

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Despite the demolition of recent years, there remains 28.3 Mdwt of ships aged 25 years or older in the current dry bulk carrier fleet, with a further 43.8 Mdwt aged 20-24 years. Existing pre-1990 built ships are heavily concentrated in the Handysize and Handymax fleets, yet both the Capesize and Panamax sectors contain substantial concentrations of tonnage in the 20-25 year age range. As a result, 20+ year old vessels account for 18.3% of total Handysize dwt capacity, compared with 8.4% of Handymaxes, 7.5% of Panamaxes and 9.5% of Capes.

Charter Market & Freight Rates

The chartering of dry bulk vessels can take several different forms, the most typical of which are summarized below.

a) Single voyage (spot) charter

This involves the hire of a vessel for just one stipulated voyage, carrying a designated quantity of a named commodity. For most such charters, an individual ship is specified that will carry out the voyage to be undertaken. The terms of the agreement between the charterer and vessel owner usually defines the port (or ports) of cargo loading and discharge, the dates between which the cargo is to be loaded and the cargo-handling terms. The vessel owner will receive from the charterer a mutually agreed payment (normally quoted as a US$ per ton freight rate). In return, the shipowner pays all voyage expenses (e.g. the costs of fuel consumed on the voyage, plus port expenses), all operating costs (e.g. insurance and crewing of the vessel) and capital expenses (i.e. the servicing of any mortgage debt on the ship).

b) Contract of affreightment (COA)

Under a COA, the vessel owner and charterer agree terms for the carriage of a designated volume of a given commodity on a specified route (or routes), with such shipments being carried out on a regular basis. The agreement does not normally identify an individual ship that will be used to fulfil its terms but includes more

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general specifications on the vessels to be used (e.g. maximum age). Under the terms of a COA, freight is normally paid on an agreed US$ per ton basis, with the vessel owner then meeting all voyage, operating and capital costs incurred in the execution of such a charter.

c) Time charter

Under a time charter, the charterer takes the ship on hire for either (1) a trip between designated delivery and re-delivery positions or (2) for a designated period (e.g. twelve months). The freight rate agreed between the shipowner and charterer is in terms of a daily hire rate (in US dollars), rather than as a US$ per ton figure. For longer term period charters, this may escalate at a rate mutually agreed between vessel owner and charterer. Under the terms of such charters, the vessel owner meets the ship s operating and capital costs, with the charterer paying all variable voyage expenses (mainly fuel costs, plus port and canal dues). In addition, and unless otherwise stipulated in the charter agreement, the period charterer is able to trade the vessel to and from whichever loading and discharge ports that they choose, carrying whichever cargoes they prefer.

d) Bareboat charter

Under a bareboat charter, the vessel owner effectively relinquishes control of their ship to the charterer (usually for a period of several years). The shipowner receives an agreed level of remuneration (which may again escalate at a mutually agreed rate) for the duration of the charter and remains responsible for the vessel s capital costs. In return, the charterer assumes total control of the vessel, thereby becoming responsible for operating the ship and meeting all costs of such operation (e.g. crewing, repairs and maintenance), as well as the direct voyage expenses incurred (i.e. fuel costs, port expenses, etc) when it is trading.

Freight Rates

Freight rates are determined by the balance of tonnage demand and tonnage supply. Primarily as the result of record newbuilding deliveries, fleet utilization rates have dropped sharply from the peak levels of 2007, as illustrated by movements in key freight market indicators.

Given the diversity of routes and cargoes traded by the dry bulk fleet, freight market measures tend to focus on average worldwide spot earnings (expressed in US$/day). The most recognized of these measures are published on a daily basis by the Baltic Exchange in London. In addition to global averages for standard designs of Handysize (28,000 dwt), Supramax (52,450 dwt), Panamax (74,000 dwt) and Capesize (172,000 dwt) vessels, together with a number of component routes, the Baltic Exchange also publishes a daily composite Index for the entire dry bulk market (the BDI or Baltic Exchange Dry Index). The Baltic Exchange Capesize Index has been based on a 180,000 dwt design since May 6, 2014, but for a transitional period daily assessments are also being published for the previous 172,000 dwt vessel description.

From its all-time high of almost 12,000 points in May 2008, just prior to the global financial crisis, the BDI fell to below 700 points in December of the same year. After partial recovery in 2009, negative pressure on freight markets returned under the weight of sustained fleet supply growth. At 920 points in 2012, the BDI s annual average was the lowest since the 1980s. The corresponding 2013 level was 1,206 points, but this annual average obscured sharp differences between the first and second halves of 2013. From its lowest quarterly average since 1986 in the first quarter of 2013 (796 points), the BDI rose to its highest quarterly average for two years in the fourth quarter of 2013 (1,854 points) against the background of sharply reduced fleet supply growth and new peaks for dry bulk trade.

Volatility remains a feature of dry bulk spot markets due, in part, to fluctuations in cargo availability (such as Indonesian bauxite and nickel ore) and port congestion, as well as shifts in patterns of import demand. In the year to date, the BDI has ranged between 2,113 and 723 points, averaging 1,097 points, which is 21% higher than during the same period in 2013.

The first of the accompanying charts traces developments in representative twelve month time charter rates for the four main sizes from January 2002 to mid-August 2014, encompassing the all-time highs in vessel earnings and the subsequent slump in rates. The second chart looks in more detail at developments since the beginning of 2009. It shows that during the first quarter of 2014, Capesize period rates had strengthened to their highest levels since 2010, whereas Panamax and Supramax period rates were at their firmest since 2011. Despite some subsequent softening, they remain above the corresponding levels of a year ago in all four sizes. These are based on existing modern (i.e. under ten years of age) vessels. Within these individual size ranges, period rates will vary according to such factors as vessel age, size, fuel consumption and yard of build.

Although both charts show the extent to which vessel earnings in the different size ranges move broadly in tandem, they also highlight that the sharpness of market rises and falls vary in degree. Those size groups that carry the narrowest range of cargoes - or which are employed on the least number of routes - tend to experience the greatest variations in charter rates. Hence, in the dry bulk shipping sector, earnings of Capesizes have been prone to fluctuate to a far greater degree than those of smaller vessels. It appears that as the average size of Capesize has increased, so has its relative volatility compared with the other sizes.

A feature of recent freight market downswings has been the relative resilience of earnings in the Handymax and Handysize sectors compared with the larger vessel sizes. This can be partly attributed to the greater trading versatility offered by the cargo gear on Handymax types, but also relative rates of fleet supply growth.

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Asset Values

In addition to the global balance between the demand for new vessels and available shipbuilding capacity, newbuilding prices are also influenced by changes in vessel construction costs, due to such factors as movements in steel plate prices or exchange rates against the US dollar in key shipbuilding nations (principally China, Japan and South Korea).

A higher US dollar cost base helps to explain why oversupplied shipbuilding markets did not return newbuilding prices to their previous historic lows. For example, Panamax bulk carrier newbuilding prices in Japan fell from $56 million in the third quarter of 2008 to $29 million in the final quarter of 2012, which compares with an estimated $20 million in the first quarter of 2002. By the end of 2013 Japanese prices had climbed to a 38-month high of $35 million, chiefly as the result of recovering newbuilding demand, and remained at similar levels in the first seven months of 2014.

Secondhand values are primarily shaped by actual and anticipated earnings, newbuilding replacement costs (which are relevant for modern vessels) and residual scrap value (more relevant for older units). To an extent, prices are also influenced by the availability and cost of ship finance, as this will help to determine whether investors are able to realise their demand for new or secondhand vessels.

The accompanying charts compare the development of representative newbuilding, five and ten year old secondhand prices for Handysize, Handymax, Panamax and Capesize vessels since 2002. Individual vessel prices will vary according to such factors as specific size, age, cargo gear, yard of build and fuel consumption. Following the pattern of the charter markets, prices peaked between mid-2007 and mid-2008. Such was the shortage of shipbuilding capacity during that period - with a lengthening lead time between contracting and delivery - that demand for existing vessels with prompt delivery briefly created the abnormal situation in which secondhand vessels were priced at a premium to newbuildings.

Consequently, the percentage decline in secondhand prices from their peaks was more severe than for newbuildings. Nevertheless, prices did not fall back to their 2002 lows but instead showed a firmer trend from the beginning of 2013 to March 2014, during which time five year old values rose by an average of approximately 50%, led by a 60-70% increase in Capesize prices. The onset of weaker spot and period charter

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rates during the second quarter of 2014 began to erode secondhand values with five year old prices declining by an average of 10-15% between the end of March and the end of July. However, in all four of the main dry bulk sizes, secondhand values remain above their corresponding levels twelve months ago.

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BUSINESS

History and Development of the Company

Scorpio Bulkers Inc. was established on March 20, 2013 under the laws of the Republic of the Marshall Islands. In July 2013, we issued and sold 31,250,000 common shares (including 1,500 common shares issued in connection with our formation) for net proceeds of $242.8 million in the July 2013 Private Placement; in September 2013, we issued and sold an additional 33,400,000 common shares for net proceeds of $290.2 million in the September 2013 Private Placement; and in October 2013, we issued and sold an additional 32,590,411 common shares for net proceeds of $291.0 million in the October 2013 Private Placement. In December 2013, we completed our underwritten initial public offering of 31,300,000 common shares at $9.75 per share, and in January 2014, the underwriters in the initial public offering exercised their option to purchase an additional 4,695,000 common shares. In February 2014, we completed our offer to exchange unregistered common shares that were previously issued in Norwegian equity private placements (other than the common shares owned by affiliates of us) for common shares that were registered under the Securities Act of 1933, as amended, which we refer to as the Exchange Offer. Upon completion of the Exchange Offer, holders of 95,766,779 unregistered common shares validly tendered their shares in exchange for such registered common shares, representing a participation rate of 99.7%. On July 31, 2014, we delisted from the Norwegian OTC. Our common shares currently trade on the New York Stock Exchange under the symbol SALT.

Following the completion of this offering, we expect to have in excess of $ million of available cash. As of June 30, 2014, we have paid a total of $764.1 million in initial installment payments due under our shipbuilding contracts for our Newbuilding Program. We plan to finance the remaining contractual commitments of $2,338.8 million with the net proceeds received from this offering, cash on hand, cash flows from operations, borrowings under committed and proposed new secured credit facilities, and from capital raised in the public and private debt and equity markets. We cannot assure you that we will be successful in obtaining the financing necessary to fund all of our remaining contractual obligations under our shipbuilding contracts or will be able to take delivery of all the vessels we have agreed to acquire.

In addition, we plan to use all or substantially all of the net proceeds from this offering and the net proceeds from future equity or debt offerings or both, together with the amounts we expect to be available to us under our credit facilities, to fund installment payments due under our Newbuilding Program, and the remaining amounts, if any, for general corporate purposes and working capital. Our intention is to acquire additional latest generation drybulk carriers with fuel-efficient vessel specifications and carrying capacities of greater than 30,000 dwt, either directly from shipyards or from owners with existing newbuilding vessel contracts. We may also acquire secondhand vessels that meet our stringent vessel specifications. The timing of these vessel acquisitions will depend on our ability to identify suitable vessels on attractive acquisition terms. Although we may have the capacity to obtain additional financing, we intend to maintain moderate levels of leverage of not more than 60% of the value of our vessels collateralizing our indebtedness on a consolidated basis.

Business Overview

We are a newly formed international shipping company focused on acquiring and operating the latest generation newbuilding drybulk carriers with fuel-efficient specifications and carrying capacities of greater than

30,000 dwt. We believe that it is an opportune time to acquire these vessels because acquisition costs for these vessels are currently near the lowest average levels of the past 10 years. In addition, we believe that recent advances in shipbuilding design and technology should make these latest generation vessels more fuel-efficient than older vessels in the global fleet that compete with us for charters, providing us with a competitive advantage. Our fleet transports a broad range of major and minor bulk commodities, including ores, coal, grains, and fertilizers, along worldwide shipping routes, and are, or are expected to be, employed primarily in the spot market or in spot market-oriented pools of similarly sized vessels. As of the date of this prospectus, our operating fleet consists of 19 drybulk vessels, of which 18 are vessels that we charter-in and one is a recently delivered Kamsarmax vessel from our Newbuilding Program, with an aggregate carrying capacity of approximately 1.5 million dwt, which we refer to as our Operating Fleet. We also have one time charter-in contract that is scheduled to commence during the first half of 2015 and contracts for the construction of 79 newbuilding drybulk vessels at established shipyards in Japan, China, South Korea and Romania, which we have agreed to acquire for an aggregate purchase price of $3,070.8 million, including 29 Ultramax vessels, 22 Kamsarmax vessels and 28 Capesize vessels, each with a carrying capacity of between 60,000 dwt and 180,000 dwt and an aggregate carrying capacity of approximately 8.6 million dwt. We refer to these newbuilding vessels as our Newbuilding Program. We expect to take delivery of the vessels in our Newbuilding Program as follows: one vessel in 2014, 42 vessels in 2015 and 36 vessels in 2016. Until we have taken delivery of a larger number of the vessels in our Newbuilding Program, we do not anticipate earning a material amount of revenues from our operations.

Our primary objective is to profitably grow our business and increase shareholder value by focusing on latest generation drybulk carriers. We intend to leverage the relationships, expertise and reputation of the Scorpio Tankers and the Scorpio Group to manage, service and employ our fleet and to identify opportunities to expand our fleet through newbuildings and selective acquisitions.

Our Relationship with the Scorpio Group

We believe that one of our principal strengths is our relationship with Scorpio Tankers and the Scorpio Group of companies. Our vessel operations are managed under the supervision of our board of directors, by our management team and by members of the Scorpio Group of companies. We expect that our relationship with Scorpio Tankers and the Scorpio Group of companies will give us access to their relationships with major international charterers, lenders and shipbuilders. We will have access to Scorpio Group s customer and supplier relationships and their technical, commercial and managerial expertise, which we believe will allow us to compete more effectively and operate our vessels on a cost efficient basis. The Scorpio Group, through SSH, beneficially owns approximately 4.0% of our common shares, excluding the common shares to be issued pursuant to the Administrative Services Agreement. Please see Security Ownership of Certain Beneficial Owners and Management.

In addition to our relationship with Scorpio Tankers, we believe there are opportunities for us to benefit from operational, charterer and shipyard-based synergies due to our broader shared relationship with the Scorpio Group which includes:

- SSM, which provides vessel technical management services for 40 vessels owned by third-parties, including Scorpio Tankers, and provides us with the same services for all of our vessels.

- SCM, which provides vessel commercial management services for 100 vessels owned by third-parties, including Scorpio Tankers, and provides us with the same services for all of our vessels. SCM manages 75 vessels (excluding the vessels in our fleet) through the spot market-oriented Scorpio Group Pools, which currently include the Scorpio LR2 Pool, the Scorpio Panamax Tanker Pool, the Scorpio MR Pool, Scorpio Handymax Tanker Pool, the Scorpio Ultramax Pool, Scorpio Kamsarmax Pool and the Scorpio Capesize Pool.

SSH, which provides us and related entities with administrative services and services related to the acquisition of vessels.

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We can provide no assurance, however, that we will realize any benefits from our relationship with Scorpio Tankers or the Scorpio Group.

Emanuele Lauro, our Co-Founder, Chairman and Chief Executive Officer, is a member of the Lolli-Ghetti family which owns and controls SCM, our commercial manager, and SSM, our technical manager. These relationships, and other relationships between certain of our executive officers and members of the Scorpio Group, may create certain conflicts of interest between us, on the one hand, and other members of the Scorpio Group, including our commercial and technical manager, on the other hand. For example, our Chief Executive Officer, President, and Chief Operating Officer each participate in business activities not associated with us, including serving as members of the management team of Scorpio Tankers, and are not required to work full-time on our affairs. We expect that each of our executive officers devote a substantial portion of his business time to the completion of our Newbuilding Program and management of the Company. Additionally, our executive officers named above serve in similar positions in the Scorpio Group. This may create conflicts of interest in matters involving or affecting us and our customers, including in the chartering, purchase, sale and operation of the vessels in our fleet versus vessels managed by other members of the Scorpio Group. As result of these conflicts, it is not certain that these conflicts of interest will be resolved in our favor, and other members of the Scorpio Group, who have limited contractual duties, may favor their own or other owners interest over our interests. Please see Risk Factors Our Chief Executive Officer, President and Chief Operating Officer will not devote all of their time to our business, which may hinder our ability to operate successfully.

Our Competitive Strengths

We believe that we possess a number of competitive strengths in our industry, including:

Experienced management teams. Our Company s leadership has considerable depth of shipping industry expertise. Since 2003, under the leadership of Mr. Emanuele Lauro, our Co-Founder, Chairman and Chief Executive Officer, the Scorpio Group, together with Scorpio Tankers, has grown from an owner of three vessels in 2003 to an owner of 75 vessels, and an operator or manager of approximately100 vessels, as of August 28, 2014. Mr. Robert Bugbee, our Co-Founder, President and Director, also holds a senior management position within the Scorpio Group and is the President and a Director of Scorpio Tankers, has more than 27 years of experience in the shipping industry and was formerly the President and Chief Operating Officer of OMI, which was a publicly traded shipping company until its sale in 2007. Messrs. Lauro and Bugbee are supported by Mr. Cameron Mackey, Mr. Hugh Baker and Mr. Luca Forgione, who serve as our Chief Operating Officer, our Chief Financial Officer, and our General Counsel, respectively, of whom, Messrs. Mackey and Forgione also serve as members of the management team of Scorpio Tankers. Mr. Mackey is also a director of Scorpio Tankers. Messrs. Mackey, Baker and Forgione serve in similar positions in the Scorpio Group and have 20, 22, and 11 years of experience, respectively, in the shipping industry, and, with Messrs. Lauro and Bugbee, collectively have over 80 years of combined shipping experience, and have developed industry relationships with charterers, lenders, shipbuilders, insurers and other industry participants. In addition, our Chief Executive Officer has experience in the ownership and operation of dry bulk carriers, through the Scorpio Group, which has owned and operated several dry bulk carriers, and in the upstream and downstream supply chain of dry bulk commodities, as founder, Chief Executive Officer and Chairman of Scorpio Logistics Ltd. Our executive officers are not required to work full-time on our affairs and also perform services for other companies, including Scorpio Tankers. Initially, we expect that our executive officers will devote a substantial portion of their business time to the completion of our drybulk carrier acquisition program and management of the Company.

Attractive Fleet. The 79 drybulk carriers in our Newbuilding Program, including 29 Ultramax vessels, 22 Kamsarmax vessels and 28 Capesize vessels, are scheduled to be delivered to us between the third quarter or 2014 and the third quarter of 2016. In addition, we own one Kamsarmax vessel that was recently delivered to us from the shipyard. We believe that owning a modern, well-maintained fleet with fuel efficient specifications reduces operating costs, improves the quality of service we deliver and provides us with a competitive advantage in securing favorable time and spot charters with high-quality counterparties. We believe that it is an opportune time to acquire these latest generation, fuel-efficient drybulk vessels because acquisition costs for these vessels are currently near the lowest average levels of the past 10 years. In addition, we believe that recent advances in shipbuilding design and technology should make these latest generation vessels more fuel-efficient than older vessels in the global fleet that compete with us for charters, providing us with a competitive advantage.

Significant available liquidity to pursue acquisition and expansion opportunities. Following the completion of this offering, we expect to have at least $ million of available cash, including $346.0 million which is a portion of the net proceeds from the Equity Private Placements and our Initial Public Offering. We intend to use the substantial majority of our available cash, and borrowing capacity under the secured credit facilities we intend to enter, to pursue vessel acquisitions, including the vessels in our Newbuilding Program, consistent with our business strategy. We believe that our strong balance sheet, financing capacity and future access to capital will allow us to make opportunistic acquisitions at attractive prices.

Access to attractive acquisition and chartering opportunities. Scorpio Group, including Scorpio Tankers, has established strong global relationships with shipping companies, charterers, shipyards, brokers and commercial shipping lenders. We believe that the Scorpio Group s relationships with these counterparties and its strong sale and purchase track record and reputation as a creditworthy counterparty should provide us, as a member of the Scorpio Group, with access to attractive asset acquisitions, chartering and vessel financing opportunities.

High quality, cost efficient vessel opportunities. We believe that Scorpio Group s experience with the commercial and technical management of vessels and its reputation in the industry as an operator with high safety and quality operating standards will be important in establishing and retaining high quality charterers that are looking for reliable and responsible operators to meet their exacting standards for vessel chartering and day-to-day operation.

Our Business Strategies

Our primary objectives are to profitably grow our business and emerge as a successful owner and operator of drybulk vessels. The key elements of our strategy are:

Expanding our fleet through opportunistic acquisitions of high-quality vessels at attractive prices. We intend to acquire latest generation drybulk carriers with fuel-efficient specifications and carrying capacities of greater than 30,000 dwt through timely and selective acquisitions. We currently view this vessel class as providing attractive return characteristics given the relatively low vessel price levels. A key element to our acquisition strategy will be to acquire high-quality vessels at attractive prices. When evaluating acquisitions, we will consider and analyze, among other things, our expectation of fundamental developments in the drybulk shipping industry sector, the level of liquidity in the resale and charter market, the cash flow earned by the vessel in relation to its value, its condition and technical specifications with particular regard to fuel consumption, expected remaining useful life, the credit quality of the charterer and duration and terms of charter contracts for vessels acquired with charters attached, as well as the overall diversification of our fleet and customers. We believe that these circumstances combined with our management s knowledge of the shipping industry present an opportunity for us to grow our fleet at favorable prices.

Optimizing vessel revenues primarily through spot market exposure. The Baltic Dry Index, or the BDI, a daily average of charter rates for key drybulk routes published by the Baltic Exchange Limited, which has long been viewed as the main benchmark to monitor the movements of the drybulk vessel charter market and the performance of the entire drybulk shipping market, has recently increased from the record low levels of 647 in February 2012 to 755 on July 31, 2014. We intend to employ a chartering strategy to capture upside opportunities in the spot market. We may also use fixed-rate time charters as the charter market improves to reduce downside risks. There can be no assurance that the drybulk charter market will increase and the market could decline.

Focusing on drybulk carriers based on the experience and expertise of the Scorpio Group and our management team in the international shipping industry. We believe that major international commodity

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companies seek transportation partners that are financially stable and have a reputation for reliability, safety, and high environmental and quality standards. We intend to leverage the operational expertise and customer base of the Scorpio Group and the members of our management team in order to further expand these relationships with consistent delivery of superior customer service.

Minimizing operating and corporate expenses. Pursuant to the Master Agreement, SSM and SCM coordinates and oversees the technical and commercial management of our fleet, respectively. We believe that SSM and SCM will be able to provide these services at costs that are lower than what we could achieve by performing these functions in-house.

Maintain a strong balance sheet through moderate use of leverage. We plan to finance the remaining contractual commitments due under our Newbuilding Program and future vessel acquisitions with a mix of debt and equity, but intend to maintain moderate levels of leverage over time, even though we may have the capacity to obtain additional financing. By maintaining moderate levels of leverage of not more than 60% of the value of the vessels collateralizing our indebtedness, we expect to retain greater flexibility than our more leveraged competitors to operate our vessels under shorter spot or period charters. Charterers have increasingly favored financially solid vessel owners, and we believe that our expected balance sheet strength will enable us to access more favorable chartering opportunities, as well as give us a competitive advantage in pursuing vessel acquisitions from commercial banks and shipyards, which have also recently displayed a preference for contracting with well capitalized counterparties.

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Our Fleet

The following table summarizes key information about our Newbuilding Program and our Operating Fleet as of the date of this prospectus:

Newbuilding Program

Capesize

Vessel Name		Expected Delivery (1)	DWT	Shipyard
1	Hull H1309 TBN SBI Puro	Q1-15	180,000	Waigaoqiao
2	Hull H1310 TBN SBI Valrico	Q2-15	180,000	Waigaoqiao
3	Hull H1311 TBN SBI Maduro	Q3-15	180,000	Waigaoqiao
4	Hull H1364 TBN SBI Belicoso	Q4-15	180,000	Waigaoqiao
5	Hull H1365 TBN SBI Corona	Q1-16	180,000	Waigaoqiao
6	Hull H1366 TBN SBI Diadema	Q2-16	180,000	Waigaoqiao
7	Hull H1367 TBN SBI Estupendo	Q3-16	180,000	Waigaoqiao
8	Hull S1205 TBN SBI Camacho	Q1-15	180,000	Sungdong
9	Hull S1206 TBN SBI Montesino	Q2-15	180,000	Sungdong
10	Hull S1211 TBN SBI Magnum	Q2-15	180,000	Sungdong
11	Hull S1212 TBN SBI Montecristo	Q3-15	180,000	Sungdong
12	Hull S1213 TBN SBI Aroma	Q3-15	180,000	Sungdong
13	Hull S1214 TBN SBI Cohiba	Q4-15	180,000	Sungdong
14	Hull S1215 TBN SBI Habano	Q4-15	180,000	Sungdong
15	Hull S1216 TBN SBI Lonsdale	Q1-16	180,000	Sungdong
16	Hull S1217 TBN SBI Partagas	Q1-16	180,000	Sungdong
17	Hull S1218 TBN SBI Parejo	Q1-16	180,000	Sungdong
18	Hull S1219 TBN SBI Toro	Q2-16	180,000	Sungdong
19	Hull S1220 TBN SBI Tuscamina	Q2-16	180,000	Sungdong
20	Hull H1059 TBN SBI Churchill	Q4-15	180,000	Daewoo
21	Hull H1060 TBN SBI Perfecto	Q4-15	180,000	Daewoo
22	Hull H1061 TBN SBI Presidente	Q1-16	180,000	Daewoo
23	Hull H1062 TBN SBI Panatela	Q1-16	180,000	Daewoo
24	Hull H1063 TBN SBI Robusto	Q2-16	180,000	Daewoo
25	Hull HN1058 TBN SBI Behike	Q3-15	180,000	Daehan
26	Hull HN1059 TBN SBI Monterrey	Q4-15	180,000	Daehan
27	Hull HN1060 TBN SBI Macanudo	Q4-15	180,000	Daehan
28	Hull HN1061 TBN SBI Cuaba	Q1-16	180,000	Daehan
	Aggregate Capesize Newbuilding DWT		**5,040,000**	

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Kamsarmax

	Vessel Name	Expected Delivery [1]	DWT	Shipyard
1	Hull H1285 TBN SBI Charleston	Q3-14	82,000	Waigaoqiao
2	Hull S1680 TBN SBI Samba	Q1-15	84,000	Imabari
3	Hull S1681 TBN SBI Rumba	Q3-15	84,000	Imabari
4	Hull 1090 TBN SBI Electra	Q3-15	82,000	Yangzijiang
5	Hull 1091 TBN SBI Flamenco	Q3-15	82,000	Yangzijiang
6	Hull 1092 TBN SBI Rock	Q4-15	82,000	Yangzijiang
7	Hull 1093 TBN SBI Twist	Q1-16	82,000	Yangzijiang
8	Hull SS164 TBN SBI Salsa	Q3-15	81,600	Tsuneishi
9	Hull SS179 TBN SBI Merengue	Q1-16	81,600	Tsuneishi
10	Hull S1228 TBN SBI Capoeira	Q1-15	82,000	Hudong
11	Hull S1722A TBN SBI Conga	Q2-15	82,000	Hudong
12	Hull S1723A TBN SBI Bolero	Q2-15	82,000	Hudong
13	Hull S1229 TBN SBI Carioca	Q2-15	82,000	Hudong
14	Hull S1724A TBN SBI Sousta	Q3-15	82,000	Hudong
15	Hull S1725A TBN SBI Reggae	Q1-16	82,000	Hudong
16	Hull S1726A TBN SBI Zumba	Q1-16	82,000	Hudong
17	Hull S1231 TBN SBI Macarena	Q1-16	82,000	Hudong
18	Hull S1735A TBN SBI Parapara	Q1-16	82,000	Hudong
19	Hull S1736A TBN SBI Mazurka	Q2-16	82,000	Hudong
20	Hull S1230 TBN SBI Lambada	Q3-15	82,000	Hudong
21	Hull S1232 TBN SBI Swing	Q2-16	82,000	Hudong
22	Hull S1233 TBN SBI Jive	Q3-16	82,000	Hudong
Aggregate Kamsarmax Newbuilding DWT			**1,807,200**	

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Ultramax

	Vessel Name	Expected Delivery [1]	DWT	Shipyard
1	Hull 1907 TBN SBI Hera	Q2-16	60,200	Mitsui
2	Hull 1906 TBN SBI Zeus	Q2-16	60,200	Mitsui
3	Hull 1911 TBN SBI Poseidon	Q3-16	60,200	Mitsui
4	Hull 1912 TBN SBI Apollo	Q3-16	60,200	Mitsui
5	Hull S870 TBN SBI Echo	Q3-15	61,000	Imabari
6	Hull S871 TBN SBI Tango	Q3-15	61,000	Imabari
7	Hull S-A098 TBN SBI Achilles	Q1-16	61,000	Imabari
8	Hull S-A089 TBN SBI Cronos	Q1-16	61,000	Imabari
9	Hull S-A090 TBN SBI Hermes	Q1-16	61,000	Imabari
10	Hull NE180 TBN SBI Bravo	Q1-15	61,000	Nacks
11	Hull NE181 TBN SBI Antares	Q1-15	61,000	Nacks
12	Hull NE182 TBN SBI Maia	Q3-15	61,000	Nacks
13	Hull NE183 TBN SBI Hydra	Q3-15	61,000	Nacks
14	Hull NE194 TBN SBI Hyperion	Q2-16	61,000	Nacks
15	Hull NE195 TBN SBI Tethys	Q2-16	61,000	Nacks
16	Hull DE018 TBN SBI Leo	Q1-15	61,000	Dacks
17	Hull DE019 TBN SBI Lyra	Q2-15	61,000	Dacks
18	Hull DE020 TBN SBI Subaru	Q2-15	61,000	Dacks
19	Hull DE021 TBN SBI Ursa	Q3-15	61,000	Dacks
20	Hull CX0610 TBN SBI Athena	Q1-15	64,000	Chengxi
21	Hull CX0651 TBN SBI Pegasus	Q3-15	64,000	Chengxi

22 Hull CX0652 TBN SBI Orion	Q4-15		64,000	Chengxi
23 Hull CX0612 TBN SBI Thalia	Q4-15		64,000	Chengxi
24 Hull CX0653 TBN SBI Hercules	Q1-16		64,000	Chengxi
25 Hull CX0627 TBN SBI Perseus	Q1-16		64,000	Chengxi
26 Hull CX0654 TBN SBI Kratos	s"> Q2-16Estimated fair value of Hilltop existing investment in SWS			74,639
Total Preliminary Estimated Merger Consideration		$366,563		

(1) The estimated cash distribution to SWS common stockholders equals the cash portion of the Merger Consideration of $1.94, multiplied by 40,288,000 shares of SWS common stock exchanged upon closing of the merger.

3. Preliminary Estimated Merger Consideration Allocation

Under the acquisition method of accounting, the total merger consideration is allocated to the acquired tangible and intangible assets and assumed liabilities of SWS based on their estimated fair values as of the closing of the SWS Merger. If the fair value of net assets purchased exceeds the merger consideration given, a "bargain purchase gain" is recognized. If the merger consideration given exceeds the fair value of the net assets received, goodwill is recognized.

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The allocation of the estimated merger consideration is preliminary because the proposed merger has not yet been completed. The preliminary allocation is based on estimates, assumptions, valuations, and other studies which have not progressed to a stage where there is sufficient information to make a definitive allocation. Accordingly, the merger consideration allocation and unaudited pro forma adjustments will remain preliminary until Hilltop management determines the final merger consideration and the fair values of assets acquired and liabilities assumed. The final determination of the merger consideration allocation is anticipated to be completed as soon as practicable after the completion of the merger and will be based on the price of Hilltop's common stock immediately prior to the effective time of the SWS Merger. The final amounts allocated to assets acquired and liabilities assumed could differ significantly from the amounts presented in the unaudited pro forma condensed combined financial statements.

The total preliminary estimated merger consideration as shown in the table above is allocated to SWS's tangible and intangible assets and liabilities as of June 30, 2014 based on their preliminary estimated fair values as follows (in thousands).

Preliminary Estimated Merger Consideration Allocation

Cash and due from banks	$	87,620
Federal funds sold and securities purchased under agreements to resell		72,582
Assets segregated for regulatory purposes		190,240
Securities		743,425
Non-covered loans, net		848,469
Broker-dealer and clearing organization receivables		1,992,941
Premises and equipment, net		12,864
Other assets		91,159
Deposits		(1,349,702)
Broker-dealer and clearing organization payables		(1,913,976)
Short-term borrowings		(98,343)
Advances from Federal Home Loan Bank		(78,891)
Other liabilities		(211,087)
Intangible assets		10,000
Bargain purchase gain		(30,738)
Preliminary Estimated Merger Consideration	$	366,563
Less Hilltop existing investment in SWS		(74,639)
Preliminary Estimated Merger Consideration, excluding Hilltop existing investment in SWS	$	291,924

Approximately $10.0 million has been preliminarily allocated to amortizable intangible assets acquired. The amortization related to the preliminary fair value of net amortizable intangible assets is reflected as a pro forma adjustment to the unaudited pro forma condensed combined financial statements.

Identifiable intangible assets. The preliminary fair values of intangible assets were determined based on the provisions of ASC 805, which defines fair value in accordance with ASC Topic 820, *Fair Value Measurements and Disclosures* ("ASC 820"). ASC 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Intangible assets were identified that met either the separability

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criterion or the contractual-legal criterion described in ASC 805. The preliminary allocation to intangible assets is as follows (dollars in thousands).

		Estimated Useful Life (Years)	Amortization Method
Customer contracts and relationships	$ 8,000	10	accelerated
Core deposit intangible	1,000	10	accelerated
Trademarks and trade names	1,000	20	straight-line
Total intangible assets	$ 10,000		

Bargain Purchase Gain. The bargain purchase gain represents the excess of the preliminary estimated fair value of the underlying net tangible and intangible assets over the preliminary estimated merger consideration. The bargain purchase gain resulting from the SWS Merger is a one-time, extraordinary gain that is not expected to be repeated in future periods. As noted above, the final amounts allocated to assets and liabilities could differ significantly from the amounts presented in the unaudited pro forma condensed combined financial statements. This may cause us to revise our estimates, which could result in the recognition of additional bargain purchase gain, or the recognition of less or no bargain purchase gain, in which case we may be required to record goodwill that would be subject to an ongoing impairment analysis.

4. Preliminary Unaudited Pro Forma and Merger Accounting Adjustments

The unaudited pro forma financial information is not necessarily indicative of what the financial position or operating results actually would have been had the SWS Merger taken place on January 1, 2013, and includes adjustments which are preliminary and may be revised. Such revisions may result in material changes. The financial position shown herein is not necessarily indicative of what the past financial position of the combined companies would have been, nor necessarily indicative of the financial position of the post-merger periods. The unaudited pro forma financial information does not give consideration to the impact of possible expense efficiencies, synergies, strategy modifications, asset dispositions, or other actions that may result from the SWS Merger.

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The following unaudited pro forma adjustments result from accounting for the merger, including the determination of fair value of the assets, liabilities and commitments which Hilltop, as the acquirer for accounting purposes, will acquire from SWS. The descriptions related to these preliminary adjustments are as follows (in thousands).

Balance Sheet

A	Adjustments to cash:		
	To reflect cash used to purchase outstanding shares of SWS	$	(78,159)
	To reflect cash used to pay estimated transaction costs		(8,000)
	To reflect cash used to pay make-whole interest on note payable by SWS to Oak Hill		(8,000)
		$	(94,159)
B	Adjustments to available for sale investments:		
	To eliminate Hilltop historical investment in SWS	$	(74,639)
	To reflect purchase fair value of Hilltop investment in SWS		80
		$	(74,559)
C	Adjustment to held to maturity investments:		
	To reflect estimated fair value at acquisition date	$	403
D	Adjustment to non-covered loans, net:		
	To reflect estimated fair value at acquisition date	$	(19,466)
E	Adjustment to premises and equipment, net:		
	To reflect estimated fair value at acquisition date	$	(3,000)
F	Adjustments to other assets:		
	To reflect deferred tax asset changes resulting from pro forma adjustments	$	12,728
	To reflect current tax recoverable from estimated transaction costs		1,400
	To reflect deferred tax liability arising from identified intangible assets		(3,500)
	To reflect estimated fair value of other assets at acquisition date		(4,947)
		$	5,681
G	Adjustment to goodwill:		
	To eliminate SWS historical acquired goodwill	$	(7,552)
H	Adjustment to other intangible assets, net:		
	To reflect the identified intangibles associated with the SWS Merger	$	10,000
I	Adjustment to deposits:		
	To reflect estimated fair value at acquisition date	$	(4,931)
J	Adjustment to advances from Federal Home Loan Bank:		
	To reflect estimated fair value at acquisition date	$	1,761
K	Adjustments to notes payable:		
	To reflect amortization of the remaining discount on notes payable held by SWS	$	12,231
	To reflect the issuance of SWS common stock in exchange for foregiveness of SWS notes payable held by Hilltop and Oak Hill		(100,000)
		$	(87,769)
L	Adjustment to stock purchase warrants:		
	To reflect the issuance of SWS common stock in exchange for foregiveness of SWS notes payable held by Hilltop and Oak Hill	$	(27,796)

M	Adjustment to other liabilities:		
	To reflect estimated fair value at acquisition date	$	4,700
N	Adjustments to common stock:		
	To reflect the issuance of SWS common stock in exchange for SWS notes payable and warrants held by Hilltop and Oak Hill	$	1,739
	To eliminate SWS historical common stock, including common stock issued for SWS notes payable and warrants held by Hilltop and Oak Hill		(5,070)
	To reflect the issuance of Hilltop common stock to SWS stockholders		101
		$	(3,230)
O	Adjustments to additional paid-in capital:		
	To reflect the issuance of SWS common stock in exchange for SWS notes payable and warrants held by Hilltop and Oak Hill	$	126,057
	To eliminate SWS historical additional paid-in capital, including common stock issued for SWS notes payable and warrants held by Hilltop and Oak Hill		(450,537)
	To reflect the issuance of Hilltop common stock to SWS stockholders		213,664
		$	(110,816)
P	Adjustments to accumulated other comprehensive loss:		
	To eliminate SWS historical accumulated other comprehensive loss	$	4,519
	To reflect recognition of unrealized gains on prior investment interests		(7,095)
		$	(2,576)
Q	Adjustments to accumulated deficit:		
	To eliminate SWS historical accumulated deficit	$	10,439
	To reflect increase in estimated fair value of Hilltop historical investment in SWS at acquisition date		52
	To reflect the bargain purchase gain associated with the SWS Merger		30,738
	To reflect estimated transactions costs, net of tax		(3,300)
	To reflect recognition of unrealized gains on prior investment interests		7,095
		$	45,024
R	Adjustment to deferred compensation, net:		
	To eliminate SWS historical deferred compensation, net	$	(3,189)
S	Adjustment to treasury stock:		
	To eliminate SWS historical treasury stock	$	6,170

Pursuant to the acquisition method of accounting, the final Merger Consideration will be based on the price of Hilltop's common stock immediately prior to the effective time of the SWS Merger. A 20% difference in per share price at the closing of the SWS Merger compared to the amount used in these unaudited pro forma condensed combined financial statements would increase or decrease total Merger Consideration and the bargain purchase gain by approximately $42 million.

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Statements of Income

		Six Months Ended June 30, 2014	Year Ended December 31, 2013
T	Adjustment to loan interest income:		
	To reflect accretion of loan discounts resulting from loan fair value pro forma adjustment	$ 1,364	$ 3,234
U	Adjustments to investment and other interest income:		
	To reflect elimination of historical interest income from Hilltop investment in SWS	$ (3,209)	$ (6,166)
	To reflect foregone interest resulting from pro forma cash adjustments, excluding make-whole provision	(38)	(97)
		$ (3,247)	$ (6,263)
V	Adjustment to interest expense on notes payable:		
	To reflect elimination of historical interest expense from Hilltop and Oak Hill notes payable in SWS	$ (6,665)	$ (12,827)
W			
	Adjustment to investment and securities advisory fees and commissions:		
	To reflect elimination of SWS discontinued operations from its historical operating results	$	$ (2,259)
X	Adjustment to employees' compensation and benefits:		
	To reflect elimination of SWS discontinued operations from its historical operating results	$	$ (1,627)
Y	Adjustments to occupancy and equipment expense:		
	To reflect reduction in deprecation expense resulting from premises and equipment pro forma adjustment	$ (300)	$ (600)
	To reflect elimination of SWS discontinued operations from its historical operating results		(127)
		$ (300)	$ (727)
Z	Adjustments to other noninterest expense:		
	To reflect elimination of historical unrealized losses from Hilltop and Oak Hill warrants in SWS	$ (3,508)	$ (54)
	To reflect intangible amortization expense resulting from identified intangibles associated with the SWS Merger	804	1,740
	To reflect elimination of SWS discontinued operations from its historical operating results		(355)
		$ (2,704)	$ 1,331
AA	Adjustments to income tax expense:		
	To reflect the income tax effect of pro forma adjustments at Hilltop's estimated combined statutory tax rate of 35%, excluding historical SWS pro forma adjustments	$ 2,725	$ (10,460)

Note that the estimated transaction costs included as part of the unaudited pro forma condensed combined balance sheet as of June 30, 2014 have not been included in the above unaudited pro forma adjustments. In addition, the unaudited pro forma condensed combined statements of income exclude nonrecurring items resulting directly from the SWS Merger and that do not have a continuing impact on results of operations. These items include estimated pre-tax income aggregating approximately $11.0 million as of June 30, 2014 associated with the recognition of gains on prior investment interests in SWS by Hilltop and the recognition of the remaining unrecognized discount on Hilltop's note receivable from SWS, and estimated pre-tax expense aggregating approximately $8.0 million as of June 30, 2014 associated with the estimated make-whole interest payment by SWS to Oak Hill.

5. Unaudited Preliminary Estimated Accretion/Amortization of Certain Purchase Accounting Adjustments

The following table sets forth an estimate of the expected effects, if not using the straight-line method, of the projected aggregate purchase accounting adjustments reflected in the unaudited pro forma condensed combined financial statements on the future income before income tax expense of Hilltop after the SWS Merger (in thousands).

	Accretion (Amortization)				
	Year 1	Year 2	Year 3	Year 4	Year 5
Loans, including fees	$ 3,234	$ 2,651	$ 2,258	$ 1,882	$ 1,122
Other intangibles	(1,690)	(1,515)	(1,339)	(1,163)	(988)
Increase in income before income tax expense	$ 1,544	$ 1,136	$ 919	$ 719	$ 134

The actual effect of purchase accounting adjustments on the future income before income tax expense of Hilltop may differ from these estimates based on the closing date estimates of fair values and the use of different amortization methods than assumed above.

6. Earnings per Common Share

Unaudited pro forma earnings per common share for the six months ended June 30, 2014 and for the year ended December 31, 2013 have been calculated using Hilltop's historic weighted average common shares outstanding plus the common shares issued as a part of the SWS Merger.

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

	Three Months Ended March 31, 2014	Year Ended December 31, 2013
Basic earnings per share:		
Pro forma combined net income	$ 46,845	$ 103,850
Less: income applicable to participating shares	(220)	(515)
Pro forma combined net earnings available to Hilltop common stockholders	$ 46,625	$ 103,335
Pro forma weighted average common shares outstanding basic:		
Historic Hilltop	89,708	84,382
Common shares issued to SWS common stockholders	10,055	10,055
Pro forma weighted average common shares outstanding basic	99,763	94,437
Pro forma combined net earnings per common share basic	$ 0.47	$ 1.09
Diluted earnings per share:		
Pro forma combined net income	$ 46,845	$ 103,850
Add: interest expense on senior exchangeable notes (net of tax)		5,059
Pro forma combined net earnings available to Hilltop common stockholders	$ 46,845	$ 108,909
Pro forma weighted average common shares outstanding basic	99,763	94,437
Effect of potentially dilutive securities	868	5,949
Pro forma weighted average common shares outstanding diluted	100,631	100,386
Pro forma combined net earnings per common share diluted	$ 0.47	$ 1.08

UNAUDITED COMPARATIVE PER SHARE DATA

The following tables present: (1) historical per share information for Hilltop; (2) pro forma per share information of the combined company after giving effect to the acquisition of SWS by Hilltop; and (3) historical and equivalent pro forma per share information for SWS.

We derived the combined company pro forma per share information primarily by combining information from the historical consolidated financial statements of Hilltop and SWS. You should read these tables, together with the historical consolidated financial statements of Hilltop which are included in this proxy statement/prospectus and of SWS which are filed with the SEC and incorporated by reference into this proxy statement/prospectus. See "Where You Can Find More Information." You should not rely on the pro forma per share information as being necessarily indicative of actual results had the acquisition occurred on January 1, 2013 (for statement of earnings purposes) or June 30, 2014 (for book value per share data purposes). The unaudited pro forma information, while helpful in illustrating the financial characteristics of the combined company under one set of assumptions, does not reflect the impact of possible business model changes as a result of current market conditions which may impact revenues, expense efficiencies, asset dispositions, share repurchases and other factors. It also does not necessarily reflect what the historical results of the combined company would have been had our companies been combined during these periods nor is it indicative of the results of operations in future periods or the future financial position of the combined company. The unaudited pro forma adjustments are based upon available information and certain assumptions that Hilltop management believes are reasonable. Upon completion of the merger, the operating results of SWS will be reflected in the consolidated financial statements of Hilltop on a prospective basis.

	Hilltop Historical	SWS Historical	Pro Forma Combined	Per Equivalent SWS Share(1)
Income (loss) from operations for the year ended December 31, 2013:				
Basic earnings (loss) per share	$ 1.43	$ (1.10)	$ 1.09	$ 0.27
Diluted earnings (loss) per share	$ 1.40	$ (1.10)	$ 1.08	$ 0.27
Dividends paid for the year ended December 31, 2013:	$	$	$	$
Book value per share as of December 31, 2013:	$ 13.27	$ 9.57	N/A	N/A
Income from operations for the six months ended June 30, 2014:				
Basic earnings per share	$ 0.56	$ (0.28)	$ 0.47	$ 0.12
Diluted earnings per share	$ 0.56	$ (0.28)	$ 0.47	$ 0.12
Dividends paid for the six months ended June 30, 2014:	$	$	$	$
Book value per share as of June 30, 2014:	$ 14.22	$ 9.46	$ 15.20	$ 3.79

(1) The per equivalent SWS share data is based only on the 0.2496 shares of Hilltop common stock to be issued to SWS stockholders as the stock portion of the merger consideration for each share of SWS common stock and does not give effect to the $1.94 in cash to be received by SWS stockholders as the cash portion of the merger consideration for each share of SWS common stock.

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COMPARATIVE MARKET PRICES AND DIVIDENDS

Hilltop common stock is listed on the New York Stock Exchange under the trading symbol "HTH." and SWS common stock is listed on the New York Stock Exchange under the trading symbol "SWS." The following table sets forth the high and low reported sale prices per share of Hilltop common stock and SWS common stock, and the cash dividends declared per share for the periods indicated.

	Hilltop Common Stock Market Price			SWS Common Stock Market Price		
	High	Low	Dividend	High	Low	Dividend
2011						
First Quarter	$ 10.13	$ 9.01	$	$ 6.49	$ 4.27	$ 0.01
Second Quarter	10.09	8.60		6.76	5.56	0.01
Third Quarter	9.01	7.12		6.31	3.67	
Fourth Quarter	8.60	6.88		7.56	4.03	
2012						
First Quarter	$ 9.10	$ 7.87	$	$ 7.77	$ 4.79	$
Second Quarter	10.89	7.75		5.94	5.08	
Third Quarter	12.80	10.21		6.58	5.23	
Fourth Quarter	14.49	12.57		6.33	4.02	
2013						
First Quarter	$ 14.21	$ 12.34	$	$ 6.82	$ 5.32	$
Second Quarter	16.94	12.59		6.29	5.30	
Third Quarter	18.71	15.46		6.28	5.19	
Fourth Quarter	24.05	17.09		6.59	5.31	
2014						
First Quarter	$ 25.61	$ 22.42	$	$ 8.29	$ 6.01	$
Second Quarter	25.08	19.72		8.06	6.95	
Third Quarter	22.39	19.32		7.60	6.89	
Fourth Quarter (through October 13, 2014)	21.13	19.41		7.22	6.64	

The following table sets forth the closing prices of Hilltop and SWS as reported on January 9, 2014, the last trading day prior to Hilltop publicly announcing its interest in a transaction with SWS and October 13, 2014, the last trading day prior to the date of this proxy statement/prospectus. The table also shows the implied value of one share of SWS common stock at each applicable date, which was calculated by multiplying the closing price for one share of Hilltop common stock by the exchange ratio of 0.2496 and adding the cash component of the merger consideration of $1.94 per SWS common share.

	Hilltop Common Stock Closing Price	SWS Common Stock Closing Price	Implied Value of SWS Common Stock
January 9, 2014	$ 23.44	$ 6.06	$ 7.79
October 13, 2014	$ 19.76	$ 6.77	$ 6.87

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RISK FACTORS

In addition to general investment risks, the other information included and incorporated by reference in this proxy statement/prospectus (please see the section entitled "Where You Can Find More Information"), including the matters addressed in the section entitled "Forward-Looking Statements," you should carefully consider the following risks before deciding whether to adopt and approve the merger agreement.

Risk Factors Relating to the Merger

Because the market price of Hilltop common stock will fluctuate and the per share merger consideration may be adjusted, SWS stockholders cannot be sure of the value of the merger consideration they will receive.

Upon completion of the merger, each share of SWS common stock will be converted into merger consideration consisting of $1.94 in cash and 0.2496 in Hilltop common stock. As of June 30, 2014, the book value per share of SWS common stock was $9.46 and the tangible book value per share of SWS common stock was $9.23. Giving effect to the merger as of June 30, 2014, the pro forma book value per equivalent SWS share is $3.79 (the per equivalent SWS share figure is based only on the 0.2496 shares of Hilltop common stock to be issued to SWS stockholders as the stock portion of the merger consideration for each share of SWS common stock and does not give effect to the $1.94 in cash to be received by SWS stockholders as the cash portion of the merger consideration for each share of SWS common stock). The market value of the merger consideration may vary from the closing price of Hilltop common stock on the date the merger was announced, on the date that this proxy statement/prospectus was mailed to SWS stockholders, on the date of the special meeting of the SWS stockholders and on the date the merger is completed and thereafter. Any change in the market price of Hilltop common stock prior to completion of the merger will affect the market value of the merger consideration that SWS stockholders will receive upon completion of the merger. Accordingly, at the time of the special meeting, SWS stockholders will not know, or be able to calculate, the value of the merger consideration they would receive upon completion of the merger. SWS is not permitted to terminate the merger agreement or resolicit the vote of its stockholders solely because of changes in the market price of Hilltop's common stock, and there will be no adjustment to the merger consideration for changes in such market price. Stock price changes may result from a variety of factors, including general market and economic conditions, changes in our respective businesses, operations and prospects, and regulatory considerations. Many of these factors are beyond SWS's control.

We urge you to obtain current market quotations for shares of Hilltop common stock before you vote your shares at the SWS special meeting.

The results of operations of Hilltop after the merger may be affected by factors different from those currently affecting the results of operations of Hilltop and SWS.

The businesses of Hilltop and SWS differ in important respects and, accordingly, the results of operations of the combined company and the market price of the combined company's common stock may be affected by factors different from those currently affecting the independent results of operations of Hilltop and SWS. For a discussion of the business of Hilltop and of certain factors to consider in connection with Hilltop's business, see "Information About the Companies Hilltop" included elsewhere in this proxy statement/prospectus and the consolidated financial statements of Hilltop beginning on page F-1 of this proxy statement/prospectus. For a discussion of the business of SWS and of certain factors to consider in connection with SWS's business, see "Information About the Companies SWS" and the information included in this proxy statement/prospectus and referred to under "Where You Can Find More Information" included elsewhere in this proxy statement/prospectus.

The fairness opinion that SWS has obtained from Sandler O'Neill, has not been, and is not expected to be, updated to reflect any changes in circumstances that may have occurred since the signing of the merger agreement.

The fairness opinions issued to the Special Committee by Sandler O'Neill regarding the fairness, from a financial point of view, of the consideration to be received by stockholders of SWS other than Hilltop in connection with the merger, speaks only as of March 31, 2014. Changes in the operations and prospects of Hilltop or SWS, general market and economic conditions and other factors which may be beyond the control of Hilltop and SWS, and on which the fairness opinion was based, may have altered the value of Hilltop or SWS or the market price of shares of Hilltop common stock as of the date of this proxy statement/prospectus, or may alter such values and market price by the time the merger is completed. For example, the implied value of SWS common stock was $7.88 per share on the date of the fairness opinion and $6.87 per share as of October 13, 2014. Sandler O'Neill does not have any obligation to update, revise or reaffirm its opinion to reflect subsequent developments, and has not done so. For a description of the opinion that SWS received from its financial advisor, please refer to "The Merger Opinion of SWS's Financial Advisor" included elsewhere in this proxy statement/prospectus. For a description of the other factors considered by SWS's board of directors in determining to approve the merger, please refer to "The Merger Reasons for the Merger and "The Merger Recommendation of the SWS Board of Directors" included elsewhere in this proxy statement/prospectus.

The merger is subject to the receipt of consents and approvals from government entities that may take longer than expected or may impose conditions that are not presently anticipated or that could have an adverse effect on the combined company following the merger.

The merger is conditioned on the receipt of all requisite governmental and regulatory authorizations, consents, orders and approvals from the Federal Reserve Board and the Texas Department of Banking and the expiration or termination of the waiting period under the HSR Act. These government entities may impose conditions on the completion of the merger and bank merger or require changes to the terms of the merger or bank merger. Although Hilltop and SWS do not currently expect that any such material conditions or changes would be imposed, there can be no assurance that they will not be, and such conditions or changes could have the effect of delaying or preventing completion of the merger or imposing additional costs on or limiting the revenues of the combined company following the merger and the bank merger, any of which might have an adverse effect on the combined company following the merger and the bank merger. See "The Merger Regulatory Approvals Required for the Merger."

Upon your receipt of shares of Hilltop common stock as merger consideration, you will become a stockholder in Hilltop, a Maryland corporation, which may change certain stockholder rights and privileges you hold as a stockholder of SWS, a Delaware corporation.

Hilltop is a Maryland corporation and is governed by the laws of the State of Maryland and by its articles of incorporation and bylaws. Maryland corporation law extends to stockholders certain rights and privileges that may not exist under Delaware law and, conversely, does not extend certain rights and privileges that you may have as a stockholder of SWS, which is governed by Delaware law and SWS's certificate of incorporation and bylaws. For a detailed discussion of the rights of Hilltop stockholders versus the rights of SWS stockholders, please see the section of this proxy statement/prospectus entitled "Comparison of Stockholders' Rights."

SWS will be subject to business uncertainties, and Hilltop and SWS are subject to contractual restrictions while the merger is pending.

Uncertainty about the effect of the merger on employees and customers may have an adverse effect on SWS and consequently on Hilltop. These uncertainties may impair SWS's ability to attract, retain and motivate key personnel while the merger is pending, and could cause customers and others that deal with SWS to seek to change existing business relationships with SWS. Retention of certain employees may be challenging during the pendency of the merger, as certain employees may experience uncertainty about their future roles. If key employees depart because of issues relating to such uncertainty or a desire not to remain with the business, SWS's or Hilltop's respective business following the merger could be negatively impacted.

In addition, the merger agreement restricts SWS and, to a lesser extent, Hilltop from taking certain specified actions until the merger occurs without the consent of the other party. These restrictions may prevent Hilltop and SWS from pursuing attractive business opportunities that may arise prior to the completion of the merger. See "The Merger Agreement Covenants and Agreement" included elsewhere in this proxy statement/prospectus for a description of the restrictive covenants applicable to Hilltop and SWS. In addition, SWS's or Hilltop's businesses may be indirectly adversely affected by the failure to pursue other beneficial opportunities due to the focus of management on the merger.

The merger is subject to certain closing conditions that, if not satisfied or waived, will result in the merger not being completed, which may cause the price of Hilltop common stock and SWS common stock to decline.

The merger is subject to customary conditions to closing, including the receipt of required regulatory approvals and approval of the SWS stockholders. If any condition to the merger is not satisfied or waived, the merger will not be completed. In addition, Hilltop and SWS may terminate the merger agreement under certain circumstances even if the merger is approved by SWS stockholders, including if the merger has not been consummated by March 31, 2015. If Hilltop and SWS do not complete the merger, the trading price of Hilltop and SWS common stock may decline to the extent that the current prices reflect a market assumption that the merger will be completed. In addition, neither company would realize any of the expected benefits of having completed the merger. If the merger is not completed, additional risks could materialize, which could materially and adversely affect the business, financial condition and results of Hilltop or SWS. For more information on closing conditions to the merger agreement, see "The Merger Agreement Conditions to Completion of the Merger" included elsewhere in this proxy statement/prospectus.

The merger agreement limits SWS's ability to pursue an alternative transaction and requires SWS to pay a termination fee of $8 million under certain circumstances relating to alternative acquisition proposals.

SWS agreed in the merger agreement that it will not, and will cause its subsidiaries not to, and will use its reasonable best efforts to cause its or their respective officers, directors, employees, representatives or agents not to, knowingly encourage, solicit, participate in, knowingly facilitate or initiate discussions, negotiations, inquiries, proposals or offers with or provide any non-public information to, any person relating to any third party acquisition (as defined below) or any inquiry, proposal or offer reasonably likely to lead to a third party acquisition, subject to exceptions set forth in the merger agreement. See "The Merger Agreement No Solicitation" included elsewhere in this proxy statement/prospectus. The merger agreement also provides for the payment by SWS of a termination fee in the amount of $8 million in the event that Hilltop terminates the merger agreement for certain reasons including a change in the recommendation of SWS's board of directors or a termination of the merger agreement in certain circumstances followed by an acquisition of, or an agreement to acquire, SWS by a third party. These provisions may discourage a potential competing acquiror that might have an interest in acquiring all or a significant part of SWS from considering or proposing such an acquisition. Furthermore, if the merger agreement is terminated and SWS's board of directors seeks another party to acquire SWS, SWS stockholders cannot be certain that SWS will be able to find a party willing to engage in a transaction or to pay the equivalent or greater consideration than that which Hilltop has agreed to pay in the merger. See "The Merger Agreement Termination Fee" included elsewhere in this proxy statement/prospectus.

SWS's Credit Agreement with Hilltop and Oak Hill contains a covenant restricting SWS's ability to enter into alternative transactions and Hilltop did not waive this covenant while Hilltop remained a lender thereunder.

On July 29, 2011, SWS entered into a Credit Agreement in respect of a $100,000,000, five-year, unsecured loan comprised of a $50,000,000 commitment from Hilltop and a $50,000,000 commitment from Oak Hill Capital Partners III, L.P. and Oak Hill Capital Management Partners III, L.P. The terms of the Credit Agreement include a covenant prohibiting SWS from undergoing a "Fundamental Change," which includes any merger, amalgamation or consolidation, and which SWS would breach by engaging in a merger, amalgamation or consolidation unless compliance were waived by each of Hilltop and Oak Hill. During the parties' negotiations with respect to the merger, Hilltop indicated to SWS that it would not be willing to grant a waiver of this covenant to permit a third party transaction. As a result of its exercise in full of its warrant to purchase 8,695,652 shares of SWS common stock disclosed elsewhere in this proxy statement/prospectus, Hilltop's portion of the loan outstanding under the Credit Agreement was eliminated and Hilltop is accordingly no longer a lender under the Credit Agreement. Oak Hill remains a lender under the Credit Agreement with a current outstanding balance of $12,500,000.75. The existence of the Merger Covenant, and Hilltop's unwillingness to waive it while Hilltop remained a lender under the Credit Agreement, may have discouraged and may continue to discourage potential competing acquirors that might have an interest in acquiring all or a significant part of SWS from considering or proposing such an acquisition (see "The Merger Background of the Merger" and "The Merger Hilltop's Relationship with SWS").

Current Hilltop stockholders and SWS stockholders will have a reduced ownership and voting interest after the merger and will exercise less influence over management.

Current Hilltop stockholders have the right to vote in the election of the Hilltop board of directors and on other matters affecting Hilltop. Current SWS stockholders have the right to vote in the election of the SWS board of directors and on other matters affecting SWS. Immediately after the merger is completed, it is expected that, on a fully diluted basis, current Hilltop stockholders will own approximately 90%, and current SWS stockholders will own approximately 10%, of the outstanding shares of Hilltop common stock. As a result of the merger, current Hilltop stockholders will have less influence on the management and policies of Hilltop post-merger than they currently have, and current SWS stockholders will have less influence on the management and policies of Hilltop post-merger than they currently have with respect to SWS.

The financial analyses and forecasts considered by Hilltop, SWS and SWS's financial advisor may not be realized, which may adversely affect the market price of Hilltop shares following the merger.

In performing its financial analyses and rendering its opinion regarding the fairness, from a financial point of view, of the merger consideration set forth in the merger agreement, the financial advisor to SWS independently reviewed and relied on, among other things, internal standalone financial analyses and forecasts provided to it by SWS. Certain of these analyses and forecasts were also provided to Hilltop. See the section titled "The Merger Certain SWS Prospective Financial Information" included elsewhere in this proxy statement/prospectus. SWS's financial advisor assumed, at the direction of the board of directors of SWS, that such financial information was reasonably prepared on a basis reflecting the best currently available estimates and judgments of the management of SWS as to the future performance of SWS and that such future financial results will be achieved at the times and in the amounts projected by management of SWS. These analyses and forecasts were prepared by, or as directed by, the management of SWS and were also considered by the SWS board of directors and the Special Committee. None of these analyses or forecasts was prepared with a view towards public disclosure or compliance with the published guidelines of the SEC, generally accepted accounting principles in the U.S. ("GAAP"), statutory accounting principles ("SAP") or the guidelines established by the American Institute of Certified Public Accountants for preparation and presentation of financial forecasts. These projections are inherently based on various estimates and assumptions that are subject to the judgment of those preparing them. These projections are also subject to significant economic, competitive, industry and other uncertainties and contingencies, all of which are difficult or impossible to predict and many of which are beyond the control of SWS and Hilltop. Accordingly, SWS's and/or Hilltop's financial condition or results of operations may not be consistent with those set forth in such analyses and forecasts. Worse financial results could have a material adverse effect on the market price of Hilltop common stock following the merger.

The directors and executive officers of SWS have interests in the merger that are different from, or in addition to, those of other SWS stockholders generally. Therefore, the directors and executive officers of SWS may have a conflict of interest in recommending the proposals being voted on at the SWS special meeting.

The directors and executive officers of SWS may have interests in the merger that are different from, or in addition to, those of SWS stockholders generally. These interests include, among others, the accelerated vesting of equity awards and other potential payments in connection with (or subsequent to) the merger. The SWS board of directors was aware of these interests and considered these interests, among other matters, when making its decision to approve the merger agreement and in recommending that SWS stockholders vote in favor of approving the merger agreement. These interests may influence the executive officers and directors of SWS to support or approve the proposals to be presented at the SWS special meeting.

See "The Merger Interests of SWS Directors and Executive Officers in the Merger" included elsewhere in this proxy statement/prospectus for a more detailed description of these interests.

The completion of the merger may trigger change in control provisions in certain agreements to which SWS is a party.

The completion of the merger may trigger change in control provisions in certain agreements to which SWS is a party. If SWS and Hilltop are unable to negotiate waivers of those provisions, the counterparties may exercise their rights and remedies under the agreements (including terminating the agreements or seeking monetary penalties). Even if SWS or Hilltop is able to obtain waivers, the counterparties may demand a fee for such waivers or seek to renegotiate the agreements on materially less favorable terms than those currently in place.

Termination of the merger agreement could negatively impact SWS and/or Hilltop.

If the merger agreement is terminated, there may be various consequences. For example, SWS's or Hilltop's businesses may have been impacted adversely by the failure to pursue other beneficial opportunities due to the focus of management on the merger, without realizing any of the anticipated benefits of completing the merger. A termination of the merger agreement may also damage the reputations and franchise values of Hilltop and SWS. If the merger agreement is terminated and SWS's board of directors seeks another merger or business combination, SWS stockholders cannot be certain that SWS will be able to find a party willing to engage in a transaction or to pay the equivalent or greater consideration than that which Hilltop has agreed to pay in the merger. In addition, if the merger agreement is terminated under certain circumstances, SWS may be required to pay Hilltop a termination fee of $8 million.

The combined company expects to incur substantial expenses related to the merger.

The combined company expects to incur substantial expenses in connection with completing the merger and combining the business, operations, networks, systems, technologies, policies and procedures of the two companies. Although Hilltop and SWS have assumed that a certain level of transaction and combination expenses would be incurred, there are a number of factors beyond their control that could affect the total amount or the timing of their combination expenses. Many of the expenses that will be incurred, by their nature, are difficult to estimate accurately at the present time. Due to these factors, the transaction and combination expenses associated with the merger could, particularly in the near term, exceed the savings that the combined company expects to achieve from the elimination of duplicative expenses and the realization of economies of scale and cost savings related to the combination of the businesses following the completion of the merger. As a result of these expenses, both Hilltop and SWS expect to take charges against their earnings before and after the completion of the merger. The charges taken in connection with the merger are expected to be significant, although the aggregate amount and timing of such charges are uncertain at present. Further, if the merger is not completed, both SWS and Hilltop would have to recognize these expenses without realizing the expected benefits of the merger.

If completed, the merger may not produce its anticipated results, and Hilltop and SWS may be unable to combine their operations in the manner expected.

Hilltop and SWS entered into the merger agreement with the expectation that the merger will result in various benefits. Achieving the anticipated benefits of the merger is subject to a number of uncertainties, including whether the Hilltop and SWS organizations can be combined in an efficient, effective and timely manner.

It is possible that the transition process could take longer than anticipated and could result in the loss of valuable employees, the disruption of each company's ongoing businesses, controls, procedures, policies and compensation arrangements, any of which could adversely affect the combined company's ability to achieve the anticipated benefits of the merger. The combined company's results of operations could also be adversely affected by any issues attributable to either company's operations that arise or are based on events or actions that occur prior to the closing of the merger. The companies may have difficulty addressing possible differences in corporate cultures and management philosophies. The transition process is subject to a number of uncertainties, and no assurance can be given that the anticipated benefits will be realized or, if realized, the timing of their realization. Failure to achieve these anticipated benefits could result in increased costs or decreases in the amount of expected revenues and could adversely affect the combined company's future business, financial condition, operating results and prospects.

The merger may not be accretive to earnings and may cause dilution to Hilltop's earnings per share, which may negatively affect the market price of Hilltop's common stock.

The merger may not be accretive to earnings, and Hilltop could encounter additional transaction and integration-related costs, may fail to realize all of the benefits anticipated in the merger or be subject to other factors that affect preliminary estimates. Any of these factors could cause a decrease in Hilltop's adjusted earnings per share or decrease or delay the expected accretive effect of the merger and contribute to a decrease in the price of Hilltop's common stock.

If the merger fails to qualify as a "reorganization" within the meaning of Section 368(a) of the Code, SWS stockholders may be required to recognize additional gain or loss on the exchange of their shares of SWS common stock in the merger for U.S. federal income tax purposes.

Hilltop and SWS have structured the merger to qualify as a "reorganization" within the meaning of Section 368(a) of the Code. Neither Hilltop nor SWS intends to request any ruling from the Internal

Revenue Service as to the tax consequences of the exchange of shares of SWS common stock for shares of Hilltop common stock in the merger. If the merger fails to qualify as a reorganization, an SWS stockholder would generally recognize gain or loss for U.S. federal income tax purposes on each share of SWS common stock exchanged in the merger in an amount equal to the difference between that stockholder's basis in such share and the sum of the amount of the cash and the fair market value of the shares of Hilltop common stock the SWS stockholder receives or may receive in exchange for each such share of SWS common stock. You are urged to consult with your own tax advisor regarding the proper reporting of the amount and timing of such gain or loss. See "United States Federal Income Tax Consequences of the Merger" elsewhere in this proxy statement/prospectus.

Pending litigation against SWS and Hilltop could result in an injunction preventing the completion of the merger or a judgment resulting in the payment of damages.

In connection with the merger, purported SWS stockholders have filed putative shareholder class action lawsuits against SWS, the members of the SWS board of directors and Hilltop. Among other remedies, the plaintiffs seek to enjoin the merger. If the cases are not resolved, these lawsuits could prevent or delay completion of the merger and result in substantial costs to SWS and Hilltop, including any costs associated with the indemnification of directors and officers. Plaintiffs may file additional lawsuits against SWS, Hilltop and/or the directors and officers of either company in connection with the merger. The defense or settlement of any lawsuit or claim that remains unresolved at the time the merger is completed may adversely affect Hilltop's business, financial condition, results of operations and cash flows.

The unaudited pro forma condensed combined financial statements included in this proxy statement/prospectus are presented for illustrative purposes only and the actual financial condition and results of operations of the combined company following the merger may differ materially.

The unaudited pro forma condensed combined financial statements contained in this proxy statement/prospectus are presented for illustrative purposes only, are based on various adjustments, assumptions and preliminary estimates and may not be an indication of the combined company's financial condition or results of operations following the merger for several reasons. The actual financial condition and results of operations of the combined company following the merger may not be consistent with, or evident from, these unaudited pro forma condensed combined financial statements. In addition, the assumptions used in preparing the unaudited pro forma financial information may not prove to be accurate, and other factors may affect the combined company's financial condition or results of operations following the merger. Any potential decline in the combined company's financial condition or results of operations may cause significant variations in the stock price of the combined company.

The market price of Hilltop common stock after the merger may be affected by factors different from those affecting the shares of SWS or Hilltop currently.

Upon completion of the merger, holders of SWS common stock will become holders of Hilltop common stock. Hilltop's business differs in important respects from that of SWS, and, accordingly, the results of operations of the combined company and the market price of Hilltop common stock after the completion of the merger may be affected by factors different from those currently affecting the independent results of operations of each of SWS and Hilltop. For a discussion of the business of Hilltop and of certain factors to consider in connection with Hilltop's business, see "Information About the Companies Hilltop" included elsewhere in this proxy statement/prospectus and the consolidated financial statements of Hilltop beginning on page F-1 of this proxy statement/prospectus. For a discussion of the business of SWS and of certain factors to consider in connection with SWS's business, see "Information About the Companies SWS" and the information incorporated by reference in this proxy statement/prospectus and referred to under "Where You Can Find More Information."

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Risk Factors Relating to Hilltop's Business

Hilltop may fail to realize all of the anticipated benefits of its merger with PlainsCapital Corporation ("PlainsCapital") or the acquisition of the deposits and assets of First National Bank ("FNB").

Achieving the anticipated cost savings and financial benefits of Hilltop's 2012 merger with PlainsCapital Corporation (the "PlainsCapital Merger") and 2013 acquisition of the deposits and substantially all of the assets of First National Bank (the "FNB Transaction") and any other acquisitions Hilltop may complete will depend, in part, on Hilltop's ability to successfully integrate the operations of the respective companies with its own in an efficient and effective manner. It is possible that the integration process could result in the loss of key employees, the disruption of ongoing business or inconsistencies in standards, controls, procedures and policies that adversely affect Hilltop's ability to maintain relationships with clients, customers, depositors and employees. In addition, the integration of certain operations will require the dedication of significant management resources, which may temporarily distract management's attention from Hilltop's day-to-day business. Any inability to realize the full extent, or any, of the anticipated cost savings and financial benefits of the PlainsCapital Merger, the FNB Transaction, as well as any delays encountered in the integration process, could have an adverse effect on Hilltop's business and results of operations, which could adversely affect Hilltop's financial condition and cause a decrease in its earnings per share or decrease or delay the expected accretive effect of the FNB Transaction and contribute to a decrease in the price of Hilltop's common stock.

If Hilltop's allowance for loan losses is insufficient to cover actual loan losses, Hilltop's banking segment earnings will be adversely affected.

As a lender, Hilltop is exposed to the risk that Hilltop could sustain losses because Hilltop's borrowers may not repay their loans in accordance with the terms of their loans. Hilltop has historically accounted for this risk by maintaining an allowance for loan losses in an amount intended to cover Bank management's estimate of losses inherent in the loan portfolio. As a result of the PlainsCapital Merger and the FNB Transaction, Hilltop was required under GAAP to estimate the fair value of the loan portfolio after the consummation of the PlainsCapital Merger in 2012 and the FNB Transaction in 2013 and write-down the recorded value of the portfolio to that estimate. For most loans, this process was accomplished by computing the net present value of estimated cash flows to be received from borrowers of these loans. PlainsCapital's and FNB's respective allowance for loan losses that had been maintained prior to the PlainsCapital Merger and the FNB Transaction were eliminated in this accounting process. A new allowance for loan losses has been established for loans made by PlainsCapital Bank (the "Bank") subsequent to consummation of the PlainsCapital Merger and for any decrease from that originally estimated as of the acquisition date in the estimate of cash flows to be received from the loans acquired in the PlainsCapital Merger and the FNB Transaction.

The estimates of fair value as of the consummation of the PlainsCapital Merger and the FNB Transaction were based on economic conditions at such time and on Bank management's projections concerning both future economic conditions and the ability of the borrowers to continue to repay their loans. If management's assumptions and projections prove to be incorrect, however, the estimate of fair value may be higher than the actual fair value and Hilltop may suffer losses in excess of those estimated. Further, the allowance for loan losses established for new loans or for revised estimates may prove to be inadequate to cover actual losses, especially if economic conditions worsen.

While management will endeavor to estimate the allowance to cover anticipated losses, no underwriting and credit monitoring policies and procedures that Hilltop could adopt to address credit risk could provide complete assurance that Hilltop will not incur unexpected losses. These losses could have a material adverse effect on Hilltop's business, financial condition, results of operations and cash flows. In addition, federal regulators periodically evaluate the adequacy of the allowance for loan losses and may require Hilltop to increase its provision for loan losses or recognize further loan charge-offs based on judgments different from those of Hilltop's Bank management.

An adverse change in real estate market values may result in losses in Hilltop's banking segment and otherwise adversely affect Hilltop's profitability.

At June 30, 2014, approximately 42% of the loan portfolio of Hilltop's banking segment was comprised of loans with real estate as the primary component of collateral. The real estate collateral in each case provides an alternate source of repayment in the event of default by the borrower and may deteriorate in value during the time the credit is extended. A decline in real estate values generally and in Texas specifically could impair the value of Hilltop's collateral and its ability to sell the collateral upon any foreclosure. In the event of a default with respect to any of these loans, the amounts Hilltop receives upon sale of the collateral may be insufficient to recover the outstanding principal and interest on the loan. As a result, Hilltop's profitability and financial condition may be adversely affected by a decrease in real estate market values.

Loans acquired in the FNB Transaction may not be covered by the loss-share agreements if the FDIC determines that Hilltop has not adequately managed these loans.

Under the terms of the loss-share agreements Hilltop entered into with the FDIC in connection with the FNB Transaction, the FDIC is obligated to reimburse Hilltop for the following losses on covered loans: (i) 80% of losses on the first $240.4 million of losses incurred; (ii) 0% of losses in excess of $240.4 million up to and including $365.7 million of losses incurred; and (iii) 80% of losses in excess of $365.7 million of losses incurred. The loss-share agreements for commercial and single family residential loans are in effect for 5 years and 10 years, respectively, and the loss recovery provisions to the FDIC are in effect for 8 years and 10 years, respectively, from September 13, 2013 (the "Bank Closing Date"). Although the FDIC has agreed to reimburse Hilltop for the substantial portion of losses on covered loans, the FDIC has the right to refuse or delay payment for loan losses if Hilltop does not manage covered loans in accordance with the loss-share agreements. In addition, reimbursable losses are based on the book value of the relevant loans as determined by the FDIC as of the effective dates of the transactions. The amount that Hilltop realizes on these loans could differ materially from the carrying value that will be reflected in Hilltop's consolidated financial statements, based upon the timing and amount of collections on the covered loans in future periods. Any losses Hilltop experiences in the assets acquired in the FNB Transaction that are not covered under the loss-share agreements could have an adverse effect on Hilltop's results of operations and financial condition.

In addition, in accordance with the loss-share agreements, the Bank may be required to make a "true-up" payment to the FDIC, approximately ten years following the Bank Closing Date, if the FDIC's initial estimate of losses on covered assets is greater than the actual realized losses. The "true-up" payment is calculated using a defined formula set forth in the purchase and assumption agreement Hilltop entered into with the FDIC in connection with the FNB Transaction.

Hilltop's business and results of operations may be adversely affected by unpredictable economic, market and business conditions.

Hilltop's business and results of operations are affected by general economic, market and business conditions. The credit quality of Hilltop's loan portfolio necessarily reflects, among other things, the general economic conditions in the areas in which Hilltop's conducts its business. Hilltop's continued financial success depends to a degree on factors beyond Hilltop's control, including:

- national and local economic conditions, such as the level and volatility of short-term and long-term interest rates, inflation, home prices, unemployment and under-employment levels, bankruptcies, household income and consumer spending;

- general economic consequences of international conditions, such as weakness in European sovereign debt and emerging markets and the impact of that weakness on the U.S. and global economies;
- the availability and cost of capital and credit;
- incidence of customer fraud; and
- federal, state and local laws affecting these matters.

The deterioration of any of these conditions, as Hilltop has experienced with the past economic downturn and continuation of a weakened economy and employment growth, could adversely affect Hilltop's consumer and commercial businesses and securities portfolios, Hilltop's level of charge-offs and provision for credit losses, the carrying value of Hilltop's deferred tax assets, the investment portfolio of Hilltop's insurance segment, Hilltop's capital levels and liquidity, and Hilltop's results of operations.

Continued elevated unemployment, under-employment and household debt, along with continued stress in the consumer real estate market and certain commercial real estate markets, pose challenges for economic performance and the financial services industry. The sustained high unemployment rate and the lengthy duration of unemployment have directly impaired consumer finances and pose risks to the financial services industry. Continued uncertainty in the housing markets and elevated levels of distressed and delinquent mortgages pose further risks to the housing market. The current environment of heightened scrutiny of financial institutions has resulted in increased public awareness of and sensitivity to banking fees and practices. Each of these factors may adversely affect Hilltop's fees and costs.

Hilltop's geographic concentration may magnify the adverse effects and consequences of any regional or local economic downturn.

Hilltop conducts its banking operations primarily in Texas. Substantially all of the real estate loans in Hilltop's loan portfolio are secured by properties located in Texas, with more than 78% and 82% secured by properties located in the Dallas/Fort Worth and Austin/San Antonio markets at December 31, 2013 and 2012, respectively. Adverse economic conditions in Texas may result in a reduction in the value of the collateral securing these loans. Likewise, substantially all of the real estate loans in Hilltop's loan portfolio are made to borrowers who live and conduct business in Texas. In addition, mortgage origination fee income is dependent to a significant degree on economic conditions in Texas and California. During 2013, approximately 23% and 18% by dollar volume of Hilltop's mortgage loans originated were collateralized by properties located in Texas and California, respectively. Texas insureds accounted for approximately 69% and 70% of Hilltop's insurance segment's gross premiums written in 2013 and 2012, respectively. Any regional or local economic downturn that affects Texas or, to a lesser extent, California, may affect Hilltop and its profitability more significantly and more adversely than Hilltop's competitors that are less geographically concentrated.

Hilltop's geographic concentration may also exacerbate the adverse effects on Hilltop's insurance segment of inherently unpredictable catastrophic events.

Hilltop's insurance segment expects to have large aggregate exposures to inherently unpredictable natural and man-made disasters of great severity, such as hurricanes, hail, tornados, windstorms, wildfires and acts of terrorism. Hurricanes Ike, Katrina and Rita highlighted the challenges inherent in predicting the impact of catastrophic events. The catastrophe models utilized by Hilltop's insurance segment to assess its probable maximum insurance losses generally failed to adequately project the financial impact of these hurricanes. Although Hilltop's insurance segment may attempt to exclude certain losses, such as terrorism and other similar risks, from some coverage that Hilltop's insurance segment writes, it may be prohibited from, or may not be successful in, doing so. The occurrence of losses from catastrophic events may have a material adverse effect on Hilltop's insurance segment's ability to write new business and on its financial condition and results of operations. Increases in the values and geographic concentrations of policyholder property and the effects of inflation have resulted in increased severity of industry losses in recent years, and Hilltop's insurance segment expects that these factors will increase the severity of losses in the future. Factors that may influence Hilltop's insurance segment's exposure to losses from these types of events, in addition to the routine adjustment of losses, include, among others:

- exhaustion of reinsurance coverage;
- increases in reinsurance rates;
- unanticipated litigation expenses;
- unrecoverability of ceded losses;
- impact on independent agent operations and future premium income in areas affected by catastrophic events;
- unanticipated expansion of policy coverage or reduction of premium due to regulatory, legislative and/or judicial action following a catastrophic event; and
- unanticipated demand surge related to other recent catastrophic events.

Hilltop's insurance segment writes insurance primarily in the states of Texas, Oklahoma, Arizona, Tennessee, Georgia and Louisiana. In 2013, Texas accounted for 69.1%, Oklahoma accounted for 9.1%, Arizona accounted for 8.7%, Tennessee accounted for 5.8% and Georgia accounted for 3.5% of Hilltop's premiums. As a result, a single catastrophe, destructive weather pattern, wildfire, terrorist attack, regulatory development or other condition or general economic trend affecting these regions or significant portions of these regions could adversely affect Hilltop's insurance segment's financial condition and results of operations more significantly than other insurance companies that conduct business across a broader geographic area. Although Hilltop's insurance segment purchases catastrophe reinsurance to limit its exposure to these types of catastrophes, in the event of one or more major catastrophes resulting in losses to it in excess of $140.0 million, Hilltop's insurance segment's losses would exceed the limits of its reinsurance coverage.

Hilltop's business is subject to interest rate risk, and fluctuations in interest rates may adversely affect Hilltop's earnings, capital levels and overall results.

The majority of Hilltop's assets are monetary in nature and, as a result, Hilltop is subject to significant risk from changes in interest rates. Changes in interest rates may impact Hilltop's net interest income in Hilltop's banking segment as well as the valuation of Hilltop's assets and liabilities in each of Hilltop's segments. Earnings in Hilltop's banking segment are significantly dependent on Hilltop's net interest income, which 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. Hilltop expects to periodically experience "gaps" in the interest rate sensitivities of Hilltop's banking segment's assets and liabilities, meaning that either Hilltop's interest-bearing liabilities will be more sensitive to changes in market interest rates than Hilltop's interest-earning assets, or vice versa. In either event, if market interest rates should move contrary to Hilltop's position, this "gap" may work against Hilltop, and Hilltop's earnings may be adversely affected.

An increase in the general level of interest rates may also, among other things, adversely affect the demand for loans and Hilltop's ability to originate loans. In particular, if mortgage interest rates increase, the demand for residential mortgage loans and the refinancing of residential mortgage loans will likely decrease, which will have an adverse effect on Hilltop's income generated from mortgage origination activities. Conversely, a decrease in the general level of interest rates, among other things, may lead to prepayments on Hilltop's loan and mortgage-backed securities portfolios and increased competition for deposits. Accordingly, changes in the general level of market interest rates may adversely affect Hilltop's net yield on interest-earning assets, loan origination volume and Hilltop's overall results.

Hilltop's insurance segment invested over 87% of its invested assets in fixed maturity assets such as bonds and mortgage-backed securities at June 30, 2014. Because bond trading prices decrease as interest rates rise, a significant increase in interest rates could have a material adverse effect on Hilltop's insurance segment's financial condition and results of operations. On the other hand, decreases in interest rates could have an adverse effect on Hilltop's insurance segment's investment income and results of operations. For example, if interest rates decline, investment of new premiums received and funds reinvested will earn less. Additionally, mortgage-backed securities typically are prepaid more quickly when interest rates fall and the holder must reinvest the proceeds at lower interest rates. In periods of increasing interest rates, mortgage-backed securities typically are prepaid more slowly, which may require Hilltop's insurance segment to receive interest payments that are below the then prevailing interest rates for longer time periods than expected. The volatility of Hilltop's insurance segment's claims may force it to liquidate securities, which may cause it to incur capital losses. If Hilltop's insurance segment's investment portfolio is not appropriately matched with its insurance liabilities, it may be forced to liquidate investments prior to maturity at a significant loss to cover these liabilities. In addition, if Hilltop experiences market disruption and volatility, such as that experienced in 2009 and 2010, Hilltop may experience additional losses on Hilltop's investments and reductions in Hilltop's earnings. Investment losses could significantly decrease the asset base and statutory surplus of Hilltop's insurance segment, thereby adversely affecting its ability to conduct business and potentially its A.M. Best financial strength rating.

Hilltop's financial advisory segment holds securities, principally fixed-income municipal bonds, to support sales, underwriting and other customer activities. If interest rates increase, the value of debt securities held in the financial advisory segment's inventory would decrease. Rapid or significant changes in interest rates could adversely affect the segment's bond sales, underwriting activities and financial advisory businesses.

In addition, Hilltop holds securities that may be sold in response to changes in market interest rates, changes in securities' prepayment risk, increases in loan demand, general liquidity needs and other similar factors are classified as available for sale and are carried at estimated fair value, which may fluctuate with changes in market interest rates. The effects of an increase in market interest rates may result in a decrease in the value of Hilltop's available for sale investment portfolio.

Market interest rates are affected by many factors outside of Hilltop's control, including inflation, recession, unemployment, money supply, international disorder and instability in domestic and foreign financial markets. Hilltop may not be able to accurately predict the likelihood, nature and magnitude of such changes or how and to what extent such changes may affect Hilltop's business. Hilltop also may not be able to adequately prepare for, or compensate for, the consequences of such changes. Any failure to predict and prepare for changes in interest rates, or adjust for the consequences of these changes, may adversely affect Hilltop's earnings and capital levels and overall results of operations.

Hilltop's banking segment is subject to funding risks associated with its high deposit concentration and its potential reliance on brokered deposits.

At June 30, 2014, the Bank's fifteen largest depositors, excluding Hilltop and First Southwest Holdings, LLC, a wholly owned subsidiary of PlainsCapital ("First Southwest"), accounted for 13.26% of the Bank's total deposits, and the Bank's five largest depositors, excluding First Southwest, accounted for 8.63% of the Bank's total deposits. Brokered deposits at June 30, 2014 accounted for 3.8% of the Bank's total deposits, and Hilltop may increase Hilltop's reliance on brokered deposits in the future. The loss of one or more of Hilltop's largest Bank customers, a significant decline in Hilltop's deposit balances due to ordinary course fluctuations related to these customers' businesses, or if Hilltop increases its reliance on brokered deposits, the loss of a significant amount of Hilltop's brokered deposits could adversely affect Hilltop's liquidity. Additionally, such circumstances could require Hilltop to raise deposit rates in an attempt to attract new deposits, or purchase federal funds or borrow funds on a short-term basis at higher rates, which would adversely affect Hilltop's results of operations. Under applicable regulations, if the Bank were no longer "well capitalized," the Bank would not be able to accept brokered deposits without the approval of the FDIC.

Hilltop is heavily dependent on dividends from its subsidiaries.

Hilltop is a financial holding company engaged in the business of managing, controlling and operating its subsidiaries, including National Lloyds Corporation ("NLC") and its two insurance company subsidiaries, NLIC and ASIC, as well as the Bank and the Bank's subsidiaries, PrimeLending and First Southwest. Hilltop conducts no material business or other activity other than activities incidental to holding stock in NLC and the Bank. As a result, Hilltop relies substantially on the profitability of, and dividends from, these subsidiaries to pay its operating expenses, to satisfy its obligations and to pay dividends on its preferred stock. As with most financial institutions, the profitability of the Bank is subject to the fluctuating cost and availability of money, changes in interest rates and in economic conditions in general. PrimeLending and First Southwest contribute to the Bank's profitability and, in turn, on its ability to pay dividends to Hilltop. If the Bank, however, is unable to make cash distributions to Hilltop, then Hilltop may also be unable to obtain funds from PrimeLending and First Southwest, and Hilltop may be unable to satisfy its obligations or make distributions on its preferred stock.

Likewise, Hilltop's insurance segment also operates as a holding company. Dividends and other permitted payments from its operating subsidiaries are expected to be its primary source of funds to meet ongoing cash requirements, including any future debt service payments and other expenses, and to pay dividends, if any, to Hilltop. NLIC and ASIC are subject to significant regulatory restrictions and limitations under debt agreements limiting their ability to declare and pay dividends, including the indenture governing NLIC's London Interbank Offered Rate ("LIBOR") plus 3.40% notes due 2035 and the surplus indentures governing NLIC's two LIBOR plus 4.10% and 4.05% notes due 2033 and ASIC's LIBOR plus 4.05% notes due 2034. Together these restrictions could, in turn, limit NLC's ability to pay dividends.

Hilltop is subject to extensive supervision and regulation that could restrict its activities and impose financial requirements or limitations on the conduct of its business and limit its ability to generate income.

Hilltop is subject to extensive federal and state regulation and supervision, including that of the Federal Reserve Board, the Texas Department of Banking, the Texas Department of Insurance, the FDIC, the CFPB, the SEC and FINRA. Banking regulations are primarily intended to protect depositors' funds, federal deposit insurance funds and the banking system as a whole, not stockholders. Insurance regulations promulgated by state insurance departments are primarily intended to protect policyholders rather than stockholders. Likewise, regulations promulgated by FINRA are primarily intended to protect customers of broker-dealer businesses rather than stockholders.

These regulations affect Hilltop's lending practices, capital structure, capital requirements, investment practices, dividend policy and growth, among other things. Failure to comply with laws, regulations or policies could result in damages, civil money penalties or reputational damage, as well as sanctions and supervisory actions by regulatory agencies that could subject Hilltop to significant restrictions on its business and its ability to expand through acquisitions or branching. While Hilltop has implemented policies and procedures designed to prevent any such violations of laws and regulations, such violations may occur from time to time, which could have a material adverse effect on its financial condition and results of operations.

The U.S. Congress and federal regulatory agencies frequently revise banking and securities laws, regulations and policies. The Dodd-Frank Act, which became law in July 2010, has had, and will continue to have, a significant effect on the regulation of financial institutions and the financial services industry. The Dodd-Frank Act, among other things, established the CFPB and requires the CFPB and other federal agencies to implement many provisions of the Dodd-Frank Act. Hilltop expects that several aspects of the Dodd-Frank Act may affect its business, including, without limitation, increased capital requirements, increased mortgage regulation, restrictions on proprietary trading in securities, restrictions on investments in hedge funds and private equity funds, executive compensation restrictions and disclosure and reporting requirements. At this time, it is difficult to predict the extent to which the Dodd-Frank Act or the resulting rules and regulations will affect Hilltop's business. Compliance with these new laws and regulations likely will result in additional costs, which could be significant and may adversely impact Hilltop's results of operations, financial condition, and liquidity. For additional discussion of the Dodd-Frank Act, see "Information About the Companies Hilltop Government Supervision and Regulation" included elsewhere in this proxy statement/prospectus.

During the second quarter of 2013, the Bank received a "satisfactory" CRA rating in connection with its most recent CRA performance evaluation. A CRA rating of less than "satisfactory" adversely affects a bank's ability to establish new branches and impairs a bank's ability to commence new activities that are "financial in nature" or acquire companies engaged in these activities. Other regulatory exam ratings or findings also may otherwise impact Hilltop's ability to branch, commence new activities or make acquisitions.

Hilltop cannot predict whether or in what form any other proposed regulations or statutes will be adopted or the extent to which its business may be affected by any new regulation or statute. Such changes could subject Hilltop's business to additional costs, limit the types of financial services and products it may offer and increase the ability of non-banks to offer competing financial services and products, among other things.

The impact of the changing regulatory capital requirements and new capital rules are uncertain.

In July 2013, the Federal Reserve Board approved a final rule that will substantially amend the risk-based capital rules applicable to Hilltop and the Bank. The final rule implements the Basel III regulatory capital reforms and changes required by the Dodd-Frank Act. The final rule includes new minimum risk-based capital and leverage ratios, which will be effective for Hilltop and the Bank on January 1, 2015, and refines the definition of what constitutes "capital" for purposes of calculating these ratios. The new minimum capital requirements will be: (i) a new common equity Tier 1 capital ratio of 4.5%; (ii) a Tier 1 to risk-based assets capital ratio of 6% (increased from 4%); (iii) a total capital ratio of 8% (unchanged from current rules); and (iv) a Tier 1 leverage ratio of 4%. The final rule also establishes a "capital conservation buffer" of 2.5% above the new regulatory minimum capital ratios and will result in the following minimum ratios: (i) a common equity Tier 1 capital ratio of 7.0%; (ii) a Tier 1 to risk-based assets capital ratio of 8.5%; and (iii) a total capital ratio of 10.5%. The new capital conservation buffer requirement would be phased in beginning in January 2016 at 0.625% of risk-weighted assets and would increase each year until fully implemented in January 2019. An institution will be subject to limitations on paying dividends, engaging in share repurchases, and paying discretionary bonuses if its capital level falls below the buffer amount. These limitations will establish a maximum percentage of eligible retained income that can be utilized for such actions. The application of more stringent capital requirements for Hilltop and the Bank could, among other things, adversely affect Hilltop's results of operations and growth, require the raising of additional capital, restrict its ability to pay dividends or repurchase shares and result in regulatory actions if Hilltop were to be unable to comply with such requirements.

In addition, the Federal Reserve Board adopted a final rule in February 2014 that clarifies how companies should incorporate the Basel III regulatory capital reforms into their capital and business projections during the 2014 and subsequent cycles of capital plan submissions and stress tests required under the Dodd-Frank Act. For companies and their subsidiary banks with between $10.0 billion and $50.0 billion in total consolidated assets, the initial stress testing cycle began on October 1, 2013 and the initial nine-quarter planning horizon for stressed capital projections continues through the fourth quarter of 2015, which overlaps with the implementation of the Basel III capital reforms beginning on January 1, 2015. At June 30, 2014, Hilltop and the Bank had approximately $9.4 billion and $8.2 billion, respectively, in total consolidated assets and their average of total consolidated assets for the four most recent consecutive quarters was $9.1 billion and $8.1 billion, respectively. Accordingly, Hilltop and the Bank are not currently subject to capital planning and stress testing requirements. However, as a result of the proposed merger, Hilltop will have more than $10.0 billion in assets and will become subject to the stress testing requirements, which would likely increase Hilltop's cost of regulatory compliance. Management continues to study the implementation of Basel III regulatory capital reforms and stress testing requirements.

The CFPB recently issued "ability-to-repay" and "qualified mortgage" rules that may have a negative impact on Hilltop's loan origination process and foreclosure proceedings, which could adversely affect Hilltop's business, operating results, and financial condition.

On January 10, 2013, the CFPB issued a final rule to implement the "qualified mortgage" provisions of the Dodd-Frank Act requiring mortgage lenders to consider consumers' ability to repay home loans before extending them credit. The CFPB's "qualified mortgage" rule took effect on January 10, 2014. The final rule describes certain minimum requirements for lenders making ability-to-repay determinations, but does not dictate that they follow particular underwriting models. Lenders will be presumed to have complied with the ability-to-repay rule if they issue "qualified mortgages," which are generally defined as mortgage loans prohibiting or limiting certain risky features. Loans that do not meet the ability-to-repay standard can be challenged in court by borrowers who default and the absence of ability-to-repay status can be used against a lender in foreclosure proceedings. Any loans that Hilltop makes outside of the "qualified mortgage" criteria could expose Hilltop to an increased risk of liability and reduce or delay Hilltop's ability to foreclose on the underlying property. It is difficult to predict how the CFPB's "qualified mortgage" rule will impact Hilltop when it takes effect, but any decreases in loan origination volume or increases in compliance and foreclosure costs caused by the rule could negatively affect Hilltop's business, operating results and financial condition.

Hilltop's mortgage origination segment is subject to investment risk on loans that it originates.

Hilltop intends to sell, and not hold for investment, substantially all residential mortgage loans that it originates through PrimeLending. At times, however, Hilltop may originate a loan or execute an interest rate lock commitment ("IRLC") with a customer pursuant to which Hilltop agrees to originate a mortgage loan on a future date at an agreed-upon interest rate without having identified a purchaser for such loan or the loan underlying such IRLC. An identified purchaser may also decline to purchase a loan for a variety of reasons. In these instances, Hilltop will bear interest rate risk on an IRLC until, and unless, Hilltop is able to find a buyer for the loan underlying such IRLC and the risk of investment on a loan until, and unless, Hilltop is able to find a buyer for such loan. In addition, if a customer defaults on a mortgage payment shortly after the loan is originated, the purchaser of the loan may have a put right, whereby the purchaser can require Hilltop to repurchase the loan at the full amount that it paid. During periods of market downturn, Hilltop has at times chosen to hold mortgage loans when the identified purchasers have declined to purchase such loans because it could not obtain an acceptable substitute bid price for such loan. The failure of mortgage loans that Hilltop holds on its books to perform adequately could have a material adverse effect on Hilltop's financial condition, liquidity and results of operations.

Changes in interest rates may change the value of Hilltop's mortgage servicing rights portfolio which may increase the volatility of Hilltop's earnings.

Hilltop has recently expanded, and may continue to expand, its residential mortgage servicing operations within its mortgage origination segment. As a result of Hilltop's mortgage servicing business, Hilltop has a portfolio of mortgage servicing rights ("MSR"). A MSR is the right to service a mortgage loan collect principal, interest and escrow amounts for a fee. Hilltop measures and carries all of its residential MSRs using the fair value measurement method. Fair value is determined as the present value of estimated future net servicing income, calculated based on a number of variables, including assumptions about the likelihood of prepayment by borrowers.

One of the principal risks associated with MSRs is that in a declining interest rate environment, they will likely lose a substantial portion of their value as a result of higher than anticipated prepayments. Moreover, if prepayments are greater than expected, the cash Hilltop receives over the life of the mortgage loans would be reduced. In the future, Hilltop may use various derivative financial instruments to provide a level of protection against such interest rate risk. However, no hedging strategy can protect Hilltop completely, and hedging strategies may fail because they are improperly designed, improperly executed and documented or based on inaccurate assumptions and, as a result, could actually increase Hilltop's risks and losses. The increasing size of Hilltop's MSR portfolio may increase its interest rate risk and correspondingly, the volatility of Hilltop's earnings, especially if Hilltop cannot adequately hedge the interest rate risk relating to its MSRs.

At June 30, 2014, Hilltop's MSRs had a fair value of $35.9 million. Changes in fair value of Hilltop's MSRs are recorded to earnings in each period. Depending on the interest rate environment, it is possible that the fair value of Hilltop's MSRs may be reduced in the future. If such changes in fair value significantly reduce the carrying value of Hilltop's MSRs, Hilltop's financial condition and results of operations would be negatively affected.

Hilltop's financial advisory business is subject to various risks associated with the securities industry, particularly those impacting the public finance industry.

Hilltop's financial advisory business is subject to uncertainties that are common in the securities industry. These uncertainties include:

- intense competition in the public finance and other sectors of the securities industry;
- the volatility of domestic and international financial, bond and stock markets;
- extensive governmental regulation;
- litigation; and
- substantial fluctuations in the volume and price level of securities.

As a result, the revenues and operating results of Hilltop's financial advisory segment may vary significantly from quarter to quarter and from year to year. Unfavorable financial or economic conditions could reduce the number and size of transactions in which Hilltop provides financial advisory, underwriting and other services. Disruptions in fixed income and equity markets could lead to a decline in the volume of transactions executed for customers and, therefore, to declines in revenues from commissions and clearing services. First Southwest is much smaller and has much less capital than many competitors in the securities industry. In addition, First Southwest is an operating subsidiary of the Bank, which means that its activities are limited to those that are permissible for the Bank.

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Income that Hilltop recognized as a bargain purchase gain in connection with the FNB Transaction is subject to change.

In September 2013, Hilltop assumed substantially all of the liabilities, including all of the deposits, and acquired substantially all of the assets, of FNB from the FDIC in the FNB Transaction. Hilltop acquired approximately $2.2 billion in assets and assumed $2.2 billion in liabilities in the FNB Transaction. The FNB Transaction was accounted for under the purchase method of accounting. Hilltop recorded a pre-tax bargain purchase gain totaling $12.6 million as a result of the FNB Transaction, which was included as a component of noninterest income in Hilltop's consolidated statement of operations for the year ended December 31, 2013. The amount of the gain was equal to the amount by which the estimated fair value of assets purchased exceeded the estimated fair value of liabilities assumed. The bargain purchase gain resulting from the FNB Transaction was a non-recurring gain that is not expected to be repeated in future periods. Hilltop used significant estimates and assumptions to value the identifiable assets acquired and liabilities assumed. Any revisions to its estimates could result in the recognition of additional bargain purchase gain, which would be recorded as noninterest income, or the recognition of less or no bargain purchase gain, in which case Hilltop would reduce noninterest income and may be required to record goodwill that would be subject to an ongoing impairment analysis.

Income that Hilltop recognizes in connection with the purchase discount of the credit-impaired loans acquired in the PlainsCapital Merger and the FNB Transaction and accounted for under Accounting Standards Codification 310-30 could be volatile in nature and have significant effects on reported net income.

In connection with the PlainsCapital Merger and the FNB Transaction, Hilltop acquired loans at a discount of $146.6 million and $343.1 million, respectively. The PlainsCapital Merger and the FNB Transaction were each accounted for under the purchase method of accounting. Accordingly, these discounts are amortized and accreted to interest income on a monthly basis. The effective yield and related discount accretion on credit-impaired loans is initially determined at the acquisition date based upon estimates of the timing and amount of future cash flows as well as the amount of credit losses that will be incurred. These estimates are updated quarterly. In future periods, if actual historical results combined with future projections of these factors (amount, timing, or credit losses) differ from the initial projections, the effective yield and the amount of discount recognized will change. Volatility may increase as the variance of actual results from initial projections increases. As the acquired loans are removed from Hilltop's books, the related discount will no longer be available for accretion into income. Accretion of $28.6 million and $61.8 million on loans purchased at a discount in the PlainsCapital Merger was recorded as interest income during the six months ended June 30, 2014 and the year ended December 31, 2013, respectively, and accretion of $15.3 million and $7.5 million on loans purchased at a discount in the FNB Transaction was recorded as interest income during the six months ended June 30, 2014 and the period from September 14, 2013 to December 31, 2013, respectively. As of June 30, 2014, the balance of Hilltop's discount on loans in the aggregate was $349.6 million.

Hilltop ultimately may write-off goodwill and other intangible assets resulting from business combinations.

As a result of purchase accounting in connection with Hilltop's acquisition of NLC, the PlainsCapital Merger and the FNB Transaction, Hilltop's consolidated balance sheet at June 30, 2014, contained goodwill of $251.8 million and other intangible assets of $65.3 million. On an ongoing basis, Hilltop evaluates whether facts and circumstances indicate any impairment of value of intangible assets. As circumstances change, the value of these intangible assets may not be realized by Hilltop. If Hilltop determines that a material impairment has occurred, Hilltop will be required to write-off the impaired portion of intangible assets, which could have a material adverse effect on its results of operations in the period in which the write-off occurs.

The accuracy of Hilltop's financial statements and related disclosures could be affected if Hilltop is exposed to actual conditions different from the judgments, assumptions or estimates used in Hilltop's critical accounting policies.

The preparation of financial statements and related disclosure in conformity with GAAP requires Hilltop to make judgments, assumptions and estimates that affect the amounts reported in Hilltop's consolidated financial statements and accompanying notes. Hilltop's critical accounting policies, which are included in this proxy statement/prospectus, describe those significant accounting policies and methods used in the preparation of Hilltop's consolidated financial statements that are considered "critical" by it because they require judgments, assumptions and estimates that materially impact Hilltop's consolidated financial statements and related disclosures. As a result, if future events differ significantly from the judgments, assumptions and estimates in Hilltop's critical accounting policies, such events or assumptions could have a material impact on Hilltop's audited consolidated financial statements and related disclosures.

Hilltop is dependent on its management team, and the loss of Hilltop's senior executive officers or other key employees could impair its relationship with customers and adversely affect Hilltop's business and financial results.

Hilltop's success is dependent, to a large degree, upon the continued service and skills of its existing management team and other key employees with long-term customer relationships. Hilltop's business and growth strategies are built primarily upon its ability to retain employees with experience and business relationships within their respective segments. The loss of one or more of these key personnel could have an adverse impact on Hilltop's business because of their skills, knowledge of the market, years of industry experience and the difficulty of finding qualified replacement personnel. In addition, Hilltop currently does not have non-competition agreements with certain members of management and other key employees. If any of these personnel were to leave and compete with Hilltop, its business, financial condition, results of operations and growth could suffer.

A decline in the market for advisory services could adversely affect Hilltop's business and results of operations.

Hilltop's financial advisory segment has historically earned a significant portion of its revenues from advisory fees paid to it by its clients, in large part upon the successful completion of the client's transaction. Financial advisory revenues from the public finance group of First Southwest represented the largest component of Hilltop's financial advisory segment's net revenues for the year ended December 31, 2013. Unlike other investment banks, First Southwest earns most of its revenues from its advisory fees and, to a lesser extent, from other business activities such as commissions and underwriting. New issuances in the municipal market by cities, counties, school districts, state and other governmental agencies, airports, healthcare institutions, institutions of higher education and other clients that First Southwest's public finance group serves can be subject to significant fluctuations based on by factors such as changes in interest rates, property tax bases, budget pressures on certain issuers caused by uncertain economic times and other factors. Hilltop expects that the reliance of its financial advisory segment on advisory fees will continue for the foreseeable future, and a decline in public finance advisory engagements or the market for advisory services generally would have an adverse effect on Hilltop's business and results of operations.

Negative publicity regarding Hilltop, or financial institutions in general, could damage Hilltop's reputation and adversely impact its business and results of operations.

Hilltop's ability to attract and retain customers and conduct its business could be adversely affected to the extent Hilltop's reputation is damaged. Reputational risk, or the risk to its business, earnings and capital from negative public opinion regarding Hilltop, or financial institutions in general, is inherent in its business. Adverse perceptions concerning Hilltop's reputation could lead to difficulties in generating and maintaining accounts as well as in financing them. In particular, negative perceptions concerning Hilltop's reputation could lead to decreases in the level of deposits that consumer and commercial customers and potential customers choose to maintain with Hilltop. Negative public opinion could result from actual or alleged conduct in any number of activities or circumstances, including lending or foreclosure practices; sales practices; corporate governance and potential conflicts of interest; ethical failures or fraud, including alleged deceptive or unfair lending or pricing practices; regulatory compliance; protection of customer information; cyber-attacks, whether actual, threatened, or perceived; negative news about Hilltop or the financial institutions industry generally; general company performance; or from actions taken by government regulators and community organizations in response to such activities or circumstances. Furthermore, Hilltop's failure to address, or the perception that it has failed to address, these issues appropriately could impact Hilltop's ability to keep and attract customers and/or employees and could expose Hilltop to litigation and/or regulatory action, which could have an adverse effect on Hilltop's business and results of operations.

Hilltop's operational systems and networks have been, and will continue to be, subject to an increasing risk of continually evolving cybersecurity or other technological risks, which could result in a loss of customer business, financial liability, regulatory penalties, damage to Hilltop's reputation or the disclosure of confidential information.

Hilltop relies heavily on communications and information systems to conduct its business and maintain the security of confidential information and complex transactions, which subjects Hilltop to an increasing risk of cyber incidents from these activities due to a combination of new technologies and the increasing use of the Internet to conduct financial transactions, as well as a potential failure of interruption or breach in the security of these systems, including those that could result from attacks or planned changes, upgrades and maintenance of these systems. Such cyber incidents could result in failures or disruptions in Hilltop's customer relationship management, securities trading, general ledger, deposits, computer systems, electronic underwriting servicing or loan origination systems. Third parties with which Hilltop does business may also be sources of cybersecurity or other technological risks.

Although Hilltop devotes significant resources to maintain and regularly upgrade its systems and networks with measures such as intrusion and detection prevention systems and monitoring firewalls to safeguard critical business applications, there is no guarantee that these measures or any other measures can provide absolute security. Hilltop's computer systems, software and networks may be adversely affected by cyber incidents such as unauthorized access; loss or destruction of data (including confidential client information); account takeovers; unavailability of service; computer viruses or other malicious code; cyber attacks; and other events. These threats may derive from human error, fraud or malice on the part of employees or third parties, or may result from accidental technological failure. Additional challenges are posed by external extremist parties, including foreign state actors, in some circumstances, as a means to promote political ends. If one or more of these events occurs, it could result in the disclosure of confidential client information, damage to Hilltop's reputation with its clients and the market, customer dissatisfaction, additional costs such as repairing systems or adding new personnel or protection technologies, regulatory penalties, exposure to litigation and other financial losses to both Hilltop and its clients and customers. Such events could also cause interruptions or malfunctions in Hilltop's operations.

Hilltop has been the subject of denial of services attacks from external sources that have limited or interrupted the availability of its online banking services. Although to date Hilltop is are not aware of any material losses relating to cyber attacks or other information security breaches, it may suffer such losses in the future. Hilltop has taken steps to improve and upgrade the security of its systems in response to such threats, such incidents could occur again, but they could occur more frequently or on a more significant scale.

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Hilltop faces strong competition from other financial institutions and financial service and insurance companies, which may adversely affect its operations and financial condition.

Hilltop's banking and mortgage origination businesses face vigorous competition from banks and other financial institutions, including savings and loan associations, savings banks, finance companies and credit unions. A number of these banks and other financial institutions have substantially greater resources and lending limits, larger branch systems and a wider array of banking services than Hilltop does. Hilltop also competes with other providers of financial services, such as money market mutual funds, brokerage firms, consumer finance companies, insurance companies and governmental organizations, each of which may offer more favorable financing than Hilltop is able to provide. In addition, some of Hilltop's non-bank competitors are not subject to the same extensive regulations that govern Hilltop. The banking business in Texas has become increasingly competitive over the past several years, and Hilltop expects the level of competition it faces to further increase. Hilltop's profitability depends on its ability to compete effectively in these markets. This competition may reduce or limit Hilltop's margins on banking services, reduce Hilltop's market share and adversely affect Hilltop's results of operations and financial condition.

The insurance industry also is highly competitive and has, historically, been characterized by periods of significant price competition, alternating with periods of greater pricing discipline during which competitors focus on other factors. In the current market environment, competition in Hilltop's insurance business' industry is based primarily on products offered, service, experience, the strength of agent and policyholder relationships, reputation, speed and accuracy of claims payment, perceived financial strength, ratings, scope of business, commissions paid and policy and contract terms and conditions. Hilltop's insurance business competes with many other insurers, including large national companies who have greater financial, marketing and management resources than Hilltop's insurance segment. Many of these competitors also have better ratings and market recognition than Hilltop's insurance business. Hilltop's insurance segment seeks to distinguish itself from its competitors by providing a broad product line and targeting those market segments that provide the best opportunity to earn an underwriting profit.

In addition, a number of new, proposed or potential industry developments also could increase competition in Hilltop's insurance business' industry. These developments include changes in practices and other effects caused by the Internet (including direct marketing campaigns by Hilltop's insurance segment's competitors in established and new geographic markets), which have led to greater competition in the insurance business and increased expectations for customer service. These developments could prevent Hilltop's insurance business from expanding its book of business. Hilltop's insurance business also faces competition from new entrants into the insurance market. New entrants do not have historic claims or losses to address and, therefore, may be able to price policies on a basis that is not favorable to Hilltop's insurance business. New competition could reduce the demand for Hilltop's insurance segment's insurance products, which could have a material adverse effect on its financial condition and results of operations.

The financial advisory and investment banking industries also are intensely competitive industries and will likely remain competitive. Hilltop's financial advisory business competes directly with numerous other financial advisory and investment banking firms, broker-dealers and banks, including large national and major regional firms and smaller niche companies, some of whom are not broker-dealers and, therefore, not subject to the broker-dealer regulatory framework. In addition to competition from firms currently in the industry, there has been increasing competition from others offering financial services, including automated trading and other services based on technological innovations. Hilltop's financial advisory business competes on the basis of a number of factors, including the quality of advice and service, innovation, reputation and price. Many of Hilltop's financial advisory segment's competitors in the investment banking industry have a greater range of products and services, greater financial and marketing resources, larger customer bases, greater name recognition, more managing directors to serve their clients' needs, greater global reach and more established relationships with their customers than Hilltop's financial advisory business. Additionally, certain competitors of Hilltop's financial advisory business have reorganized or plan to reorganize from investment banks into bank holding companies which may provide them with a competitive advantage. These larger and better capitalized competitors may be more capable of responding to changes in the investment banking market, to compete for skilled professionals, to finance acquisitions, to fund internal growth and to compete for market share generally. Increased pressure created by any current or future competitors, or by competitors of Hilltop's financial advisory business collectively, could materially and adversely affect Hilltop's business and results of operations. Increased competition may result in reduced revenue and loss of market share. Further, as a strategic response to changes in the competitive environment, Hilltop's financial advisory business may from time to time make certain pricing, service or marketing decisions that also could materially and adversely affect Hilltop's business and results of operations.

Hilltop's mortgage origination and insurance businesses are subject to seasonal fluctuations and, as a result, Hilltop's results of operations for any given quarter may not be indicative of the results that may be achieved for the full fiscal year.

Hilltop's mortgage origination business is subject to several variables that can impact loan origination volume, including seasonal and interest rate fluctuations. Hilltop typically experiences increased loan origination volume from purchases of homes during the second and third calendar quarters, when more people tend to move and buy or sell homes. In addition, an increase in the general level of interest rates may, among other things, adversely affect the demand for mortgage loans and Hilltop's ability to originate mortgage loans. In particular, if mortgage interest rates increase, the demand for residential mortgage loans and the refinancing of residential mortgage loans will likely decrease, which will have an adverse effect on Hilltop's mortgage origination activities. Conversely, a decrease in the general level of interest rates, among other things, may lead to increased competition for mortgage loan origination business. As a result of these variables, Hilltop's results of operations for any single quarter are not necessarily indicative of the results that may be achieved for a full fiscal year.

Generally, Hilltop's insurance segment's insured risks exhibit higher losses in the second and third calendar quarters due to a seasonal concentration of weather-related events in its primary geographic markets. Although weather-related losses (including hail, high winds, tornadoes and hurricanes) can occur in any calendar quarter, the second calendar quarter, historically, has experienced the highest frequency of losses associated with these events. Hurricanes, however, are more likely to occur in the third calendar quarter of the year.

If the actual losses and loss adjustment expenses of Hilltop's insurance segment exceed its loss and expense estimates, its financial condition and results of operations could be materially adversely affected.

The financial condition and results of operations of Hilltop's insurance segment depend upon its ability to assess accurately the potential losses associated with the risks that it insures. Hilltop's insurance segment establishes reserve liabilities to cover the payment of all losses and loss adjustment expenses incurred under the policies that it writes. These liability estimates include case estimates, which are established for specific claims that have been reported to Hilltop's insurance segment, and liabilities for claims that have been incurred but not reported ("IBNR"). Loss adjustment expenses represent expenses incurred to investigate and settle claims. To the extent that losses and loss adjustment expenses exceed estimates, NLIC and ASIC will be required to increase their reserve liabilities and reduce their income in the period in which the deficiency is identified. In addition, increasing reserves causes a reduction in policyholders' surplus and could cause a downgrade in the ratings of NLIC and ASIC. This, in turn, could diminish Hilltop's ability to sell insurance policies.

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The liability estimation process for Hilltop's insurance segment's casualty insurance coverage possesses characteristics that make case and IBNR reserving inherently less susceptible to accurate actuarial estimation than is the case with property coverages. Unlike property losses, casualty losses are claims made by third-parties of which the policyholder may not be aware and, therefore, may be reported a significant time after the occurrence, including sometimes years later. As casualty claims most often involve claims of bodily injury, assessment of the proper case estimates is a far more subjective process than claims involving property damage. In addition, in determining the case estimate for a casualty claim, information develops slowly over the life of the claim and can subject the case estimation to substantial modification well after the claim was first reported. Numerous factors impact the casualty case reserving process, such as venue, the amount of monetary damage, legislative activity, the permanence of the injury and the age of the claimant.

The effects of inflation could cause the severity of claims from catastrophes or other events to rise in the future. Increases in the values and geographic concentrations of policyholder property and the effects of inflation have resulted in increased severity of industry losses in recent years, and Hilltop's insurance segment expects that these factors will increase the severity of losses in the future. As NLC observed in 2008, the severity of some catastrophic weather events, including the scope and extent of damage and the inability to gain access to damaged properties, and the ensuing shortages of labor and materials and resulting demand surge, provide additional challenges to estimating ultimate losses. Hilltop's insurance segment's liabilities for losses and loss adjustment expenses include assumptions about future payments for settlement of claims and claims handling expenses, such as medical treatments and litigation costs. To the extent inflation causes these costs to increase above liabilities established for these costs, Hilltop's insurance segment expects to be required to increase its liabilities, together with a corresponding reduction in its net income in the period in which the deficiency is identified.

Estimating an appropriate level of liabilities for losses and loss adjustment expense is an inherently uncertain process. Accordingly, actual loss and loss adjustment expenses paid will likely deviate, perhaps substantially, from the liability estimates reflected in Hilltop's insurance segment's consolidated financial statements. Claims could exceed Hilltop's insurance segment's estimate for liabilities for losses and loss adjustment expenses, which could have a material adverse effect on its financial condition and results of operations.

If Hilltop's insurance segment cannot obtain adequate reinsurance protection for the risks it underwrites or its reinsurers do not pay losses in a timely fashion, or at all, Hilltop's insurance segment will suffer greater losses from these risks or may reduce the amount of business it underwrites, which may materially adversely affect its financial condition and results of operations.

Hilltop's insurance segment purchases reinsurance to protect itself from certain risks and to share certain risks it underwrites. During 2013 and 2012, Hilltop's insurance segment's personal lines ceded 10.2% and 12.1%, respectively, of its direct insurance premiums written (primarily through excess of loss, quota share and catastrophe reinsurance treaties) and its commercial lines ceded 4.6% and 4.9%, respectively, of its direct insurance premiums written (primarily through excess of loss and catastrophe reinsurance treaties). The total cost of reinsurance, inclusive of per risk excess and catastrophe, decreased 9.3% in the year ended December 31, 2013, which is partially attributable to reduced limits, lower rates and lower reinstatement premiums in 2013 of $0.2 million. Reinsurance cost generally fluctuates as a result of storm costs or any changes in capacity within the reinsurance market.

From time to time, market conditions have limited, and in some cases have prevented, insurers from obtaining the types and amounts of reinsurance that they have considered adequate for their business needs. Accordingly, Hilltop's insurance segment may not be able to obtain desired amounts of reinsurance. Even if Hilltop's insurance segment is able to obtain adequate reinsurance, it may not be able to obtain it from entities with satisfactory creditworthiness or negotiate terms that it deems appropriate or acceptable. Although the cost of reinsurance is, in some cases, reflected in Hilltop's insurance segment's premium rates, Hilltop's insurance segment may have guaranteed certain premium rates to its policyholders. Under these circumstances, if the cost of reinsurance were to increase with respect to policies for which Hilltop's insurance segment guaranteed the rates, Hilltop's insurance segment would be adversely affected. In addition, if Hilltop's insurance segment cannot obtain adequate reinsurance protection for the risks it underwrites, it may be exposed to greater losses from these risks or it may be forced to reduce the amount of business that it underwrites for such risks, which will reduce Hilltop's insurance segment's revenue and may have a material adverse effect on its results of operations and financial condition.

At June 30, 2014, Hilltop's insurance segment had $4.1 million in reinsurance recoverables, including ceded paid loss recoverables, ceded losses and loss adjustment expense recoverables and ceded unearned insurance premiums. Hilltop's insurance segment expects to continue to purchase substantial reinsurance coverage in the foreseeable future. Because Hilltop's insurance segment remains primarily liable to its policyholders for the payment of their claims, regardless of the reinsurance it has purchased relating to those claims, in the event that one of its reinsurers becomes insolvent or otherwise refuses to reimburse Hilltop's insurance segment for losses paid, or delays in reimbursing Hilltop's insurance segment for losses paid, its liability for these claims could materially and adversely affect its financial condition and results of operations.

Hilltop is subject to legal claims and litigation that could have a material adverse effect on its business.

Hilltop faces significant legal risks in each of the business segments in which Hilltop operates, and the volume of legal claims and amount of damages and penalties claimed in litigation and regulatory proceedings against financial service companies remains high. These risks often are difficult to assess or quantify, and their existence and magnitude often remain unknown for substantial periods of time. Substantial legal liability or significant regulatory action against Hilltop or any of Hilltop's subsidiaries could have a material adverse effect on Hilltop's results of operations or cause significant reputational harm to Hilltop, which could seriously harm Hilltop's business and prospects. Further, regulatory inquiries and subpoenas, other requests for information, or testimony in connection with litigation may require incurrence of significant expenses, including fees for legal representation and fees associated with document production. These costs may be incurred even if Hilltop is not a target of the inquiry or a party to the litigation. Any financial liability or reputational damage could have a material adverse effect on Hilltop's business, which, in turn, could have a material adverse effect on Hilltop's financial condition and results of operations.

Hilltop may be subject to environmental liabilities in connection with the foreclosure on real estate assets securing the loan portfolio of Hilltop's banking segment.

Hazardous or toxic substances or other environmental hazards may be located on the real estate that secures Hilltop's loans. If Hilltop acquires such properties as a result of foreclosure, or otherwise, Hilltop could become subject to various environmental liabilities. For example, Hilltop could be held liable for the cost of cleaning up or otherwise addressing contamination at or from these properties. Hilltop could also be held liable to a governmental entity or third party for property damage, personal injury or other claims relating to any environmental contamination at or from these properties. In addition, Hilltop could be held liable for costs relating to environmental contamination at or from Hilltop's current or former properties. Hilltop may not detect all environmental hazards associated with these properties. If Hilltop ever became subject to significant environmental liabilities, Hilltop's business, financial condition, liquidity and results of operations could be harmed.

If Hilltop fails to maintain an effective system of internal controls over financial reporting, the accuracy and timing of its financial reporting may be adversely affected.

Effective internal controls are necessary for Hilltop to provide timely and reliable financial reports and effectively prevent fraud. Any inability to provide reliable financial reports or prevent fraud could harm Hilltop's business. If Hilltop fails to maintain the adequacy of its internal controls, Hilltop's financial statements may not accurately reflect Hilltop's financial condition. Inadequate internal controls over financial reporting could impact the reliability and timeliness of Hilltop's financial reports and could cause investors to lose confidence in Hilltop's reported financial information, which could have a negative effect on Hilltop's business and the value of its securities.

The debt agreements of Hilltop's insurance segment and its controlled affiliates contain financial covenants and impose restrictions on its business.

The indenture governing NLC's LIBOR plus 3.40% notes due 2035 contains restrictions on its ability to, among other things, declare and pay dividends and merge or consolidate. In addition, this indenture contains a change of control provision, which provides that (i) if a person or group becomes the beneficial owner, directly or indirectly, of 50% or more of NLC's equity securities and (ii) if NLC's ratings are downgraded by a nationally recognized statistical rating organization (as defined in the Exchange Act), then each holder of the notes governed by such indenture has the right to require that NLC purchase such holder's notes, in whole or in part, at a price equal to 100% of the then outstanding principal amount. Likewise, the surplus indentures governing NLIC's two LIBOR plus 4.10% and 4.05% notes due 2033 and ASIC's LIBOR plus 4.05% notes due 2034 contain restrictions on dividends and mergers and consolidations. In addition, NLC has other credit arrangements with its affiliates and other third-parties.

NLC's ability to comply with these covenants may be affected by events beyond its control, including prevailing economic, financial and industry conditions. The breach of any of these restrictions could result in a default under the loan agreements or indentures governing the notes or under its other debt agreements. An event of default under its debt agreements would permit some of its lenders to declare all amounts borrowed from them to be due and payable, together with accrued and unpaid interest. If NLC were unable to repay debt to its secured lenders, these lenders could proceed against the collateral securing that debt. In addition, acceleration of its other indebtedness may cause NLC to be unable to make interest payments on the notes. Other agreements that NLC or its insurance company subsidiaries may enter into in the future may contain covenants imposing significant restrictions on their respective businesses that are similar to, or in addition to, the covenants under their respective existing agreements. These restrictions may affect NLC's ability to operate its business and may limit its ability to take advantage of potential business opportunities as they arise.

Risks Related to Hilltop's Substantial Cash Position and Related Strategies for its Use

Because Hilltop intends to use a substantial portion of its remaining available cash to make acquisitions or effect a business combination, Hilltop may become subject to risks inherent in pursuing and completing any such acquisitions or business combination.

Hilltop is endeavoring to make acquisitions or effect business combinations with a substantial portion of Hilltop's remaining available cash. Hilltop may not, however, be able to identify suitable targets, consummate acquisitions or effect a combination on commercially acceptable terms or, if consummated, successfully integrate personnel and operations.

The success of any acquisition or business combination will depend upon, among other things, the ability of management and Hilltop's employees to integrate personnel, operations, products and technologies effectively, to retain and motivate key personnel and to retain customers and clients of targets. In addition, any acquisition or business combination Hilltop undertakes may consume available cash resources, result in potentially dilutive issuances of equity securities and divert management's attention from other business concerns. Even if Hilltop conducts extensive due diligence on a target business that Hilltop acquires or with which Hilltop merges, its diligence may not surface all material issues that may adversely affect a particular target business, and Hilltop may be forced to later write-down or write-off assets, restructure Hilltop's operations or incur impairment or other charges that could result in Hilltop's reporting losses. Consequently, Hilltop also may need to make further investments to support the acquired or combined company and may have difficulty identifying and acquiring the appropriate resources.

Hilltop may enter, through acquisitions or a business combination, into new lines of business or initiate new service offerings subject to the restrictions imposed upon Hilltop as a regulated financial holding company. Accordingly, there is no basis for you to evaluate the possible merits or risks of the particular target business with which Hilltop may combine or that Hilltop may ultimately acquire.

Existing circumstances may result in several of Hilltop's directors having interests that may conflict with its interests.

A director who has a conflict of interest with respect to an issue presented to Hilltop's board will have no inherent legal obligation to abstain from voting upon that issue. Hilltop does not have provisions in its bylaws or charter that require an interested director to abstain from voting upon an issue, and Hilltop does not expect to add provisions in Hilltop's charter and bylaws to this effect. Although each director has a duty to act in good faith and in a manner he or she reasonably believes to be in Hilltop's best interests, there is a risk that, should interested directors vote upon an issue in which they or one of their affiliates has an interest, their vote may reflect a bias that could be contrary to Hilltop's best interests. In addition, even if an interested director abstains from voting, the director's participation in the meeting and discussion of an issue in which they have, or companies with which they are associated have, an interest could influence the votes of other directors regarding the issue.

Difficult market conditions have adversely affected the yield on Hilltop's available cash.

Hilltop's primary objective is to preserve and maintain the liquidity of Hilltop's available cash, while at the same time maximizing yields without significantly increasing risk. The capital and credit markets have been experiencing volatility and disruption for a prolonged period. This volatility and disruption reached unprecedented levels, resulting in dramatic declines in interest rates and other yields relative to risk. This downward pressure has negatively affected the yields Hilltop receives on its available cash. If current levels of market disruption and volatility continue or worsen, there can be no assurance that Hilltop will receive any significant yield on its available cash. Further, given current market conditions, no assurance can be given that Hilltop will be able to preserve its available cash.

Risks Related to Hilltop's Common Stock

Hilltop may issue shares of preferred stock or additional shares of common stock to complete an acquisition or effect a combination or under an employee incentive plan after consummation of an acquisition or combination, which would dilute the interests of Hilltop's stockholders and likely present other risks.

The issuance of shares of preferred stock or additional shares of common stock:

- may significantly dilute the equity interest of Hilltop's stockholders;

- may subordinate the rights of holders of common stock if preferred stock is issued with rights senior to those afforded Hilltop's common stock;

- could cause a change in control if a substantial number of shares of common stock are issued, which may affect, among other things, Hilltop's ability to use its net operating loss carry forwards; and

- may adversely affect prevailing market prices for Hilltop's common stock.

Hilltop's authorized capital stock includes ten million shares of preferred stock, and Hilltop currently has 114,068 shares of Series B Preferred Stock issued and outstanding, liquidation preference $1,000 per share, to the Secretary of the Treasury pursuant to the SBLF. Hilltop's board of directors, in its sole discretion, may designate and issue one or more additional series of preferred stock from the authorized and unissued shares of preferred stock. Subject to limitations imposed by law or Hilltop's charter, Hilltop's board of directors is empowered to determine the designation and number of shares constituting each series of preferred stock, as well as any designations, qualifications, privileges, limitations, restrictions or special or relative rights of additional series. The rights of preferred stockholders may supersede the rights of common stockholders. Preferred stock could be issued with voting and conversion rights that could adversely affect the voting power of the shares of Hilltop's common stock. The issuance of preferred stock could also result in a series of securities outstanding that would have preferences over the common stock with respect to dividends and in liquidation.

Hilltop's common stock price may experience substantial volatility, which may affect your ability to sell Hilltop's common stock at an advantageous price.

Price volatility of Hilltop's common stock may affect your ability to sell Hilltop's common stock at an advantageous price. Market price fluctuations in Hilltop's common stock may arise due to acquisitions, dispositions or other material public announcements, including those regarding dividends or changes in management, along with a variety of additional factors, including, without limitation, other risks identified in "Forward-looking Statements" and these "Risk Factors." In addition, the stock markets in general, including the NYSE, have experienced extreme price and trading fluctuations. These fluctuations have resulted in volatility in the market prices of securities that often have been unrelated or disproportionate to changes in operating performance. These broad market fluctuations may adversely affect the market price of Hilltop's common stock.

Hilltop's rights and the rights of Hilltop's stockholders to take action against Hilltop's directors and officers are limited.

Hilltop is organized under Maryland law, which provides that a director or officer has no liability in that capacity if he or she performs his or her duties in good faith, in a manner he or she reasonably believes to be in Hilltop's best interests and with the care that an ordinarily prudent person in a like position would use under similar circumstances. In addition, Hilltop's charter eliminates Hilltop's directors' and officers' liability to Hilltop and its stockholders for money damages, except for liability resulting from actual receipt of an improper benefit or profit in money, property or services or active and deliberate dishonesty established by a final judgment and that is material to the cause of action. Hilltop's bylaws require Hilltop to indemnify Hilltop's directors and officers for liability resulting from actions taken by them in those capacities to the maximum extent permitted by Maryland law. As a result, Hilltop's stockholders and Hilltop may have more limited rights against Hilltop's directors and officers than might otherwise exist under common law. In addition, Hilltop may be obligated to fund the defense costs incurred by Hilltop's directors and officers.

The Treasury's investment in Hilltop imposes restrictions and obligations upon Hilltop that could adversely affect the rights of Hilltop's common stockholders.

Hilltop's has sold 114,068 shares of Hilltop's Series B Preferred Stock, liquidation preference $1,000 per share, for $114.1 million, to the Secretary of the Treasury pursuant to the SBLF. The shares of Series B Preferred Stock are senior to shares of Hilltop's common stock with respect to dividends and liquidation preference. The terms of the Series B Preferred Stock provided for the payment of non-cumulative dividends on a quarterly basis. As long as shares of Series B Preferred Stock remain outstanding, Hilltop may not pay dividends to Hilltop's common stockholders (nor may Hilltop repurchase or redeem any shares of Hilltop's common stock) during any quarter in which Hilltop fails to declare and pay dividends on the Series B Preferred Stock and for the next three quarters following such failure. In addition, under the terms of the Series B Preferred Stock, Hilltop may only declare and pay dividends on Hilltop's common stock (or repurchase shares of Hilltop's common stock), if, after payment of such dividend, the dollar amount of Hilltop's Tier 1 capital would be at least ninety percent (90%) of Tier 1 capital as of September 27, 2011, excluding any charge-offs and redemptions of the Series B Preferred Stock.

Provisions in Hilltop's charter and bylaws, as well as applicable banking and insurance laws, could discourage acquisition bids or merger proposals, which may adversely affect the market price of Hilltop's common stock.

Authority to Issue Additional Shares. Under Hilltop's charter, its board of directors may issue up to an aggregate of ten million shares of preferred stock without stockholder action. The preferred stock may be issued, in one or more series, with the preferences and other terms designated by Hilltop's board of directors that may delay or prevent a change in control of Hilltop, even if the change is in the best interests of the SWS stockholders. At June 30, 2014, 114,068 shares of preferred stock were designated or outstanding.

Banking Laws. Any change in control of Hilltop is subject to prior regulatory approval under the Bank Holding Company Act or the Change in Bank Control Act, which may delay, discourage or prevent an attempted acquisition or change in control of Hilltop.

Insurance Laws. NLIC and ASIC are domiciled in the State of Texas. Before a person can acquire control of an insurance company domiciled in Texas, prior written approval must be obtained from the Texas Department of Insurance. Acquisition of control would be presumed on the acquisition, directly or indirectly, of ten percent or more of Hilltop's outstanding voting stock, unless the regulators determine otherwise. Prior to granting approval of an application to acquire control of a domestic insurer, the Texas Department of Insurance will consider several factors, such as:

- the financial strength of the acquirer;
- the integrity and management experience of the acquirer's board of directors and executive officers;
- the acquirer's plans for the management of the insurer;
- the acquirer's plans to declare dividends, sell assets or incur debt;
- the acquirer's plans for the future operations of the domestic insurer;
- the impact of the acquisition on continued licensure of the domestic insurer;
- the impact on the interests of Texas policyholders; and
- any anti-competitive results that may arise from the consummation of the acquisition of control.

These laws may discourage potential acquisition proposals for Hilltop and may delay, deter or prevent a change of control of Hilltop, including transactions that some or all of Hilltop's stockholders might consider desirable.

Restrictions on Calling Special Meeting, Cumulative Voting and Director Removal. Hilltop's bylaws includes a provision prohibiting the holders of less than a majority of the voting power represented by all of Hilltop's shares issued, outstanding and entitled to be voted at a proposed meeting, from calling a special meeting of stockholders. Hilltop's charter does not provide for the cumulative voting in the election of directors. In addition, Hilltop's charter provides that Hilltop's directors may be removed only for cause and then only by an affirmative vote of at least two-thirds of the votes entitled to be cast in the election of directors. Any amendment to Hilltop's charter relating to the removal of directors requires the affirmative vote of two-thirds of all of the votes entitled to be cast on the matter. These provisions of Hilltop's bylaws and charter may delay, discourage or prevent an attempted acquisition or change in control of Hilltop.

An investment in Hilltop's common stock is not an insured deposit.

An investment in Hilltop's common stock is not a bank deposit and is not insured or guaranteed by the FDIC, SIPC, the Texas Department of Insurance or any other government agency. Accordingly, you should be capable of affording the loss of any investment in Hilltop's common stock.

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FORWARD LOOKING STATEMENTS

This proxy statement/prospectus contains or incorporates by reference a number of "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, including statements about the financial conditions, results of operations, earnings outlook and prospects of Hilltop, SWS and the potential combined company and may include statements for the period following the completion of the merger. You can find many of these statements by looking for words such as "plan," "believe," "expect," "intend," "anticipate," "estimate," "budget," "indicate," "target," "project," "potential," "could," "should," "may," "possible" or other similar expressions which identify these forward-looking statements and appear in a number of places in this proxy statement/prospectus (and the documents to which we refer you in this proxy statement/prospectus) and include, but are not limited to, all statements relating directly or indirectly to the timing or likelihood of completing the merger, plans for future growth and other business development activities as well as capital expenditures, financing sources and the effects of regulation and competition and all other statements regarding our intent, plans, beliefs or expectations or those of our directors or officers.

The forward-looking statements involve certain risks and uncertainties. The ability of either Hilltop or SWS to predict results or the actual effects of its plans and strategies, or those of the combined company, is subject to inherent uncertainty. Factors that may cause actual events or results to differ materially from such forward-looking statements include those set forth under "Risk Factors" included elsewhere in, or incorporated in, this proxy statement/prospectus, as well as, among others, the following:

- those discussed and identified in public filings with the SEC made by Hilltop or SWS;
- fluctuations in the market price of Hilltop common stock and the related effect on the market value of the merger consideration that common stockholders will receive upon completion of the merger;
- business uncertainties and contractual restrictions while the merger is pending;
- the possibility that the proposed merger does not close when expected or at all because required regulatory, stockholder or other approvals and other conditions to closing are not received or satisfied on a timely basis or at all;
- the terms of the proposed merger may need to be modified to satisfy such approvals or conditions;
- the anticipated benefits from the proposed merger are not realized in the time frame anticipated or at all as a result of changes in general economic and market conditions, interest and exchange rates, monetary policy, laws and regulations (including changes to capital requirements) and their enforcement, and the degree of competition in the geographic and business areas in which the companies operate;
- the ability to promptly and effectively combine the businesses of SWS and Hilltop;
- reputational risks and the reaction of the companies' respective customers to the merger;
- diversion of management time on merger related issues;
- changes in general economic, market and business conditions;
- changes in asset quality and credit risk and risks associated with concentrations in real estate related loans;

the inability to sustain revenue and earnings;

changes in interest rates and capital markets and the value of securities held;

- inflation;
- customer borrowing, repayment, investment and deposit practices;
- the introduction, withdrawal, success and timing of business initiatives;
- changes in accounting policies;
- changes in tax and regulatory compliance requirements;
- changes in federal, state and local tax rates;
- the ability to attract and retain key personnel;
- the availability of borrowings under credit lines, credit agreements and credit facilities;
- the potential for litigation and other regulatory liability;
- technology changes;
- competitive conditions; and
- the impact, extent and timing of actions of the Federal Reserve Board and federal and state banking regulators, and legislative and regulatory actions and reforms, including those associated with the Dodd-Frank Act.

Because these forward-looking statements are subject to assumptions and uncertainties, actual results may differ materially from those expressed or implied by these forward-looking statements. You are cautioned not to place undue reliance on these statements, which speak only as of the date of this proxy statement/prospectus or the date of any document incorporated by reference in this proxy statement/prospectus. Any forward-looking statements made or incorporated in this proxy statement/prospectus are qualified in their entirety by these cautionary statements, and there can be no assurance that the actual results or developments anticipated by Hilltop or SWS will be realized or, even if substantially realized, that they will have the expected consequences to, or effects on, us or our business or operations.

All subsequent written and oral forward-looking statements concerning the merger or other matters addressed or incorporated in this proxy statement/prospectus and attributable to Hilltop or SWS or any person acting on their behalf are expressly qualified in their entirety by the cautionary statements contained or referred to in this proxy statement/prospectus. Except to the extent required by applicable law or regulation, Hilltop and SWS undertake no obligation to update these forward-looking statements to reflect events or circumstances after the date of this proxy statement/prospectus or to reflect new information or the occurrence of unanticipated events.

THE SWS SPECIAL MEETING

This section contains information about the special meeting of SWS stockholders that has been called to allow SWS stockholders to consider and vote on the merger agreement and other related matters.

Together with this proxy statement/prospectus, SWS is also sending you a notice of the SWS special meeting and a form of proxy that is solicited by the SWS board of directors for use at the special meeting and at any adjournments or postponements of the special meeting. The SWS special meeting will be held on November 21, 2014, at 9:00 a.m., local time, at Renaissance Tower, 1201 Elm Street, Suite 4200, Dallas, Texas 75270.

Matters to be Considered

At the SWS special meeting, holders of SWS common stock as of the record date will be asked to consider and vote on:

- a proposal to adopt and approve the merger agreement (the "merger proposal");
- a proposal to approve, on a non-binding, advisory basis, compensation that may be paid or would be payable to SWS's named executive officers that is based on or otherwise relates to the merger (the "compensation proposal"); and
- a proposal to approve the adjournment of the SWS special meeting, if necessary or appropriate, to solicit additional proxies, in the event that there are not sufficient votes at the time of the SWS special meeting to approve the merger proposal (the "adjournment proposal").

Proxies

Each copy of this proxy statement/prospectus mailed to holders of SWS common stock is accompanied by a form of proxy with instructions for voting. If you hold stock in your name as a stockholder of record, you may complete, sign, date and mail your proxy card in the enclosed postage paid return envelope as soon as possible, vote by telephone by calling the toll-free number listed on the SWS proxy card, vote by accessing the internet site listed on the SWS proxy card or vote in person at the SWS special meeting. If you hold your stock in "street name" through a bank or broker, you must direct your bank or broker to vote in accordance with the instruction form included with these materials and forwarded to you by your bank or broker. This voting instruction form provides instructions for voting. To vote using the proxy card you must sign, date and return it in the enclosed postage-paid envelope. Instructions on how to vote by telephone or by the internet are included with your proxy card.

If you are a holder of record, to change your vote, you must:

- mail a new signed proxy card with a later date to SWS;
- vote by calling the toll-free number listed on the SWS proxy card or accessing the internet site listed on the SWS proxy card by 11:59 p.m., Eastern Time, on November 20, 2014; or
- attend the SWS special meeting and vote in person.

If you wish to revoke rather than change your vote, you must send a written, signed revocation to SWS Group, Inc., 1201 Elm Street, Suite 3500, Dallas, Texas 75270, Attn: Corporate Secretary, which must be received prior to the exercise of the proxy. You must include your control number.

If you hold shares in "street name" and wish to change or revoke your vote, please refer to the information on the voting instruction form included with these materials and forwarded to you by your bank, broker or other holder of record to see your voting options.

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All shares represented by valid proxies that we receive through this solicitation, and that are not revoked, will be voted in accordance with your instructions on the proxy card. If you make no specification on your proxy card as to how you want your shares voted before signing and returning it, your proxy will be voted as recommended by the SWS board of directors.

SWS stockholders with shares represented by stock certificates should not send SWS stock certificates with their proxy cards. After the merger is completed, holders of SWS common stock certificates or shares of SWS common stock held in book-entry form will be mailed a transmittal form with instructions on how to exchange their SWS stock certificates or book-entry shares for the merger consideration.

Participants in the SWS 401(k) Plan

If you hold shares indirectly in the SWS 401(k) Plan, you have the right to direct the plan trustee how to vote the shares that you hold in your account. In accordance with the terms of the plan, if you fail to instruct the plan trustee how to vote your plan shares, the trustee will generally vote your plan shares in the same proportion as the shares voted pursuant to the instructions of participants who timely give such instructions.

Solicitation of Proxies

SWS will bear the entire cost of soliciting proxies from its stockholders. In addition to solicitation of proxies by mail, SWS will request that banks, brokers, and other record holders send proxies and proxy material to the beneficial owners of SWS common stock and secure their voting instructions. SWS will reimburse the record holders for their reasonable expenses in taking those actions. If necessary, SWS may use several of its regular employees, who will not be specially compensated, to solicit proxies from SWS stockholders, either personally or by telephone, facsimile, letter or other electronic means. SWS has made arrangements with MacKenzie Partners, Inc. to assist SWS in soliciting proxies and has agreed to pay them $30,000, plus reasonable expenses for these services. In addition, Hilltop has made arrangements with Innisfree M&A Incorporated to provide advisory services in connection with the merger that may include the solicitation of proxies and has agreed to pay them $25,000 plus reasonable expenses for these services.

Record Date

The close of business on October 3, 2014 has been fixed as the record date for determining the SWS stockholders entitled to receive notice of and to vote at the SWS special meeting. At that time, 48,456,850 shares of SWS common stock were outstanding, held by approximately 98 holders of record.

Quorum

In order to conduct business at the SWS special meeting, there must be a quorum. A quorum is the number of shares that must be present at the meeting, either in person or by proxy. To have a quorum at the special meeting requires the presence of stockholders or their proxies who are entitled to cast at least a majority of the votes that all stockholders are entitled to cast. Abstentions and broker non-votes will be counted for the purpose of determining whether a quorum is present.

You are entitled to one vote for each share of SWS common stock you held as of the record date.

Vote Required

Approval of the merger proposal requires the affirmative vote of a majority of the shares of SWS common stock outstanding on the record date for the SWS special meeting. Because the affirmative vote of the holders of at least a majority of the shares of SWS common stock outstanding on the record date for the SWS special meeting is needed to approve the merger proposal, an abstention or a broker non-vote will have the effect of a vote against the merger proposal. Approval of the compensation proposal and the adjournment proposal require, in each case, the affirmative vote of a majority of the shares of SWS common stock represented in person or by proxy at the SWS special meeting and entitled to vote on such proposal. An abstention or broker non-vote will have no effect on the compensation proposal or the adjournment proposal. Each holder of SWS common stock will be entitled to one vote per share on each of the proposals presented at the SWS annual meeting. As of the date of this proxy statement/prospectus, Hilltop owns 10,171,039 shares of SWS common stock, or approximately 21.0% of the currently outstanding SWS common shares.

Every SWS stockholder's vote is important. The SWS board of directors urges SWS stockholders to promptly vote by: (1) completing, signing, dating and mailing your proxy card in the enclosed postage paid return envelope as soon as possible; (2) calling the toll-free number listed on the SWS proxy card; or (3) accessing the internet site listed on the SWS proxy card. If you hold your stock in "street name" through a bank or broker, please direct your bank or broker to vote in accordance with the instruction form included with these materials and forwarded to you by your bank or broker.

Shares Held by Officers and Directors

As of the record date, to the knowledge of SWS, directors and executive officers of SWS had the right to vote approximately 2,425,026 shares of SWS common stock (not including the shares held by Hilltop described below), or approximately 5% of the outstanding shares of SWS common stock entitled to vote at the special meeting. We currently expect that each of these individuals will vote their shares of SWS common stock in favor of the proposals to be presented at the special meeting.

Shares Held by Hilltop

As of the date of this proxy statement/prospectus, Hilltop owns 10,171,039 shares of SWS common stock, or approximately 21.0% of the currently outstanding SWS common shares. Hilltop has agreed in the merger agreement to vote any shares of SWS that it owns as of the record date for the SWS special meeting in favor of approval and adoption of the merger agreement.

Recommendation of the SWS Board of Directors

The SWS board of directors (other than Messrs. Gerald J. Ford and J. Taylor Crandall, who recused themselves), upon the unanimous recommendation of the Special Committee, has approved the merger agreement and the transactions contemplated thereby, including the merger. See "The Merger Reasons for the Merger" and "The Merger Recommendation of the SWS Board of Directors" included elsewhere in this proxy statement/prospectus for a more detailed discussion of the SWS board of directors' recommendation.

The SWS board of directors (other than Messrs. Gerald J. Ford and J. Taylor Crandall, who recused themselves) recommends that you vote your shares as follows:

"**FOR**" the adoption and approval of the merger agreement;

"**FOR**" the approval, on a non-binding, advisory basis, of the compensation that may be paid or would be payable to SWS's named executive officers that is based on or otherwise relates to the merger; and

"**FOR**" the approval of the proposal to adjourn the special meeting, if necessary or appropriate, to solicit additional proxies in the event that there are not sufficient votes at the time of the special meeting to adopt and approve the merger proposal

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Attending the Special Meeting

All holders of SWS common stock, including holders of record and stockholders who hold their stock through banks, brokers, nominees or any other holder of record, are invited to attend the SWS special meeting. Only stockholders of record on the record date can vote in person at the SWS special meeting. If you are not a stockholder of record, you must obtain a proxy executed in your favor from the record holder of your shares, such as a broker, bank or other nominee, to be able to vote in person at the SWS special meeting. If you plan to attend the SWS special meeting, you must hold your shares in your own name or have a letter from the record holder of your shares confirming your ownership and you must bring a form of personal photo identification with you in order to be admitted. SWS reserves the right to refuse admittance to anyone without proper proof of share ownership and without proper photo identification.

Delivery of Proxy Materials

As permitted by applicable law, only one copy of this joint proxy statement/prospectus is being delivered to stockholders residing at the same address, unless such stockholders have notified SWS of their desire to receive multiple copies of the joint proxy statement/prospectus.

SWS will promptly deliver, upon oral or written request, a separate copy of the joint proxy statement/prospectus to any stockholder residing at an address to which only one copy of such document was mailed. Requests for additional copies should be directed to Investor Relations, at 1201 Elm Street, Suite 3500, Dallas, Texas 75270 or by telephone at (214) 859-1800.

Appraisal/Dissenter's Rights

Section 262 of the DGCL provides holders of shares of SWS common stock with the right to dissent from the merger and seek appraisal of their shares of SWS common stock in accordance with Delaware law. A holder of shares of SWS common stock who properly seeks appraisal and complies with the applicable requirements under Delaware law, referred to as a dissenting stockholder, will forego the merger consideration and instead receive a cash payment equal to the fair value of such stockholder's shares of SWS common stock in connection with the merger. Fair value will be determined by the Delaware Court of Chancery following an appraisal proceeding. Dissenting stockholders will not know the appraised fair value at the time such holders must elect whether to seek appraisal. The ultimate amount dissenting stockholders receive in an appraisal proceeding may be more or less than, or the same as, the amount such holders would have received under the merger agreement.

To seek appraisal, a stockholder of SWS must strictly comply with all of the procedures required under Delaware law, including:

- delivering a written demand for appraisal to SWS before the vote is taken on the merger agreement at the SWS special meeting;
- not voting in favor of the merger proposal; and
- continuing to hold its shares of common stock through the effective time of the merger.

In connection with the foregoing, SWS stockholders who wish to seek appraisal should note that:

- if you return a signed proxy without voting instructions, your proxy will be voted as recommended by the SWS board of directors and you may lose dissenters' rights;
- if you return a signed proxy with instructions to vote "FOR" the merger agreement, your shares will be voted in favor of the merger agreement and you will lose dissenters' rights; and

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if you wish to dissent and you execute and return a proxy, you must specify that your shares are to be either voted "AGAINST" or "ABSTAIN" with respect to approval of the merger.

Failure to follow exactly the procedures specified under Delaware law will result in the loss of appraisal rights.

For a further description of the appraisal rights available to SWS stockholders and procedures required to exercise appraisal rights, see the section entitled "The Merger Appraisal/Dissenters' Rights" included elsewhere in this joint proxy statement/prospectus and the provisions of the DGCL that grant appraisal rights and govern such procedures which are attached as Annex C to this document. If a stockholder of SWS holds shares of SWS common stock through a bank, brokerage firm or other nominee and the SWS stockholder wishes to exercise appraisal rights, such stockholder should consult with such stockholder's bank, brokerage firm or nominee. In view of the complexity of Delaware law, SWS stockholders who may wish to pursue appraisal rights should consult their legal and financial advisors promptly.

PROPOSALS SUBMITTED TO SWS STOCKHOLDERS

Adoption and Approval of the Merger Agreement (Proposal 1)

This proxy statement/prospectus is being furnished to SWS stockholders as part of the solicitation of proxies by the SWS board of directors for use at the SWS special meeting to consider and vote on the proposal to adopt and approve the merger agreement. **IF SWS STOCKHOLDERS FAIL TO ADOPT AND APPROVE THE MERGER AGREEMENT, THE MERGER CANNOT BE COMPLETED**. Holders of SWS common stock should read this proxy statement/prospectus carefully and in its entirety, including the annexes, for more detailed information concerning the merger agreement and the merger. A copy of the merger agreement is attached to this proxy statement/prospectus as Annex A.

After careful consideration, upon the unanimous recommendation of the Special Committee, the SWS board of directors (other than Messrs. Gerald J. Ford and J. Taylor Crandall, who recused themselves) determined that the merger agreement and the transactions contemplated thereby were advisable and fair to and in the best interests of the SWS stockholders and approved the merger agreement and the transactions contemplated by the merger agreement, including the merger. See "The Merger Reasons for the Merger" and "The Merger Recommendation of the SWS Board of Directors" included elsewhere in this proxy statement/prospectus for a more detailed discussion of the SWS board of directors' recommendation.

Approval of the merger proposal requires the affirmative vote of a majority of the shares of SWS common stock outstanding on the record date for the SWS special meeting.

The SWS board of directors (other than Messrs. Gerald J. Ford and J. Taylor Crandall, who recused themselves) recommends that its stockholders vote "**FOR**" the adoption and approval of the merger agreement. For a discussion of interests of SWS's directors and executive officers in the merger that may be different from, or in addition to, the interest of SWS stockholders generally, see "The Merger Interests of SWS Certain Directors and Executive Officers in the Merger" included elsewhere in this proxy statement/prospectus.

Non-Binding Advisory Vote Approving Compensation (Proposal 2)

The Dodd-Frank Act and Rule 14a-21(c) under the Exchange Act require SWS to provide its stockholders with the opportunity to vote to approve, on a non-binding, advisory basis, the compensation that may be paid or would be payable to the named executive officers of SWS that is based on or otherwise relates to the merger. Information required by Item 402(t) of Regulation S-K concerning this compensation, subject to certain assumptions described herein, is presented under the heading "The Merger Interests of SWS Directors and Executive Officers in the Merger Golden Parachute Compensation."

Accordingly, SWS is requesting that holders of SWS common stock approve the following resolution:

> "RESOLVED, that the stockholders of SWS Group, Inc. approve, on a non-binding advisory basis, the compensation that may be paid or would be payable to its named executive officers that is based on or otherwise relates to the merger, as disclosed in the proxy statement/prospectus relating to the SWS special meeting in the table titled "Golden Parachute Compensation" pursuant to Item 402(t) of Regulation S-K, including the related footnotes and associated narrative discussion."

Approval of this proposal is not a condition to completion of the merger. **While the SWS board of directors intends to consider the vote resulting from this proposal, the vote is advisory, and therefore not binding on SWS or on Hilltop or the board of directors or the compensation committees of SWS or Hilltop**. Accordingly, such compensation, including amounts that SWS is contractually obligated to pay, would still be payable regardless of the outcome of this advisory vote, subject only to the conditions applicable thereto.

Approval of the compensation proposal requires the affirmative vote of a majority of the shares of SWS common stock represented in person or by proxy at the special meeting and entitled to vote on the proposal.

The SWS board of directors recommends (other than Messrs. Gerald J. Ford and J. Taylor Crandall, who recused themselves) that its stockholders vote "**FOR**" the approval, on a non-binding, advisory basis, of the compensation that may be paid or would be payable to SWS's named executive officers that is based on or otherwise relates to the merger.

Approval of the Adjournment or Postponement of the SWS Special Meeting (Proposal 3)

The SWS special meeting may be adjourned to another time or place, if necessary or appropriate, to permit, among other things, further solicitation of proxies if necessary to obtain additional votes in favor of the merger proposal.

If, at the SWS special meeting, the number of shares of SWS common stock present or represented and voting in favor of the merger proposal is insufficient to approve such proposal, SWS intends to move to adjourn the SWS special meeting in order to solicit additional proxies for the adoption and approval of the merger agreement. In accordance with the SWS bylaws, a vote to approve the proposal to adjourn the SWS special meeting, if necessary or appropriate, to solicit additional proxies if there are insufficient votes at the time of the SWS special meeting to approve the merger proposal may be taken in the absence of a quorum. **SWS does not intend to call a vote on this proposal if the merger proposal has been approved at the SWS special meeting.**

In this proposal, SWS is asking its stockholders to authorize the holder of any proxy solicited by the SWS board of directors to vote in favor of granting discretionary authority to proxy holders, and each of them individually, to adjourn the SWS special meeting to another time and place for the purpose of soliciting additional proxies. If SWS stockholders approve this adjournment proposal, SWS could adjourn the SWS special meeting and any adjourned session of the SWS special meeting and use the additional time to solicit additional proxies, including the solicitation of proxies from SWS stockholders who have previously voted.

Approval of the adjournment proposal requires the affirmative vote of a majority of the shares of SWS common stock represented in person or by proxy at the SWS special meeting and entitled to vote on the proposal.

The SWS board of directors (other than Messrs. Gerald J. Ford and J. Taylor Crandall, who recused themselves) recommends that holders of SWS common stock vote "**FOR**" the approval of the proposal to adjourn the special meeting, if necessary or appropriate, to solicit additional proxies in the event that there are not sufficient votes at the time of the special meeting to adopt and approve the merger agreement.

INFORMATION ABOUT THE COMPANIES HILLTOP

Unless the context otherwise indicates, all references in this "Information About the Companies Hilltop" section to the "Company," "we," "us," "our" or "ours" or similar words are to Hilltop Holdings Inc. and its direct and indirect wholly owned subsidiaries (and, for avoidance of doubt, do not refer to SWS), references to "Hilltop" refer solely to Hilltop Holdings Inc., references to "PlainsCapital" refer to PlainsCapital Corporation (a wholly owned subsidiary of Hilltop), references to the "Bank" refer to PlainsCapital Bank (a wholly owned subsidiary of PlainsCapital), references to "FNB" refer to First National Bank, references to "First Southwest" refer to First Southwest Holdings, LLC (a wholly owned subsidiary of the Bank) and its subsidiaries as a whole, references to "FSC" refer to First Southwest Company (a wholly owned subsidiary of First Southwest), references to "PrimeLending" refer to PrimeLending, a PlainsCapital Company (a wholly owned subsidiary of the Bank) and its subsidiaries as a whole, and references to "NLC" refer to National Lloyds Corporation (a wholly owned subsidiary of Hilltop) and its subsidiaries as a whole.

Business

Company Background

Beginning in 1995, we operated as several companies under the name "Affordable Residential Communities" or "ARC," a Maryland corporation. We engaged in the business of acquiring, renovating, repositioning and operating manufactured home communities, as well as certain related businesses.

In January 2007, we acquired NLC, a property and casualty insurance holding company.

On July 31, 2007, we sold substantially all of the operating assets used in our manufactured home communities business and our retail sales and financing business to American Residential Communities LLC. In conjunction with this transaction, we transferred to the buyer the rights to the "Affordable Residential Communities" name, changed our name to Hilltop Holdings Inc., and moved our headquarters to Dallas, Texas. As a result, our primary operations from August 2007 through November 2012 were limited to providing fire and homeowners insurance to low value dwellings and manufactured homes primarily in Texas and other areas of the southern United States through NLC. NLC operates through its wholly owned subsidiaries, National Lloyds Insurance Company ("NLIC") and American Summit Insurance Company ("ASIC").

On November 30, 2012, we acquired PlainsCapital Corporation through a plan of merger (the "PlainsCapital Merger"), whereby PlainsCapital Corporation merged into our wholly owned subsidiary, which continued as the surviving entity under the name "PlainsCapital Corporation". Concurrent with the consummation of the PlainsCapital Merger, we became a financial holding company registered under the Bank Holding Company Act of 1956 (the "Bank Holding Company Act"), as amended by the Gramm-Leach-Bliley Act of 1999 (the "Gramm-Leach-Bliley Act").

On September 13, 2013, the Bank assumed substantially all of the liabilities, including all of the deposits, and acquired substantially all of the assets, of FNB from the FDIC, as receiver, and reopened former FNB branches acquired from the FDIC under the "PlainsCapital Bank" name (the "FNB Transaction").

We intend to make acquisitions with certain of the remaining proceeds from the American Residential Communities transaction and, if necessary or appropriate, from additional equity or debt financing sources.

Following the PlainsCapital Merger, our primary line of business has been to provide business and consumer banking services from offices located throughout central, north and west Texas through the Bank. The acquisition of FNB's expansive branch network allows the Bank to further develop its Texas footprint through expansion into the Rio Grande Valley, Houston, Corpus Christi, Laredo and El Paso markets, among others. In addition to the Bank, our other subsidiaries have specialized areas of expertise that allow us to provide an array of financial products and services such as mortgage origination, insurance and financial advisory services.

At June 30, 2014, on a consolidated basis, we had total assets of $9.4 billion, total deposits of $6.2 billion, total loans, including loans held for sale, of $6.0 billion and stockholders' equity of $1.4 billion. Our operating results beginning December 1, 2012 include the banking, mortgage origination and financial advisory operations acquired in the PlainsCapital Merger and the results of our banking operations include the operations acquired in the FNB Transaction since September 14, 2013.

Our common stock is listed on the New York Stock Exchange, or NYSE, under the symbol "HTH."

Our principal office is located at 200 Crescent Court, Suite 1330, Dallas, Texas 75201, and our telephone number at that location is (214) 855-2177. Our internet address is www.hilltop-holdings.com. Our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act are available on our website at http://ir.hilltop-holdings.com/ under the tab "SEC Filings" as soon as reasonably practicable after we electronically file such reports with, or furnish them to, the Securities and Exchange Commission (the "SEC"). The references to our website in this proxy statement/prospectus are inactive textual references only. The information on our website is not incorporated by reference into this proxy statement/prospectus.

Organizational Structure

Our organizational structure is comprised of two primary operating business units, NLC (insurance) and PlainsCapital (financial services and products). Within the PlainsCapital unit are three primary wholly owned operating subsidiaries: the Bank, PrimeLending and First Southwest. The following provides additional details regarding our updated organizational structure at June 30, 2014.

Geographic Dispersion of our Businesses

The Bank provides traditional banking services, residential mortgage lending, wealth and investment management, treasury management and capital equipment leasing. Substantially all of our banking operations are in Texas, and as a result of the FNB Transaction, the Bank has a presence in every major market in Texas.

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For the year ended December 31, 2013, approximately 66% of PrimeLending's origination volume was concentrated in nine states (none of the other states in which PrimeLending operated during 2013 had volume of 3% or more). The following table is a summary of the origination volume by state for the year ended December 31, 2013 (dollars in thousands).

	Volume	% of Total
Texas	$ 2,660,810	22.56%
California	2,082,184	17.66%
North Carolina	618,802	5.25%
Virginia	466,531	3.96%
Florida	456,643	3.87%
Arizona	392,006	3.32%
Maryland	385,215	3.27%
Ohio	383,518	3.25%
Washington	360,100	3.05%
All other states	3,986,753	33.81%
	$ 11,792,562	100.00%

Our insurance products are distributed through a broad network of independent agents and a select number of managing general agents, referred to as MGAs, which are concentrated in five states (none of the other states in which we operated during 2013 had gross written premiums of 3% or more). The following table sets forth our total gross written premiums by state for the periods shown (dollars in thousands).

	Year Ended December 31,					
	2013	% of Total	2012	% of Total	2011	% of Total
Texas	$ 125,696	69.1%	$ 118,361	69.5%	$ 117,046	73.0%
Oklahoma	16,494	9.1%	15,398	9.1%	10,804	6.7%
Arizona	15,904	8.7%	13,914	8.2%	12,376	7.7%
Tennessee	10,589	5.8%	10,527	6.2%	9,489	5.9%
Georgia	6,393	3.5%	5,454	3.2%	4,380	2.7%
All other states	6,892	3.8%	6,547	3.8%	6,346	4.0%
Total	$ 181,968	100.0%	$ 170,201	100.0%	$ 160,441	100.0%

FSC, a diversified investment banking firm and a registered broker-dealer, competes for business nationwide. Public finance financial advisory revenues, of which 76% are from entities located in Texas, represent a significant portion of total segment revenues.

Business Segments

Under U.S. generally accepted accounting principles ("GAAP"), our two business units are comprised of four reportable business segments organized primarily by the core products offered to the segments' respective customers: banking, mortgage origination, insurance and financial advisory. These segments reflect the manner in which operations are managed and the criteria used by our chief operating decision maker function to evaluate segment performance, develop strategy and allocate resources. Our chief operating decision maker function consists of the President and Chief Executive Officer of Hilltop and the Chief Executive Officer of PlainsCapital.

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For more financial information about each of our business segments, see " Management's Discussion and Analysis of Financial Condition and Results of Operations," herein. See also Note 30 in the notes to our audited consolidated financial statements included herein.

Banking

The banking segment includes the operations of the Bank and, since September 14, 2013, the operations acquired in the FNB Transaction. At June 30, 2014, our banking segment had $8.2 billion in assets and total deposits of $6.0 billion. The primary sources of our deposits are residents and businesses located in Texas.

Business Banking. Our business banking customers primarily consist of agribusiness, energy, health care, institutions of higher education, real estate (including construction and land development) and wholesale/retail trade companies. We provide these customers with extensive banking services, such as Internet banking, business check cards and other add-on services as determined on a customer-by-customer basis. Our treasury management services, which are designed to reduce the time, burden and expense of collecting, transferring, disbursing and reporting cash, are also available to our business customers. We offer these business customers lines of credit, equipment loans and leases, letters of credit, agricultural loans, commercial real estate loans and other loan products.

The table below sets forth a distribution of the banking segment's non-covered and covered loans, classified by portfolio segment and segregated between those considered to be purchased credit impaired ("PCI") loans and all other originated or acquired loans at December 31, 2013 (dollars in thousands). PCI loans showed evidence of credit deterioration that makes it probable that all contractually required principal and interest payments will not be collected. The banking segment's loan portfolio includes "covered loans" acquired in the FNB Transaction that are subject to loss-share agreements with the FDIC, while all other loans held by the Bank are referred to as "non-covered loans." The commercial and industrial non-covered loans category includes a $1.3 billion warehouse line of credit extended to PrimeLending, of which $1.0 billion was drawn at December 31, 2013, as well as term loans at First Southwest that had an outstanding balance of $23.0 million at December 31, 2013. Amounts advanced against the warehouse line and the First Southwest term loans are included in the table below, but are eliminated from the consolidated balance sheets.

Non-covered loans	**Loans, excluding PCI Loans**	**PCI Loans**	**Total Loans**	**% of Total Non-Covered Loans**
Commercial and industrial:				
Secured	$ 2,229,778	$ 35,372	$ 2,265,150	53.3%
Unsecured	106,855	1,444	108,299	2.6%
Real estate:				
Secured by commercial properties	1,045,964	36,255	1,082,219	25.5%
Secured by residential properties	373,242	2,995	376,237	8.9%
Construction and land development:				
Residential construction loans	65,079		65,079	1.5%
Commercial construction loans and land development	279,655	19,817	299,472	7.0%
Consumer	51,067	4,509	55,576	1.3%
Total non-covered loans	$ 4,151,640	$ 100,392	$ 4,252,032	100.0%

Covered loans	Loans, excluding PCI Loans	PCI Loans	Total Loans	% of Total Covered Loans
Commercial and industrial:				
Secured	$ 24,913	$ 28,520	$ 53,433	5.3%
Unsecured	3,620	9,890	13,510	1.4%
Real estate:				
Secured by commercial properties	64,819	365,306	430,125	42.7%
Secured by residential properties	158,485	199,372	357,857	35.6%
Construction and land development:				
Residential construction loans	7,463	4,705	12,168	1.2%
Commercial construction loans and land development	17,913	121,363	139,276	13.8%
Total covered loans	$ 277,213	$ 729,156	$ 1,006,369	100.0%

Our lending policies seek to achieve the goal of establishing an asset portfolio that will provide a return on stockholders' equity sufficient to maintain capital to assets ratios that meet or exceed established regulations. In support of that goal, we have designed our underwriting standards to determine:

That our borrowers possess sound ethics and competently manage their affairs;

That we know the source of the funds the borrower will use to repay the loan;

That the purpose of the loan makes economic sense; and

That we identify relevant risks of the loan and determine that the risks are acceptable.

We implement our underwriting standards according to the facts and circumstances of each particular loan request, as discussed below.

Commercial and industrial loans are primarily made within Texas and are underwritten on the basis of the borrower's ability to service the debt from cash flow from an operating business. In general, commercial and industrial loans involve more credit risk than residential and commercial mortgage loans and, therefore, usually yield a higher return. The increased risk in commercial and industrial loans results primarily from the type of collateral securing these loans, which typically includes commercial real estate, accounts receivable, equipment and inventory. Additionally, increased risk arises from the expectation that commercial and industrial loans generally will be serviced principally from operating cash flow of the business, and such cash flows are dependent upon successful business operations. Historical trends have shown these types of loans to have higher delinquencies than mortgage loans. As a result of the additional risk and complexity associated with commercial and industrial loans, such loans require more thorough underwriting and servicing than loans to individuals. To manage these risks, our policy is to attempt to secure commercial and industrial loans with both the assets of the borrowing business and other additional collateral and guarantees that may be available. In addition, depending on the size of the credit, we actively monitor the financial condition of the borrower by analyzing the borrower's financial statements and assessing certain financial measures, including cash flow, collateral value and other appropriate credit factors. We also have processes in place to analyze and evaluate on a regular basis our exposure to industries, products, market changes and economic trends.

The Bank also offers term financing on commercial real estate properties that include retail, office, multi-family, industrial, warehouse and non-owner occupied single family residences. Commercial mortgage lending can involve high principal loan amounts, and the repayment of these loans is dependent, in large part, on a borrower's on-going business operations or on income generated from

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the properties that are leased to third parties. Accordingly, we apply the measures described above for commercial and industrial loans to our commercial real estate lending, with increased emphasis on analysis of collateral values. As a general practice, the Bank requires its commercial mortgage loans to (i) be secured with first lien positions on the underlying property, (ii) generate adequate equity margins, (iii) be serviced by businesses operated by an established management team and (iv) be guaranteed by the principals of the borrower. The Bank seeks lending opportunities where cash flow from the collateral provides adequate debt service coverage and/or the guarantor's net worth is comprised of assets other than the project being financed.

The Bank offers construction financing for (i) commercial, retail, office, industrial, warehouse and multi-family developments, (ii) residential developments and (iii) single family residential properties. Construction loans involve additional risks because loan funds are advanced upon the security of a project under construction, and the project is of uncertain value prior to its completion. If the Bank is forced to foreclose on a project prior to completion, it may not be able to recover the entire unpaid portion of the loan. Additionally, it may be required to fund additional amounts to complete a project and may have to hold the property for an indeterminate period of time. Because of uncertainties inherent in estimating construction costs, the market value of the completed project and the effects of governmental regulation on real property, it can be difficult to accurately evaluate the total funds required to complete a project and the related loan-to-value ratio. As a result of these uncertainties, construction lending often involves the disbursement of substantial funds with repayment dependent, in part, on the success of the ultimate project rather than the ability of a borrower or guarantor to repay the loan. We generally require that the subject property of a construction loan for commercial real estate be pre-leased, since cash flows from the completed project provide the most reliable source of repayment for the loan. Loans to finance these transactions are generally secured by first liens on the underlying real property. The Bank conducts periodic completion inspections, either directly or through an agent, prior to approval of periodic draws on these loans.

In addition to the real estate lending activities described above, a portion of the Bank's real estate portfolio consists of single family residential mortgage loans typically collateralized by owner occupied properties located in its market areas. These residential mortgage loans are generally secured by a first lien on the underlying property and have maturities up to thirty years. At December 31, 2013, the Bank had $582.6 million in one-to-four family residential loans, which represented 12.9% of its total loans held for investment.

Personal Banking. We offer a broad range of personal banking products and services for individuals. Similar to our business banking operations, we also provide our personal banking customers with a variety of add-on features such as check cards, safe deposit boxes, Internet banking, bill pay, overdraft privilege services, gift cards and access to automated teller machine (ATM) facilities throughout the United States. We offer a variety of deposit accounts to our personal banking customers including savings, checking, interest-bearing checking, money market and certificates of deposit.

We loan to individuals for personal, family and household purposes, including lines of credit, home improvement loans, home equity loans, credit cards and loans for purchasing and carrying securities. At December 31, 2013, we had $55.6 million of loans for these purposes, which are shown in the non-covered loans table above as "Consumer."

Wealth and Investment Management. Our private banking team personally assists high net worth individuals and their families with their banking needs, including depository, credit, asset management, and trust and estate services. We offer trust and asset management services in order to assist these customers in managing, and ultimately transferring, their wealth. Our wealth management services provide personal trust, investment management and employee benefit plan administration services, including estate planning, management and administration, investment portfolio management, employee benefit accounts and individual retirement accounts.

Mortgage Origination

Our mortgage origination segment operates through a wholly owned subsidiary of the Bank, PrimeLending. Founded in 1986, PrimeLending is a residential mortgage banker licensed to originate and close loans in all 50 states and the District of Columbia. At June 30, 2014, it operated from over 300 locations in 42 states. During 2013, PrimeLending originated approximately 23% of its mortgages from its Texas locations and approximately 18% of its mortgages from locations in California. The mortgage lending business is subject to seasonality, as we typically experience increased loan origination volume from purchases of homes during the spring and summer, when more people tend to move and buy or sell homes, and the overall demand for mortgage loans is driven largely by the applicable interest rates at any given time.

PrimeLending handles loan processing, underwriting and closings in-house. Mortgage loans originated by PrimeLending are funded through a warehouse line of credit maintained with the Bank. PrimeLending sells substantially all mortgage loans it originates to various investors in the secondary market, the majority with servicing released. While PrimeLending's loan origination volume has decreased since the second quarter of 2013, PrimeLending increased the amount of loans on which it retained servicing. As mortgage loans are sold in the secondary market, PrimeLending pays down its warehouse line of credit with the Bank. Loans sold are subject to certain standard indemnification provisions with investors, including the repurchase of loans sold and the repayment of sales proceeds to investors under certain conditions.

Our mortgage lending underwriting strategy, driven in large measure by secondary market investor standards, seeks primarily to originate conforming loans. Our underwriting practices include:

- granting loans on a sound and collectible basis;
- obtaining a balance between maximum yield and minimum risk;
- ensuring that primary and secondary sources of repayment are adequate in relation to the amount of the loan; and
- ensuring that each loan is properly documented and, if appropriate, adequately insured.

Since its inception, PrimeLending has grown from a staff of 20 individuals producing approximately $80 million in annual closed mortgage loan volume to a staff of approximately 2,600 producing $11.8 billion in 2013. PrimeLending offers a variety of loan products catering to the specific needs of borrowers seeking purchase or refinancing options, including 30-year and 15-year fixed rate conventional mortgages, adjustable rate mortgages, jumbo loans, and Federal Housing Administration ("FHA") and Veteran Affairs ("VA") loans. Mortgage loans originated by PrimeLending are secured by a first lien on the underlying property. PrimeLending does not currently originate subprime loans (which we define to be loans to borrowers having a Fair Isaac Corporation (FICO) score lower than 620 on conventional mortgages and VA loans or 600 on FHA loans or loans that do not comply with applicable agency or investor-specific underwriting guidelines).

Insurance

The operations of NLC comprise our insurance segment. NLC specializes in providing fire and limited homeowners insurance for low value dwellings and manufactured homes primarily in Texas and other areas of the south, southeastern and southwestern United States. NLC's product lines also include enhanced homeowners products offering higher coverage limits with distribution restricted to select agents. NLC targets underserved markets through a broad network of independent agents currently operating in 14 states and a select number of MGAs, which require underwriting expertise that many larger carriers have been unwilling to develop given the relatively small volume of premiums produced by local agents.

Ratings. Many insurance buyers, agents and brokers use the ratings assigned by A.M. Best and other rating agencies to assist them in assessing the financial strength and overall quality of the companies from which they purchase insurance. The ratings for NLIC and ASIC of "A" (Excellent) were affirmed by A.M. Best in April 2014. An "A" rating is the third highest of 16 rating categories used by A.M. Best. In evaluating a company's financial and operating performance, A.M. Best reviews a company's profitability, leverage and liquidity, as well as its book of business, the adequacy and soundness of its reinsurance, the quality and estimated market value of its assets, the adequacy of its liabilities for losses and loss adjustment expenses ("LAE"), the adequacy of its surplus, its capital structure, the experience and competence of its management and its market presence. This rating assignment is subject to the ability to meet A.M. Best's expectations as to performance and capitalization on an ongoing basis, and is subject to revocation or revision at any time at the sole discretion of A.M. Best. NLC cannot ensure that NLIC and ASIC will maintain their present ratings.

Product Lines. NLC's business is conducted in two product lines: personal lines and commercial lines. The personal lines include homeowners, dwelling fire, manufactured home, flood and vacant policies. The commercial lines include commercial multi-peril, builders risk, builders risk renovation, sports liability and inland marine policies.

The NLC companies specialize in writing fire and homeowners insurance coverage for low value dwellings and manufactured homes. The vast majority of NLC's property coverage is written on policies that provide actual cash value payments, as opposed to replacement cost. Under actual cash value policies, the insured is entitled to receive only the cost of replacing or repairing damaged or destroyed property with comparable new property, less depreciation. Replacement cost does not include such a deduction for depreciation. In 2010, NLC expanded its homeowners insurance products to include replacement cost coverage, which also includes limited water coverage. These new products have been marketed and sold primarily in Texas. The development and implementation of these new products contributed to the premium growth at NLC since 2011. Rate increases and exposure management are expected to moderate future policy growth.

Underwriting and Pricing. NLC applies its regional expertise, underwriting discipline and a risk-adjusted, return-on-equity-based approach to capital allocation to primarily offer short-tail insurance products in its target markets. NLC's underwriting process involves securing an adequate level of underwriting information from its independent agents, identifying and evaluating risk exposures and then pricing the risks it chooses to accept. Management reviews pricing on an ongoing basis to monitor any emerging issues on a specific coverage or geographic territory.

Catastrophe Exposure. NLC maintains a comprehensive risk management strategy, which includes actively monitoring its catastrophe prone territories by zip code to ensure a diversified book of risks. NLC utilizes software and risk support from its reinsurance brokers to analyze its portfolio and catastrophe exposure. Biannually, NLC has its entire portfolio analyzed by its reinsurance broker who utilizes hurricane and severe storm models to predict risk.

Reinsurance. NLC purchases reinsurance to reduce its exposure to liability on individual risks and claims and to protect against catastrophe losses. NLC's management believes that less volatile, yet reasonable returns are in the long-term interest of NLC.

Reinsurance involves an insurance company transferring, or ceding, a portion of its risk to another insurer, the reinsurer. The reinsurer assumes the exposure in return for a portion of the premium. The ceding of risk to a reinsurer does not legally discharge the primary insurer from its liability for the full amount of the policies on which it obtains reinsurance. Accordingly, the primary insurer remains liable for the entire loss if the reinsurer fails to meet its obligations under the reinsurance agreement, and as a result, the primary insurer is exposed to the risk of non-payment by its reinsurers. In formulating its reinsurance programs, NLC believes that it is selective in its choice of reinsurers and considers numerous factors, the most important of which are the financial stability of the reinsurer, its history of responding to claims and its overall reputation.

NLC purchases catastrophe excess of loss reinsurance to a limit that exceeds the Hurricane 200-year return time as modeled by RMS Risk Link v.13.0 and equals the Hurricane 500-year return time as modeled by AIR Classic v.15.0.

Liabilities for Unpaid Losses and Loss Adjustment Expenses. NLC's liabilities for losses and loss adjustment expenses include liabilities for reported losses, liabilities for incurred but not reported, or IBNR, losses and liabilities for LAE, less a reduction for reinsurance recoverables related to those liabilities. The amount of liabilities for reported claims is based primarily on a claim-by-claim evaluation of coverage, liability, injury severity or scope of property damage, and any other information considered relevant to estimating exposure presented by the claim. The amounts of liabilities for IBNR losses and LAE are estimated on the basis of historical trends, adjusted for changes in loss costs, underwriting standards, policy provisions, product mix and other factors. Estimating the liability for unpaid losses and LAE is inherently judgmental and is influenced by factors that are subject to significant variation. Liabilities for LAE are intended to cover the ultimate cost of settling claims, including investigation and defense of lawsuits resulting from such claims. Based upon the contractual terms of the reinsurance agreements, reinsurance recoverables offset, in part, NLC's gross liabilities.

Significant periods of time can elapse between the occurrence of an insured loss, the reporting of the loss to the insurer and the insurer's payment of that loss. NLC's liabilities for unpaid losses represent the best estimate at a given point in time of what it expects to pay claimants, based on facts, circumstances and historical trends then known. During the loss settlement period, additional facts regarding individual claims may become known and, consequently, it often becomes necessary to refine and adjust the estimates of liability.

Loss Development. The following tables set forth the annual calendar year-end reserves of NLIC and ASIC since 2004 and the subsequent development of these reserves through December 31, 2013. These tables present accident year development data. The first line of each table shows, for the years indicated, net liability, including IBNR, as originally estimated. The next section sets forth the re-estimates in later years of incurred losses, including payments, for the years indicated. The changes in the original estimate are caused by a combination of factors, including: (1) claims being settled for amounts different than originally estimated; (2) the net liability being increased or decreased for claims remaining open as more information becomes known about those individual claims; and (3) more or fewer claims being reported after December 31, 2004 than had occurred prior to that date. The bottom section of the table shows, by year, the cumulative amounts of net losses and LAE paid as of the end of each succeeding year.

The "net cumulative redundancy (deficiency)" represents, as of December 31, 2013, the difference between the latest re-estimated net liability and the net liability as originally estimated for losses and LAE retained by us. A redundancy means the original estimate was higher than the current estimate; and a deficiency means that the original estimate was lower than the current estimate. The following loss development tables for NLIC and ASIC are presented net of reinsurance recoverable (in thousands).

National Lloyds Insurance Company

	Year Ended December 31,									
	2004	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**
Original Reserve*	$ 33,951	$ 41,282	$ 47,684	$ 44,613	$ 65,592	$ 60,392	$ 55,482	$ 81,589	$ 87,943	$ 86,524
1 year later	28,106	36,332	43,640	44,064	64,864	62,337	54,987	82,065	88,708	
2 years later	27,593	40,391	43,465	44,134	65,070	62,014	54,672	81,782		
3 years later	25,747	41,231	43,394	43,950	64,702	61,759	54,554			
4 years later	25,712	39,735	43,387	43,788	64,569	61,328				
5 years later	25,579	39,699	43,366	43,649	64,547					
6 years later	25,582	39,675	43,365	43,679						
7 years later	25,568	39,674	43,363							
8 years later	25,565	39,677								
9 years later	25,565									
Net cumulative redundancy (deficiency)	8,386	1,605	4,321	934	1,045	(936)	928	(193)	(765)	
Cumulative amount of net liability paid as of:										
1 year later	24,747	32,871	42,301	42,478	63,761	59,977	53,387	79,853	82,762	
2 years later	25,149	34,625	42,668	43,245	64,203	60,517	53,872	80,591		
3 years later	25,388	36,157	43,140	43,495	64,391	61,081	54,161			
4 years later	25,462	39,533	43,361	43,563	64,477	61,233				
5 years later	25,521	39,646	43,365	43,648	64,538					
6 years later	25,538	37,674	43,365	43,650						
7 years later	25,564	39,674	43,363							
8 years later	25,565	39,677								
9 years later	25,565									

American Summit Insurance Company

	Year Ended December 31,									
	2004	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**
Original Reserve*	$ 8,297	$ 11,041	$ 13,003	$ 9,351	$ 12,769	$ 9,773	$ 12,486	$ 14,829	$ 13,547	$ 15,152
1 year later	7,388	9,932	13,014	9,154	12,009	9,423	13,153	14,126	13,235	
2 years later	6,999	9,918	12,998	9,335	11,943	9,088	12,974	14,044		
3 years later	6,859	9,918	13,435	9,235	11,880	9,023	12,873			
4 years later	6,772	9,797	13,216	9,200	12,048	8,701				
5 years later	6,714	9,820	13,195	9,197	12,342					
6 years later	6,787	9,815	13,188	9,196						
7 years later	6,743	9,812	13,187							
8 years later	6,730	9,913								
9 years later	6,730									
Net cumulative redundancy (deficiency)	1,567	1,128	(184)	155	427	1,072	(387)	785	312	
Cumulative amount of net liability paid as of:										
1 year later	6,566	9,341	12,429	8,732	11,560	8,800	12,390	13,511	12,423	
2 years later	6,610	9,578	12,639	9,095	11,637	8,803	12,632	13,842		
3 years later	6,682	9,679	13,326	9,193	11,726	8,917	12,792			
4 years later	6,699	9,740	13,161	9,196	12,040	8,672				
5 years later	6,714	9,813	13,188	9,196	12,341					
6 years later	6,720	9,813	13,188	9,196						

7 years later	6,723	9,812	13,187
8 years later	6,730	9,813	
9 years later	6,730		

* Including amounts paid in respective year.

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Please refer to Note 28 in the notes to Hilltop's audited consolidated financial statements included in this proxy statement/prospectus for a reconciliation of the reserves presented in the tables above to the reserves for losses and loss adjustment expenses set forth in the consolidated balance sheets at December 31, 2013 and 2012.

Current loss reserve development has been generally favorable with the exception of accident year 2012. Accident years 2007 through 2011 have shown cumulative favorable loss development of $3.8 million through December 31, 2013. Accident year 2012 had net unfavorable loss development of $0.5 million, with unfavorable development of $0.8 million at NLIC, offset by favorable loss development of $0.3 million at ASIC. The unfavorable loss development at NLIC is significantly attributable to extraordinary increases in losses from wind and hail losses and storms that occurred in Texas during 2012.

The following table is a reconciliation of the gross liability to net liability for losses and loss adjustment expenses (in thousands).

	December 31,*						
	2007	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**
Gross unpaid losses	$ 18,091	$ 34,023	$ 33,780	$ 58,882	$ 44,835	$ 34,012	$ 27,468
Reinsurance recoverable	(2,692)	(14,613)	(21,102)	(43,773)	(25,083)	(10,385)	(4,508)
Net unpaid losses	$ 15,399	$ 19,410	$ 12,678	$ 15,109	$ 19,752	$ 23,627	$ 22,960

* Information is not presented for the periods ended prior to January 31, 2007, as that is the date Hilltop Holdings Inc. acquired the insurance operations.

The methods that our actuaries utilize to estimate ultimate loss and LAE amounts are the paid and reported loss development method and the paid and reported Bornhuetter-Ferguson method (the "BF method"). Insured losses for a given accident year change in value over time as additional information on claims is received, as claim conditions change and as new claims are reported. This process is commonly referred to as loss development. To project ultimate losses and LAE, our actuaries examine the paid and reported losses and LAE for each accident year and multiply these values by a loss development factor. The selected loss development factors are based upon a review of the loss development patterns indicated in the companies' historical loss triangles and applicable insurance industry loss development factors.

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

The results of each actuarial method performed by year are reviewed to select an ultimate loss and LAE amount for each accident year. In general, more weight is given to the loss development projections for more mature accident periods and more weight is given to the BF methods for less mature accident periods.

The combination of the methodologies described above is used for all insurance lines of business, regardless of whether the line is a short-tailed or long-tailed line of business, though specific parameter selections within the methods vary to reflect the nature of the underlying line of business. ASIC and NLIC specialize in writing fire and extended coverage for low-value dwellings, mobile homes and homeowners, which generally are considered short-tailed coverages. In addition, ASIC and NLIC write a small amount of commercial risks, which are still predominantly property coverages, along with some low-limit liability coverages.

The reserve analysis performed by our actuaries provides preliminary central estimates of the unpaid losses and LAE. At each quarter-end, the results of the reserve analysis are summarized and discussed with our senior management. The senior management group considers many factors in determining the amount of reserves to record for financial statement purposes. These factors include the extent and timing of any recent catastrophic events, historical pattern and volatility of the actuarial indications, the sensitivity of the actuarial indications to changes in paid and reported loss patterns, the consistency of claims handling processes, the consistency of case reserving practices, changes in our pricing and underwriting, and overall pricing and underwriting trends in the insurance market.

In arriving at our best estimate of the unpaid losses and LAE, and based on management discussion with our actuaries, we would consider reasonably likely changes in the key assumptions, such as the underlying loss development pattern or the expected loss ratio, to have an impact on our best estimate by plus or minus 10%. At December 31, 2013, this equates to approximately plus or minus $2.3 million, or 1.8% of insurance segment equity, and 2.1% of calendar year 2013 insurance losses.

Financial Advisory

Our financial advisory segment operates through First Southwest. FSC, a wholly owned subsidiary of First Southwest, is a diversified investment banking firm and a registered broker-dealer with the SEC and the Financial Industry Regulatory Authority ("FINRA") and a member of the New York Stock Exchange. First Southwest's primary focus is on providing public finance services.

At June 30, 2014, First Southwest employed approximately 400 people and maintained 25 locations nationwide, nine of which are in Texas. At June 30, 2014, First Southwest had consolidated assets of $712.7 million, maintained $120.4 million in equity capital and had more than 1,600 public sector clients.

First Southwest has four primary lines of business: (i) public finance, (ii) capital markets, (iii) correspondent clearing services, and (iv) asset management.

Public Finance. First Southwest's public finance group represents its largest department. This group advises cities, counties, school districts, utility districts, tax increment zones, special districts, state agencies and other governmental entities nationwide. In addition, the group provides specialized advisory and investment banking services for airports, convention centers, healthcare institutions, institutions of higher education, housing, industrial development agencies, toll road authorities, and public power and utility providers.

Capital Markets. Through its capital markets group, First Southwest trades fixed income securities to support sales and other customer activities, underwrites tax-exempt and taxable fixed income securities and trades equities on an agency basis on behalf of its retail and institutional clients. In addition, First Southwest provides asset and liability management advisory services to community banks.

Correspondent Clearing Services. The correspondent clearing services group offers omnibus and fully disclosed clearing services to FINRA member firms for trade executing, clearing and back office services. Services are provided to approximately 80 correspondent firms.

Asset Management. First Southwest Asset Management is an investment advisor registered under the Investment Advisers Act of 1940 providing state and local governments with advice and assistance with respect to arbitrage rebate compliance, portfolio management and local government investment pool administration. In the area of arbitrage rebate, First Southwest Asset Management advises municipalities with respect to the emerging regulations relating to arbitrage rebates. Further, First Southwest Asset Management assists governmental entities with the complexities of investing public funds in the fixed income markets. As an investment adviser registered with the SEC, First Southwest Asset Management promotes cash management-based investment strategies that seek to adhere to the standards imposed by the fiduciary responsibilities of investment officers of public funds. At June 30, 2014, First Southwest Asset Management served as investment manager of $6.8 billion in short-term fixed income portfolios of municipal governments and investment adviser for $5.1 billion invested by municipal governments, and a group within FSC served as administrator for local government investment pools totaling $7.8 billion.

Competition

We face significant competition with respect to the business segments in which we operate and the geographic markets we serve. Many of our competitors have substantially greater financial resources, lending limits and larger branch networks than we do, and offer a broader range of products and services.

Our lending and mortgage origination competitors include commercial banks, savings banks, savings and loan associations, credit unions, finance companies, pension trusts, mutual funds, insurance companies, mortgage bankers and brokers, brokerage and investment banking firms, asset-based non-bank lenders, government agencies and certain other non-financial institutions. Competition for deposits and in providing lending and mortgage origination products and services to businesses in our market area is intense and pricing is important. Other factors encountered in competing for savings deposits are convenient office locations, interest rates and fee structures of products offered. Direct competition for savings deposits also comes from other commercial bank and thrift institutions, money market mutual funds and corporate and government securities that may offer more attractive rates than insured depository institutions are willing to pay. Competition for loans includes such additional factors as interest rates, loan origination fees and the range of services offered by the provider. We seek to distinguish ourselves from our competitors through our commitment to personalized customer service and responsiveness to customer needs while providing a range of competitive loan and deposit products and other services.

Our insurance business competes with a large number of other companies in its selected lines of business, including major U.S. and non-U.S. insurers, regional companies, mutual companies, specialty insurance companies, underwriting agencies and diversified financial services companies. The personal lines market in Texas is dominated by a few large carriers and their subsidiaries and affiliates. We seek to distinguish ourselves from our competitors by targeting underserved market segments that provide us with the best opportunity to obtain favorable policy terms, conditions and pricing.

We also face significant competition for financial advisory services on a number of factors, including price, perceived expertise, quality of advice, range of services, innovation and local presence. Our financial advisory business competes directly with numerous other financial advisory and investment banking firms, broker-dealers and banks, including large national and major regional firms and smaller niche companies, some of whom are not broker-dealers and, therefore, are not subject to the broker-dealer regulatory framework.

Employees

At June 30, 2014, we employed approximately 4,400 people, substantially all of which are full-time. None of our employees are represented by any collective bargaining unit or a party to any collective bargaining agreement.

Government Supervision and Regulation

General

We are subject to extensive regulation under federal and state laws. The regulatory framework is intended primarily for the protection of customers and clients of our financial advisory services, depositors, borrowers, the insurance funds of the FDIC and the Securities Investment Protection Corporation (the "SIPC") and the banking system as a whole, and not for the protection of our stockholders or creditors. In many cases, the applicable regulatory authorities have broad enforcement power over bank holding companies, banks and their subsidiaries, including the power to impose substantial fines and other penalties for violations of laws and regulations. The following discussion describes the material elements of the regulatory framework that applies to us and our subsidiaries. References in this discussion to applicable statutes and regulations are brief summaries thereof, do not purport to be complete, and are qualified in their entirety by reference to such statutes and regulations.

Recent Regulatory Developments. New regulations and statutes are regularly proposed and/or adopted that contain wide-ranging proposals for altering the structures, regulations and competitive relationships of financial institutions operating and doing business in the United States. Certain of these recent proposals and changes are described below.

On July 21, 2010, President Obama signed into law the Dodd-Frank Act. The Dodd-Frank Act aims to restore responsibility and accountability to the financial system by significantly altering the regulation of financial institutions and the financial services industry. Most of the provisions contained in the Dodd-Frank Act have delayed effective dates. Full implementation of the Dodd-Frank Act will require many new rules to be issued by federal regulatory agencies over the next several years, which will profoundly affect how financial institutions will be regulated in the future. The ultimate effect of the Dodd-Frank Act and its implementing regulations on the financial services industry in general, and on us in particular, is uncertain at this time.

The Dodd-Frank Act, among other things:

- Established the Consumer Financial Protection Bureau (the "CFPB"), an independent organization within the Federal Reserve which has the authority to promulgate consumer protection regulations applicable to all entities offering consumer financial products or services, including banks and mortgage originators. The CFPB has broad rule-making authority for a wide range of consumer protection laws, including the authority to prohibit "unfair, deceptive or abusive" acts and practices. The CFPB has exclusive examination authority and primary enforcement authority with respect to financial institutions with total assets of more than $10.0 billion and their affiliates for purposes of federal consumer protection laws. After June 30, 2011, a financial institution becomes subject to the CFPB's exclusive examination authority and primary enforcement authority after it has reported total assets of greater than $10.0 billion in its quarterly call reports for four consecutive quarters.

- Established the Financial Stability Oversight Council, tasked with the authority to identify and monitor institutions and systems which pose a systemic risk to the financial system, and to impose standards regarding capital, leverage, liquidity, risk management, and other requirements for financial firms.

- Changed the base for FDIC insurance assessments.

- Increased the minimum reserve ratio for the Deposit Insurance Fund from 1.15% to 1.35% (the FDIC subsequently increased it by regulation to 2.00%).
- Permanently increased the deposit insurance coverage amount from $100,000 to $250,000.
- Directed the Federal Reserve to establish interchange fees for debit cards pursuant to a restrictive "reasonable and proportional cost" per transaction standard.
- Limits the ability of banking organizations to sponsor or invest in private equity and hedge funds and to engage in proprietary trading in a provision known as the "Volcker Rule".
- Grants the U.S. government authority to liquidate or take emergency measures with respect to troubled nonbank financial companies that fall outside the existing resolution authority of the FDIC, including the establishment of an orderly liquidation fund.
- Increases regulation of asset-backed securities, including a requirement that issuers of asset-backed securities retain at least 5% of the risk of the asset-backed securities.
- Increases regulation of consumer protections regarding mortgage originations, including banker compensation, minimum repayment standards, and prepayment consideration.
- Establishes new disclosure and other requirements relating to executive compensation and corporate governance.

On June 21, 2010, the Federal Reserve Board, the Office of the Comptroller of the Currency, the Office of Thrift Supervision and the FDIC jointly issued comprehensive final guidance on incentive compensation policies (the "Incentive Compensation Guidance") intended to ensure that the incentive compensation policies of banking organizations do not undermine the safety and soundness of such organizations by encouraging excessive risk-taking. The Incentive Compensation Guidance sets expectations for banking organizations concerning their incentive compensation arrangements and related risk-management, control and governance processes. The Incentive Compensation Guidance, which covers all employees that have the ability to materially affect the risk profile of an organization, either individually or as part of a group, is based upon three primary principles: (i) balanced risk-taking incentives, (ii) compatibility with effective controls and risk management, and (iii) strong corporate governance. Any deficiencies in compensation practices that are identified may be incorporated into the organization's supervisory ratings, which can affect its ability to make acquisitions or perform other actions. In addition, under the Incentive Compensation Guidance, a banking organization's federal supervisor may initiate enforcement action if the organization's incentive compensation arrangements pose a risk to the safety and soundness of the organization.

On April 14, 2011, the Federal Reserve Board and various other federal agencies published a notice of proposed rulemaking implementing provisions of the Dodd-Frank Act that would require reporting of incentive-based compensation arrangements by a covered financial institution and prohibit incentive-based compensation arrangements at a covered financial institution that provide excessive compensation or that could expose the institution to inappropriate risks that could lead to material financial loss. The Dodd-Frank Act defines "covered financial institution" to include, among other entities, a depository institution or depository institution holding company that has $1 billion or more in assets. There are enhanced requirements for institutions with more than $50 billion in assets. The proposed rule states that it is consistent with the Incentive Compensation Guidance.

On January 10, 2013, the CFPB issued a final rule to implement the "qualified mortgage", or "QM" provisions of the Dodd-Frank Act requiring mortgage lenders to consider consumers' ability to repay home loans before extending them credit. The final rule describes certain minimum requirements for creditors making ability-to-repay determinations, but does not dictate that they follow particular underwriting models. Lenders will be presumed to have complied with the ability-to-repay rule if they issue "qualified mortgages", which are generally defined as mortgage loans prohibiting or limiting

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certain risky features. Loans that do not meet the ability-to-repay standard can be challenged in court by borrowers who default and the absence of ability-to-repay status can be used against a creditor in foreclosure proceedings. The CFPB's QM rule took effect on January 10, 2014.

In December 2013, U.S. regulators issued final regulations to implement the Volcker Rule. The Volcker Rule will, over time, prohibit "banking entities," including Hilltop and its subsidiaries, from engaging in certain prohibited "proprietary trading" activities, as defined in the Volcker Rule regulations, subject to specified exemptions. The Volcker Rule will also require banking entities to either restructure or unwind certain investments and relationships with "covered funds," as defined in the Volcker Rule regulations. Banking entities have until July 21, 2015 to bring all of their activities and investments into conformance with the Volcker Rule, subject to possible extensions. The Volcker Rule requires banking entities to establish comprehensive compliance programs designed to help ensure and monitor compliance with restrictions under the Volcker Rule. We are continuing to evaluate the effects of the final regulations implementing the Volcker Rule, but we do not currently anticipate that the Volcker Rule will have a material effect on our operations.

We cannot predict whether or in what form any proposed regulation or statute will be adopted or the extent to which our business may be affected by any new regulation or statute.

Hilltop

Hilltop is a legal entity separate and distinct from PlainsCapital and its other subsidiaries. On November 30, 2012, concurrent with the consummation of the PlainsCapital Merger, Hilltop became a financial holding company registered under the Bank Holding Company Act, as amended by the Gramm-Leach-Bliley Act. Accordingly, it is subject to supervision, regulation and examination by the Federal Reserve Board. The Dodd-Frank Act, Gramm-Leach-Bliley Act, the Bank Holding Company Act and other federal laws subject financial and bank holding companies to particular restrictions on the types of activities in which they may engage and to a range of supervisory requirements and activities, including regulatory enforcement actions for violations of laws and regulations.

Changes of Control. Federal and state laws impose additional notice, approval and ongoing regulatory requirements on any investor that seeks to acquire direct or indirect "control" of a regulated holding company, such as Hilltop. These laws include the Bank Holding Company Act, the Change in Bank Control Act and the Texas Insurance Code. Among other things, these laws require regulatory filings by an investor that seeks to acquire direct or indirect "control" of a regulated holding company. The determination whether an investor "controls" a regulated holding company is based on all of the facts and circumstances surrounding the investment. As a general matter, an investor is deemed to control a depository institution or other company if the investor owns or controls 25% or more of any class of voting stock. Subject to rebuttal, an investor may be presumed to control the regulated holding company if the investor owns or controls 10% or more of any class of voting stock. Accordingly, these laws would apply to a person acquiring 10% or more of Hilltop's common stock. Furthermore, these laws may discourage potential acquisition proposals and may delay, deter or prevent change of control transactions, including those that some or all of our stockholders might consider to be desirable.

Regulatory Restrictions on Dividends; Source of Strength. It is the policy of the Federal Reserve Board that bank holding companies should pay cash dividends on common stock only out of income available over the past year and only if prospective earnings retention is consistent with the organization's expected future needs and financial condition. The policy provides that bank holding companies should not maintain a level of cash dividends that undermines the bank holding company's ability to serve as a source of strength to its banking subsidiaries. The Dodd-Frank Act requires the regulatory agencies to issue regulations requiring that all bank and savings and loan holding companies serve as a source of financial and managerial strength to their subsidiary depository institutions by providing capital, liquidity and other support in times of financial stress; however, no such proposals have yet been published.

Under Federal Reserve Board policy, a bank holding company is expected to act as a source of financial strength to each of its banking subsidiaries and commit resources to their support. Such support may be required at times when, absent this Federal Reserve Board policy, a holding company may not be inclined to provide it. As discussed herein, a bank holding company, in certain circumstances, could be required to guarantee the capital plan of an undercapitalized banking subsidiary.

Scope of Permissible Activities. Under the Bank Holding Company Act, Hilltop and PlainsCapital generally may not acquire a direct or indirect interest in, or control of more than 5% of, the voting shares of any company that is not a bank or bank holding company. Additionally, the Bank Holding Company Act prohibits Hilltop from engaging in activities other than those of banking, managing or controlling banks or furnishing services to, or performing services for, its subsidiaries, except that it may engage in, directly or indirectly, certain activities that the Federal Reserve Board has determined to be closely related to banking or managing and controlling banks as to be a proper incident thereto. In approving acquisitions or the addition of activities, the Federal Reserve Board considers, among other things, whether the acquisition or the additional activities can reasonably be expected to produce benefits to the public, such as greater convenience, increased competition, or gains in efficiency, that outweigh such possible adverse effects as undue concentration of resources, decreased or unfair competition, conflicts of interest or unsound banking practices.

Notwithstanding the foregoing, the Gramm-Leach-Bliley Act, effective March 11, 2000, eliminated the barriers to affiliations among banks, securities firms, insurance companies and other financial service providers and permits bank holding companies to become financial holding companies and thereby affiliate with securities firms and insurance companies and engage in other activities that are financial in nature. The Gramm-Leach-Bliley Act defines "financial in nature" to include: securities underwriting; dealing and market making; sponsoring mutual funds and investment companies; insurance underwriting and agency; merchant banking activities; and activities that the Federal Reserve Board has determined to be closely related to banking. Prior to enactment of the Dodd-Frank Act, regulatory approval was not required for a financial holding company to acquire a company, other than a bank or savings association, engaged in activities that were financial in nature or incidental to activities that were financial in nature, as determined by the Federal Reserve Board.

Under the Gramm-Leach-Bliley Act, a bank holding company may become a financial holding company by filing a declaration with the Federal Reserve Board if each of its subsidiary banks is "well capitalized" under the Federal Deposit Insurance Corporation Improvement Act prompt corrective action provisions, is "well managed", and has at least a "satisfactory" rating under the Community Reinvestment Act of 1977 (the "CRA"). The Dodd-Frank Act underscores the criteria for becoming a financial holding company by amending the Bank Holding Company Act to require that bank holding companies be "well capitalized" and "well managed" in order to become financial holding companies. Hilltop became a financial holding company on December 1, 2012.

Safe and Sound Banking Practices. Bank holding companies are not permitted to engage in unsafe and unsound banking practices. The Federal Reserve Board's Regulation Y, for example, generally requires a holding company to give the Federal Reserve Board prior notice of any redemption or repurchase of its equity securities, if the consideration to be paid, together with the consideration paid for any repurchases or redemptions in the preceding year, is equal to 10% or more of the company's consolidated net worth. In addition, bank holding companies are required to consult with the Federal Reserve Board prior to making any redemption or repurchase, even within the foregoing parameters. The Federal Reserve Board may oppose the transaction if it believes that the transaction would constitute an unsafe or unsound practice or would violate any law or regulation. Depending upon the circumstances, the Federal Reserve Board could take the position that paying a dividend would constitute an unsafe or unsound banking practice.

The Federal Reserve Board has broad authority to prohibit activities of bank holding companies and their nonbanking subsidiaries that represent unsafe and unsound banking practices or that constitute violations of laws or regulations, and can assess civil money penalties for certain activities conducted on a knowing and reckless basis, if those activities caused a substantial loss to a depository institution. The penalties can be as high as $1.425 million for each day the activity continues. In addition, the Dodd-Frank Act authorizes the Federal Reserve Board to require reports from and examine bank holding companies and their subsidiaries, and to regulate functionally regulated subsidiaries of bank holding companies.

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

Capital Adequacy Requirements. The Federal Reserve Board currently uses a system of risk-based capital guidelines to evaluate the capital adequacy of bank holding companies. Under the guidelines, a risk weight factor of 0% to 100% is assigned to each category of assets based generally on the perceived credit risk of the asset class. The risk weights are then multiplied by the corresponding asset balances to determine a "risk-weighted" asset base. Under the Federal Reserve Board's current regulatory capital standards, at least half of the risk-based capital must consist of core (Tier 1) capital, which is comprised of:

- common stockholders' equity (includes common stock and any related surplus, undivided profits, disclosed capital reserves that represent a segregation of undivided profits and foreign currency translation adjustments, excluding changes in other comprehensive income (loss));
- certain noncumulative perpetual preferred stock and related surplus; and
- minority interests in the equity capital accounts of consolidated subsidiaries (excludes goodwill and various intangible assets).

Under the Federal Reserve Board's current regulatory capital standards, the remainder, supplementary (Tier 2) capital, may consist of:

- allowance for loan losses, up to a maximum of 1.25% of risk-weighted assets;
- certain perpetual preferred stock and related surplus;
- hybrid capital instruments;
- perpetual debt;
- mandatory convertible debt securities;
- term subordinated debt;
- intermediate term preferred stock; and
- certain unrealized holding gains on equity securities.

Total capital is the sum of Tier 1 and Tier 2 capital. Under the Federal Reserve Board's current regulatory capital standards, the guidelines require a minimum ratio of total capital to total risk-weighted assets of 8.0% (of which at least 4.0% is required to consist of Tier 1 capital elements). At June 30, 2014, our ratio of Tier 1 capital to total risk-weighted assets was 18.11% and our ratio of total capital to total risk-weighted assets was 18.79%.

In addition to the risk-based capital guidelines, the Federal Reserve Board uses a leverage ratio as an additional tool to evaluate the capital adequacy of bank holding companies. The leverage ratio is a company's Tier 1 capital divided by its average total consolidated assets. We are required to maintain a leverage ratio of 4.0%, and, at June 30, 2014, our leverage ratio was 13.51%.

The federal banking agencies' risk-based and leverage ratios are minimum supervisory ratios generally applicable to banking organizations that meet certain specified criteria, assuming that they have the highest regulatory rating. Banking organizations not meeting these criteria are expected to operate with capital positions well above the minimum ratios. The federal bank regulatory agencies may set capital requirements for a particular banking organization that are higher than the minimum ratios when circumstances warrant. Federal Reserve Board guidelines also provide that banking organizations experiencing internal growth or making acquisitions will be expected to maintain strong capital positions substantially above the minimum supervisory levels, without significant reliance on intangible assets.

The Dodd-Frank Act directs federal banking agencies to establish minimum leverage capital requirements and minimum risk-based capital requirements for insured depository institutions, depository institution holding companies, and nonbank financial companies supervised by the Federal Reserve Board. These minimum capital requirements may not be less than the "generally applicable leverage and risk-based capital requirements" applicable to insured depository institutions, in effect applying the same leverage and risk-based capital requirements that apply to insured depository institutions to most bank holding companies. Beginning on January 1, 2015, Hilltop, PlainsCapital and the Bank will become subject to new capital rules based on Basel III requirements. These requirements are discussed below.

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

The aggregate liability of the holding company of an undercapitalized bank is limited to the lesser of 5% of the institution's assets at the time it became undercapitalized or the amount necessary to cause the institution to be "adequately capitalized." The bank regulators have greater power in situations where an institution becomes "significantly" or "critically" undercapitalized or fails to submit a capital restoration plan. For example, a bank holding company controlling such an institution can be required to obtain prior Federal Reserve Board approval of proposed dividends, or might be required to consent to a consolidation or to divest the troubled institution or other affiliates.

Acquisitions by Bank Holding Companies. The Bank Holding Company Act requires every bank holding company to obtain the prior approval of the Federal Reserve Board before it may acquire all or substantially all of the assets of any bank, or ownership or control of any voting shares of any bank, if after such acquisition it would own or control, directly or indirectly, more than 5% of the voting shares of such bank. In approving bank acquisitions by bank holding companies, the Federal Reserve Board is required to consider, among other things, the financial and managerial resources and future prospects of the bank holding company and the banks concerned, the convenience and needs of the communities to be served, and various competitive factors. In addition, the Dodd-Frank Act requires the Federal Reserve Board to consider "the risk to the stability of the U.S. banking or financial system" when evaluating acquisitions of banks and nonbanks under the Bank Holding Company Act. With respect to interstate acquisitions, the Dodd-Frank Act amends the Bank Holding Company Act by raising the standard by which interstate bank acquisitions are permitted from a standard that the acquiring bank holding company be "adequately capitalized" and "adequately managed", to the higher standard of being "well capitalized" and "well managed".

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Control Acquisitions. The Change in Bank Control Act prohibits a person or group of persons from acquiring "control" of a bank holding company unless the Federal Reserve Board has been notified and has not objected to the transaction. Under a rebuttable presumption established by the Federal Reserve Board, the acquisition of 10% or more of a class of voting stock of a bank holding company with a class of securities registered under Section 12 of the Exchange Act, would, under the circumstances set forth in the presumption, constitute acquisition of control of such company.

In addition, an entity is required to obtain the approval of the Federal Reserve Board under the Bank Holding Company Act before acquiring 25% (5% in the case of an acquirer that is a bank holding company) or more of any class of our outstanding common stock, or otherwise obtaining control or a "controlling influence" over us.

Emergency Economic Stabilization Act of 2008 and the Small Business Jobs Act of 2010. The U.S. Congress, the U.S. Department of the Treasury ("U.S. Treasury") and the federal banking regulators took broad action beginning in early September 2008 to address volatility in the U.S. banking system. The Emergency Economic Stabilization Act of 2008 authorized the U.S. Treasury to purchase from financial institutions and their holding companies certain mortgage loans, mortgage-backed securities and certain other financial instruments, including debt and equity securities issued by financial institutions and their holding companies in the Troubled Asset Relief Program ("TARP") Capital Purchase Program.

On December 19, 2008, PlainsCapital sold 87,631 shares of its Fixed Rate Cumulative Perpetual Stock, Series A and a warrant to purchase, upon net exercise, 4,382 shares of its Fixed Rate Cumulative Perpetual Stock, Series B to the U.S. Treasury for $87.6 million pursuant to the TARP Capital Purchase Program. The U.S. Treasury immediately exercised its warrant on December 19, 2008, and PlainsCapital issued the underlying shares of its Series B Preferred Stock to the U.S. Treasury. On September 27, 2011, PlainsCapital entered into a Securities Purchase Agreement with the Secretary of the Treasury (the "Purchase Agreement") pursuant to which PlainsCapital issued 114,068 shares of its newly designated Non-Cumulative Perpetual Preferred Stock, Series C for a total purchase price of $114,068,000. The proceeds from the sale of PlainsCapital's Series C Preferred Stock were used to redeem and repurchase PlainsCapital's Series A and Series B Preferred Stock. PlainsCapital's Series C Preferred Stock was issued pursuant to the Small Business Lending Fund program, a $30 billion fund established under the Small Business Jobs Act of 2010 that was created to encourage lending to small businesses by providing capital to qualified community banks with assets of less than $10 billion. In connection with the PlainsCapital Merger, Hilltop assumed PlainsCapital's obligations under the Purchase Agreement and redeemed PlainsCapital's outstanding Series C Preferred Stock in exchange for the Non-Cumulative Perpetual Preferred Stock, Series B of Hilltop (the "Hilltop Series B Preferred Stock").

On November 29, 2012, Hilltop filed with the State Department of Assessments and Taxation of the State of Maryland articles supplementary for the Hilltop Series B Preferred Stock, setting forth its terms. Holders of the Hilltop Series B Preferred Stock are entitled to noncumulative cash dividends at a fluctuating dividend rate based on the Bank's level of qualified small business lending ("QSBL"). The Hilltop Series B Preferred Stock is non-voting, except in limited circumstances, and ranks senior to Hilltop's common stock with respect to the payment of dividends and distribution of assets upon any liquidation, dissolution or winding up of Hilltop.

The terms of the Hilltop Series B Preferred Stock restrict Hilltop's ability to pay dividends on, make distributions with respect to, or redeem, purchase or acquire, or make a liquidation payment on its common stock and other Hilltop capital stock ranking junior to the Hilltop Series B Preferred Stock, and on other preferred stock and other stock ranking on a parity with the Hilltop Series B Preferred Stock, in the event that Hilltop does not declare dividends on the Hilltop Series B Preferred Stock during any dividend period.

The Hilltop Series B Preferred Stock qualifies as Tier 1 capital and is entitled to receive non-cumulative dividends, payable quarterly, on each January 1, April 1, July 1 and October 1. Until December 31, 2013, the dividend rate, as a percentage of the liquidation amount (being $1,000 per share of Series B Preferred Stock), fluctuated based upon changes in the level of QSBL by the Bank. From January 1, 2014 until March 26, 2016, the dividend rate is fixed at 5.0% based upon the Bank's level of QSBL at September 30, 2013. Beginning March 27, 2016, the dividend rate on any outstanding shares of Hilltop Series B Preferred Stock will be fixed at nine percent (9%) per annum.

Except as noted in the next sentence, the Hilltop Series B Preferred Stock may be redeemed at any time at the Company's option, at a redemption price of 100 percent of the liquidation amount (being $1,000 per share of Series B Preferred Stock) plus accrued but unpaid dividends to the date of redemption for the current period, subject to approval of the Federal Reserve Board. In the agreement and plan of merger with PlainsCapital Corporation, the Company agreed not to redeem or otherwise acquire the Hilltop Series B Preferred Stock prior to the second anniversary of the closing date of the PlainsCapital Merger, or November 30, 2014. For more information, see "Risk Factors Risks Relating to Hilltop's Business The Treasury's investment in us imposes restrictions and obligations upon us that could adversely affect the rights of our common stockholders."

Governmental Monetary Policies. Our earnings are affected by domestic economic conditions and the monetary and fiscal policies of the U.S. government and its agencies. The monetary policies of the Federal Reserve Board have had, and are likely to continue to have, an important impact on the operating results of commercial banks through its power to implement national monetary policy in order, among other things, to curb inflation or combat a recession. The monetary policies of the Federal Reserve Board affect the levels of bank loans, investments and deposits through its influence over the issuance of U.S. government securities, its regulation of the discount rate applicable to member banks and its influence over reserve requirements to which member banks are subject. We cannot predict the nature or impact of future changes in monetary and fiscal policies.

PlainsCapital Bank

The Bank is subject to various requirements and restrictions under the laws of the United States, and to regulation, supervision and regular examination by the Texas Department of Banking. The Bank, as a state member bank, is also subject to regulation and examination by the Federal Reserve Board. As a bank with less than $10 billion in assets, the Bank became subject to the regulations issued by the CFPB on July 21, 2011, although the Federal Reserve Board continued to examine the Bank for compliance with federal consumer protection laws. As of June 30, 2014, the Bank's total assets were $8.2 billion. If the Bank's total assets were to increase, either organically or through an acquisition, merger or combination, to over $10.0 billion (as measured on four consecutive quarterly call reports of the Bank and any institutions it acquires), the Bank would become subject to the CFPB's supervisory and enforcement authority with respect to federal consumer financial laws beginning in the following quarter. The Bank is also an insured depository institution and, therefore, subject to regulation by the FDIC, although the Federal Reserve Board is the Bank's primary federal regulator. The Federal Reserve Board, the Texas Department of Banking, the CFPB and the FDIC have the power to enforce compliance with applicable banking statutes and regulations. Such requirements and restrictions include requirements to maintain reserves against deposits, restrictions on the nature and amount of loans that may be made and the interest that may be charged thereon and restrictions relating to investments and other activities of the Bank. In July 2010, the FDIC voted to revise its Memorandum of Understanding with the primary federal regulators to enhance the FDIC's existing backup authorities over insured depository institutions that the FDIC does not directly supervise. As a result, the Bank may be subject to increased supervision by the FDIC.

Restrictions on Transactions with Affiliates. Transactions between the Bank and its nonbanking affiliates, including Hilltop and PlainsCapital, are subject to Section 23A of the Federal Reserve Act. In general, Section 23A imposes limits on the amount of such transactions, and also requires certain levels of collateral for loans to affiliated parties. It also limits the amount of advances to third parties that are collateralized by the securities or obligations of Hilltop or its subsidiaries. Among other changes, the Dodd-Frank Act expands the definition of "covered transactions" and clarifies the amount of time that the collateral requirements must be satisfied for covered transactions, and amends the definition of "affiliate" in Section 23A to include "any investment fund with respect to which a member bank or an affiliate thereof is an investment advisor."

Affiliate transactions are also subject to Section 23B of the Federal Reserve Act, which generally requires that certain transactions between the Bank and its affiliates be on terms substantially the same, or at least as favorable to the Bank, as those prevailing at the time for comparable transactions with or involving other nonaffiliated persons. The Federal Reserve has also issued Regulation W, which codifies prior regulations under Sections 23A and 23B of the Federal Reserve Act and interpretive guidance with respect to affiliate transactions.

Loans to Insiders. The restrictions on loans to directors, executive officers, principal stockholders and their related interests (collectively referred to herein as "insiders") contained in the Federal Reserve Act and Regulation O apply to all insured institutions and their subsidiaries and holding companies. These restrictions include limits on loans to one borrower and conditions that must be met before such a loan can be made. There is also an aggregate limitation on all loans to insiders and their related interests. These loans cannot exceed the institution's total unimpaired capital and surplus, and the Federal Reserve Board may determine that a lesser amount is appropriate. Insiders are subject to enforcement actions for knowingly accepting loans in violation of applicable restrictions. The Dodd-Frank Act amends the statutes placing limitations on loans to insiders by including credit exposures to the person arising from a derivatives transaction, repurchase agreement, reverse repurchase agreement, securities lending transaction, or securities borrowing transaction between the member bank and the person within the definition of an extension of credit.

Restrictions on Distribution of Subsidiary Bank Dividends and Assets. Dividends paid by the Bank have provided a substantial part of PlainsCapital's operating funds and for the foreseeable future it is anticipated that dividends paid by the Bank to PlainsCapital will continue to be PlainsCapital's and Hilltop's principal source of operating funds. Capital adequacy requirements serve to limit the amount of dividends that may be paid by the Bank. Pursuant to the Texas Finance Code, a Texas banking association may not pay a dividend that would reduce its outstanding capital and surplus unless it obtains the prior approval of the Texas Banking Commissioner. Additionally, the FDIC and the Federal Reserve Board have the authority to prohibit Texas state banks from paying a dividend when they determine the dividend would be an unsafe or unsound banking practice. As a member of the Federal Reserve System, the Bank must also comply with the dividend restrictions with which a national bank would be required to comply. Those provisions are generally similar to those imposed by the state of Texas. Among other things, the federal restrictions require that if losses have at any time been sustained by a bank equal to or exceeding its undivided profits then on hand, no dividend may be paid.

In the event of a liquidation or other resolution of an insured depository institution, the claims of depositors and other general or subordinated creditors are entitled to a priority of payment over the claims of holders of any obligation of the institution to its stockholders, including any depository institution holding company (such as PlainsCapital and Hilltop) or any stockholder or creditor thereof.

Branching. The establishment of a branch must be approved by the Texas Department of Banking and the Federal Reserve Board, which consider a number of factors, including financial history, capital adequacy, earnings prospects, character of management, needs of the community and consistency with corporate powers. The regulators will also consider the applicant's CRA record.

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Interstate Branching. Effective June 1, 1997, the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 (the "Riegle-Neal Act") amended the Federal Deposit Insurance Act and certain other statutes to permit state and national banks with different home states to merge across state lines, with approval of the appropriate federal banking agency, unless the home state of a participating bank had passed legislation prior to May 31, 1997 expressly prohibiting interstate mergers. Under the Riegle-Neal Act amendments, once a state or national bank has established branches in a state, that bank may establish and acquire additional branches at any location in the state at which any bank involved in the interstate merger transaction could have established or acquired branches under applicable federal or state law. If a state opted out of interstate branching within the specified time period, no bank in any other state may establish a branch in the state which has opted out, whether through an acquisition or de novo. Under the Dodd-Frank Act, de novo interstate branching by national banks is permitted if, under the laws of the state where the branch is to be located, a state bank chartered in that state would have been permitted to establish a branch.

Prompt Corrective Action. The Federal Deposit Insurance Corporation Improvement Act of 1991 establishes a system of prompt corrective action to resolve the problems of undercapitalized financial institutions. Under this system, the federal banking regulators have established five capital categories ("well capitalized," "adequately capitalized," "undercapitalized," "significantly undercapitalized" and "critically undercapitalized") in which all institutions are placed. Federal banking regulators are required to take various mandatory supervisory actions and are authorized to take other discretionary actions with respect to institutions in the three undercapitalized categories. The severity of the action depends upon the capital category in which the institution is placed. Generally, subject to a narrow exception, the banking regulator must appoint a receiver or conservator for an institution that is critically undercapitalized. The federal banking agencies have specified by regulation the relevant capital level for each category.

An institution that is categorized as "undercapitalized", "significantly undercapitalized" or "critically undercapitalized" is required to submit an acceptable capital restoration plan to its appropriate federal banking agency. A bank holding company must guarantee that a subsidiary depository institution meets its capital restoration plan, subject to various limitations. The controlling holding company's obligation to fund a capital restoration plan is limited to the lesser of 5% of an undercapitalized subsidiary's assets at the time it became undercapitalized or the amount required to meet regulatory capital requirements. An undercapitalized institution is also generally prohibited from increasing its average total assets, making acquisitions, establishing any branches or engaging in any new line of business, except under an accepted capital restoration plan or with FDIC approval. The regulations also establish procedures for downgrading an institution to a lower capital category based on supervisory factors other than capital.

FDIC Insurance Assessments. The FDIC has adopted a risk-based assessment system for insured depository institutions that takes into account the risks attributable to different categories and concentrations of assets and liabilities. The system assigns an institution to one of three capital categories: (1) "well capitalized;" (2) "adequately capitalized;" or (3) "undercapitalized." These three categories are substantially similar to the prompt corrective action categories described above, with the "undercapitalized" category including institutions that are undercapitalized, significantly undercapitalized and critically undercapitalized for prompt corrective action purposes. The FDIC also assigns an institution to one of three supervisory subgroups based on a supervisory evaluation that the institution's primary federal regulator provides to the FDIC and information that the FDIC determines to be relevant to the institution's financial condition and the risk posed to the deposit insurance funds. The FDIC may terminate its insurance of deposits if it finds that the institution has engaged in unsafe and unsound practices, is in an unsafe or unsound condition to continue operations, or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC.

In 2009, the FDIC adopted a final rule requiring a special assessment on insured institutions as part of its effort to rebuild the FDIC deposit insurance fund ("DIF"). The FDIC administers the DIF, and all insured depository institutions are required to pay assessments to the FDIC that fund the DIF. The Dodd-Frank Act broadens the base for FDIC insurance assessments. Assessments will now be based on the average consolidated total assets less tangible equity capital of a financial institution during the assessment period. On February 7, 2011, the FDIC issued a final rule implementing revisions to the assessment system mandated by the Dodd-Frank Act. The new regulation was effective April 1, 2011 and was reflected in the June 30, 2011 FDIC DIF balance and the invoices for assessments due September 30, 2011. Accruals for DIF assessments were $1.0 million for the year ended December 31, 2013.

The FDIC is required to maintain a designated reserve ratio of the DIF to insured deposits in the United States. The Dodd-Frank Act requires the FDIC to assess insured depository institutions to achieve a DIF ratio of at least 1.35 percent by September 30, 2020. Pursuant to its authority in the Dodd-Frank Act, the FDIC on December 20, 2010, published a final rule establishing a higher long-term target DIF ratio of greater than 2%. Deposit insurance assessment rates are subject to change by the FDIC and will be impacted by the overall economy and the stability of the banking industry as a whole. The FDIC will notify the Bank concerning an assessment rate that we will be charged for the assessment period. As a result of the new regulations, we expect to incur higher annual deposit insurance assessments, which could have a significant adverse impact on our financial condition and results of operations.

The Dodd-Frank Act permanently increased the standard maximum deposit insurance amount from $100,000 to $250,000. The FDIC insurance coverage limit applies per depositor, per insured depository institution for each account ownership category.

The Dodd-Frank Act instituted, for all insured depository institutions, unlimited deposit insurance on noninterest-bearing transaction accounts for the period from December 31, 2010 through December 31, 2012 for all depositors, including consumers, businesses and government entities. This unlimited insurance coverage, which expired on December 31, 2012, was separate from, and in addition to, the insurance coverage provided to a depositor's other deposit accounts held at an FDIC-insured institution up to the permissible limit of $250,000.

Community Reinvestment Act. The CRA requires, in connection with examinations of financial institutions, that federal banking regulators (in the Bank's case, the Federal Reserve Board) evaluate the record of each financial institution in meeting the credit needs of its local community, including low and moderate-income neighborhoods. These facts are also considered in evaluating mergers, acquisitions and applications to open a branch or facility. Failure to adequately meet these criteria could impose additional requirements and limitations on the Bank. Additionally, the Bank must publicly disclose the terms of various CRA-related agreements.

During the second quarter of 2013, the Bank received a "satisfactory" CRA rating in connection with its most recent CRA performance evaluation. A CRA rating of less than "satisfactory" adversely affects a bank's ability to establish new branches and impairs a bank's ability to commence new activities that are "financial in nature" or acquire companies engaged in these activities. See "Risk Factors Risks Relating to Hilltop's Business We are subject to extensive supervision and regulation that could restrict our activities and impose financial requirements or limitations on the conduct of our business and limit our ability to generate income."

Privacy. Under the Gramm-Leach-Bliley Act, financial institutions are required to disclose their policies for collecting and protecting confidential information. Customers generally may prevent financial institutions from sharing nonpublic personal financial information with nonaffiliated third parties except under narrow circumstances, such as the processing of transactions requested by the consumer or when the financial institution is jointly sponsoring a product or service with a nonaffiliated third party. Additionally, financial institutions generally may not disclose consumer account numbers to any nonaffiliated third party for use in telemarketing, direct mail marketing or other marketing to consumers. The Bank and all of its subsidiaries have established policies and procedures to comply with the privacy provisions of the Gramm-Leach-Bliley Act.

Federal Laws Applicable to Credit Transactions. The loan operations of the Bank are also subject to federal laws applicable to credit transactions, such as the:

- Truth-In-Lending Act, governing disclosures of credit terms to consumer borrowers;
- Home Mortgage Disclosure Act of 1975, requiring financial institutions to provide information to enable the public and public officials to determine whether a financial institution is fulfilling its obligation to help meet the housing needs of the community it serves;
- Equal Credit Opportunity Act, prohibiting discrimination on the basis of race, creed or other prohibited factors in extending credit;
- Fair Credit Reporting Act of 1978, governing the use and provision of information to credit reporting agencies and preventing identity theft;
- Fair Debt Collection Practices Act, governing the manner in which consumer debts may be collected by collection agencies;
- Service Members Civil Relief Act, which amended the Soldiers' and Sailors' Civil Relief Act of 1940, governing the repayment terms of, and property rights underlying, secured obligations of persons in military service;
- The Dodd-Frank Act, which establishes the CFPB, an independent entity within the Federal Reserve, dedicated to promulgating and enforcing consumer protection laws applicable to all entities offering consumer financial services or products; and
- The rules and regulations of the various federal agencies charged with the responsibility of implementing these federal laws.

Interest and other charges collected or contracted for by the Bank are subject to state usury laws and federal laws concerning interest rates.

Federal Laws Applicable to Deposit Operations. The deposit operations of the Bank are subject to:

- Right to Financial Privacy Act, which imposes a duty to maintain confidentiality of consumer financial records and prescribes procedures for complying with administrative subpoenas of financial records;
- Truth in Savings Act, which requires the Bank to disclose the terms and conditions on which interest is paid and fees are assessed in connection with deposit accounts; and
- Electronic Funds Transfer Act and Regulation E issued by the Federal Reserve Board and the CFPB to implement that act, which govern automatic deposits to and withdrawals from deposit accounts and customers' rights and liabilities arising from the use of ATMs and other electronic banking services. The Dodd-Frank Act amends the Electronic Funds Transfer Act to, among other things, give the Federal Reserve Board the authority to establish rules regarding interchange fees charged for electronic debit transactions by payment card issuers having assets over $10 billion and to enforce a new statutory requirement that such fees be reasonable and proportional to the actual cost of a transaction to the issuer.

Capital Requirements. The Federal Reserve Board and the Texas Department of Banking monitor the capital adequacy of the Bank by using a combination of risk-based guidelines and leverage ratios. The agencies consider the Bank's capital levels when taking action on various types of applications and when conducting supervisory activities related to the safety and soundness of individual banks and the banking system.

Under the regulatory capital guidelines (without giving effect to Basel III discussed below), the Bank must maintain a total risk-based capital to risk-weighted assets ratio of at least 8.0%, a Tier 1 capital to risk-weighted assets ratio of at least 4.0%, and a Tier 1 capital to average total assets ratio of at least 4.0% (3.0% for banks receiving the highest examination rating) to be considered "adequately capitalized." See the discussion herein under "The FDIC Improvement Act." At June 30, 2014, the Bank's ratio of total risk-based capital to risk-weighted assets was 13.90%, the Bank's ratio of Tier 1 capital to risk-weighted assets was 13.22% and the Bank's ratio of Tier 1 capital to average total assets was 9.97%.

BASEL III. In December 2010, the Basel Committee on Banking Supervision (the "Basel Committee") released revised frameworks for the regulation of capital and liquidity of internationally active banking organizations. These new frameworks are generally referred to as "Basel III." On July 2, 2013, the Federal Reserve, the FDIC, and the Office of the Comptroller of the Currency released final rules that substantially amend the regulatory risk-based capital rules applicable to the Company and the Bank. These final rules implement the Basel III regulatory capital reforms and changes required by the Dodd-Frank Act. Hilltop, PlainsCapital and the Bank will begin transitioning to the new final rules on January 1, 2015 when new minimum capital requirements, as set forth in the table below, are effective. However, the new capital conservation buffer and certain deductions from common equity Tier 1 capital phase in over a time period from 2015 through 2019.

The following table summarizes the Basel III transition schedule for new ratios and capital definitions beginning January 1, 2015.

Year (as of January 1)	2015	2016	2017	2018	2019
Minimum common equity Tier 1 capital ratio	4.5%	4.5%	4.5%	4.5%	4.5%
Common equity Tier 1 capital conservation buffer	N/A	0.625%	1.25%	1.875%	2.5%
Minimum common equity Tier 1 capital ratio plus capital conservation buffer	4.5%	5.125%	5.75%	6.375%	7.0%
Phase-in of most deductions from common equity Tier 1 (including 10 percent & 15 percent common equity Tier 1 threshold deduction items that are over the limits)(1)	40.0%	60.0%	80.0%	100.0%	100.0%
Minimum Tier 1 capital ratio	6.0%	6.0%	6.0%	6.0%	6.0%
Minimum Tier 1 capital ratio plus capital conservation buffer	N/A	6.625%	7.25%	7.875%	8.5%
Minimum total capital ratio	8.0%	8.0%	8.0%	8.0%	8.0%
Minimum total capital ratio plus conservation buffer	N/A	8.625%	9.25%	9.875%	10.5%

* N/A means not applicable.

(1) Deductions from common equity Tier 1 capital include goodwill and other intangibles, deferred tax assets that arise from net operating loss and tax credit carryforwards (above certain levels), gains-on-sale in connection with a securitization, any defined benefit pension fund net asset (for banking organizations that are not insured depository institutions), investments in a banking organization's own capital instruments, mortgage servicing assets (above certain levels) and investments in the capital of unconsolidated financial institutions (above certain levels).

The new rules take important steps toward improving the quality and increasing the quantity of capital for all banking organizations as well as setting higher standards for large, internationally active banking organizations. The regulatory agencies believe that the new rules will result in capital requirements that better reflect banking organizations' risk profiles, thereby improving the overall resilience of the banking system. The regulatory agencies carefully considered the potential impacts on all banking organizations, including community banking organizations such as Hilltop and the Bank, and sought to minimize the potential burden of these changes where consistent with applicable law and the agencies' goals of establishing a robust and comprehensive capital framework.

The new rules treatment of one- to four-family residential mortgage exposures remains the same as under current general risk-based capital rules. This includes a 50 percent risk weight for prudently underwritten first lien mortgage loans that are not past due, reported as nonaccrual, or restructured, and a 100 percent risk weight for all other residential mortgages. Also in the new rules, non-advanced approaches banking organizations, such as Hilltop and the Bank, are given a one-time option to filter certain Accumulated Other Comprehensive Income ("AOCI") components, comparable to the treatment under the current general risk-based capital rule. The AOCI opt-out election must be made on the institution's first regulatory filing after January 1, 2015.

The new rules also make certain major changes from the current general risk-based capital rules, including, but not limited to the following:

- Implementing higher minimum capital requirements, including a new common equity Tier 1 capital requirement, and establishes criteria that instruments must meet in order to be considered common equity Tier 1 capital, additional Tier 1 capital or Tier 2 capital. The new minimum capital to risk-weighted assets requirements are a common equity Tier 1 capital ratio of 4.5 percent and a Tier 1 capital ratio of 6.0 percent (an increase from 4.0 percent), and a total capital ratio that remains at 8.0 percent. The minimum leverage ratio (Tier 1 capital to total assets) is 4.0 percent. The new rules maintain the general structure of the current prompt corrective action framework (described below) while incorporating these increased minimum requirements starting January 1, 2015.

- Changing the definition of capital by incorporating stricter eligibility criteria for regulatory capital instruments that would disallow the including of instruments such as trust preferred securities in Tier 1 capital going forward, and new constraints on the inclusion of minority interests, mortgage-servicing rights, deferred tax assets, and other certain investments in the capital of unconsolidated financial institutions. In addition, the new rules require that most regulatory capital deductions be made from common equity Tier 1 capital.

- The Dodd-Frank Act prohibits references to, and reliance on, external credit ratings in the banking regulations and directs the agencies to use alternative standards of creditworthiness. The new rules replace the ratings-based approach with a simplified supervisory formula approach in order to determine the appropriate risk-weights of securitization exposures. Alternatively, banking organizations may use the existing gross-up approach to assign securitization exposures to a risk weight category or choose to assign such exposures a 1,250 percent risk weight.

- Mortgage servicing assets and deferred tax assets are subject to stricter individual and aggregate limitations as a percentage of common equity Tier 1 capital than those applicable under the current general risk-based capital rules.

- Increasing the risk weights for past-due loans, certain commercial real estate loans, and some equity exposures, and makes selected other changes in risk-weights and credit conversion factors.

- In order to avoid limitations on capital distributions, including dividend payments and certain discretionary bonus payments to executive officers, a banking organization must hold a capital conservation buffer composed of common equity Tier 1 capital above its minimum risk-based capital requirements. This buffer will help to ensure that banking organizations conserve capital when it is most needed, allowing them to better weather periods of economic stress. The buffer is measured relative to risk-weighted assets. Phase-in of the capital conservation buffer requirements will begin on January 1, 2016.

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The following table summarizes how much a banking organization can pay out in the form of distributions or discretionary bonus payments in a quarter based on its capital conservation buffer. A banking organization with a buffer greater than 2.5 percent would not be subject to limits on capital distributions or discretionary bonus payments; however, a banking organization with a buffer of less than 2.5 percent would be subject to increasingly stringent limitations as the buffer approaches zero.

Capital Conservation Buffer (as a percentage of risk-weighted assets)	**Maximum Payout (as a percentage of eligible retained income)**
Greater than 2.5 percent	No payout limitation applies
Less than or equal to 2.5 percent and greater than 1.875 percent	60 percent
Less than or equal to 1.875 percent and greater than 1.25 percent	40 percent
Less than or equal to 1.25 percent and greater than 0.625 percent	20 percent
Less than or equal to 0.625 percent	0 percent

The new rules also prohibit a banking organization from making distributions or discretionary bonus payments during any quarter if its eligible retained income is negative in that quarter and its capital conservation buffer ratio was less than 2.5 percent at the beginning of the quarter. The eligible retained income of a banking organization is defined as its net income for the four calendar quarters preceding the current calendar quarter, based on the organization's quarterly regulatory reports, net of any distributions and associated tax effects not already reflected in net income. When the new rules are fully phased-in in 2019, the minimum capital requirements plus the capital conservation buffer will exceed the prompt corrective action well-capitalized thresholds.

Although these new capital ratios do not become effective until 2015 and 2016, the banking regulators will expect bank holding companies and banks to meet these requirements well ahead of that date. The bank regulatory agencies may also set higher capital requirements for holding companies or banks whose circumstances warrant it. For example, holding companies experiencing internal growth or making acquisitions are expected to maintain strong capital positions substantially above the minimum supervisory levels, without significant reliance on intangible assets. At this time, the bank regulatory agencies are more inclined to impose higher capital requirements in order to meet well-capitalized standards, and future regulatory change could impose higher capital standards as a routine matter.

On January 6, 2013, the Group of Governors and Heads of Supervision, the oversight body of the Basel Committee, met and unanimously endorsed a four year delay in the Basel Committee's rules establishing a liquidity coverage ratio ("LCR"). Under the revised liquidity requirements, large, internationally active banks would be required to meet 60 percent of the LCR obligations by 2015, and the full rule would be phased in annually through 2019. The proposal would also apply a less stringent, modified LCR to bank holding companies and savings and loan holding companies that are not internally active but have more than $50 billion in total assets, such as the Company. The proposal would not apply to bank holding companies with less than $50 billion in total assets. We continue to monitor developments related to Basel III.

FIRREA. The Financial Institutions Reform, Recovery and Enforcement Act of 1989, or FIRREA, includes various provisions that affect or may affect the Bank. Among other matters, FIRREA generally permits bank holding companies to acquire healthy thrifts as well as failed or failing thrifts. FIRREA removed certain cross marketing prohibitions previously applicable to thrift and bank subsidiaries of a common holding company. Furthermore, a multi-bank holding company may now be required to indemnify the DIF against losses it incurs with respect to such company's affiliated banks, which in effect makes a bank holding company's equity investments in healthy bank subsidiaries available to the FDIC to assist such company's failing or failed bank subsidiaries.

In addition, pursuant to FIRREA, any depository institution that has been chartered less than two years, is not in compliance with the minimum capital requirements of its primary federal banking regulator, or is otherwise in a troubled condition must notify its primary federal banking regulator of the proposed addition of any person to its board of directors or the employment of any person as a senior executive officer of the institution at least 30 days before such addition or employment becomes effective. During such 30 day period, the applicable federal banking regulatory agency may disapprove of the addition of or employment of such director or officer. The Bank is not subject to any such requirements. FIRREA also expanded and increased civil and criminal penalties available for use by the appropriate regulatory agency against certain "institution affiliated parties" primarily including: (i) management, employees and agents of a financial institution; (ii) independent contractors such as attorneys and accountants and others who participate in the conduct of the financial institution's affairs and who caused or are likely to cause more than minimum financial loss to or a significant adverse effect on the institution, who knowingly or recklessly violate a law or regulation, breach a fiduciary duty or engage in unsafe or unsound practices. Such practices can include the failure of an institution to timely file required reports or the submission of inaccurate reports. Furthermore, FIRREA authorizes the appropriate banking agency to issue cease and desist orders that may, among other things, require affirmative action to correct any harm resulting from a violation or practice, including restitution, reimbursement, indemnifications or guarantees against loss. A financial institution may also be ordered to restrict its growth, dispose of certain assets or take other action as determined by the ordering agency to be appropriate.

The FDIC Improvement Act. The Federal Deposit Insurance Corporation Improvement Act of 1991, or FDICIA, made a number of reforms addressing the safety and soundness of the deposit insurance system, supervision of domestic and foreign depository institutions, and improvement of accounting standards. This statute also limited deposit insurance coverage, implemented changes in consumer protection laws and provided for least-cost resolution and prompt regulatory action with regard to troubled institutions.

FDICIA requires every bank with total assets in excess of $500 million to have an annual independent audit made of the bank's financial statements by a certified public accountant to verify that the financial statements of the bank are presented in accordance with GAAP and comply with such other disclosure requirements as prescribed by the FDIC.

FDICIA also places certain restrictions on activities of banks depending on their level of capital. FDICIA divides banks into five different categories, depending on their level of capital. Under current regulations:

- a bank is deemed to be "well capitalized" if it has a total Risk-Based Capital Ratio of 10.0% or more, a Tier 1 Capital Ratio of 6.0% or more, a Leverage Ratio of 5.0% or more, and the bank is not subject to an order or capital directive to meet and maintain a certain capital level;

- a bank is deemed to be "adequately capitalized" if it has a total Risk-Based Capital Ratio of 8.0% or more, a Tier 1 Capital Ratio of 4.0% or more and a Leverage Ratio of 4.0% or more (unless it receives the highest composite rating at its most recent examination and is not experiencing or anticipating significant growth, in which instance it must maintain a Leverage Ratio of 3.0% or more);

- a bank is deemed to be "undercapitalized" if it has a total Risk-Based Capital Ratio of less than 8.0%, a Tier 1 Capital Ratio of less than 4.0% or a Leverage Ratio of less than 4.0%;

- a bank is deemed to be "significantly undercapitalized" if it has a Risk-Based Capital Ratio of less than 6.0%, a Tier 1 Capital Ratio of less than 3.0% and a Leverage Ratio of less than 3.0%; and

- a bank is deemed to be "critically undercapitalized" if it has a Leverage Ratio of less than or equal to 2.0%.

Under the new capital rules discussed above, banks will have to maintain a common equity Tier 1 capital ratio of 6.5%, a Tier 1 capital ratio of 8%, a total capital ratio of 10%, and a leverage ratio of 5% to be deemed "well capitalized" for purposes of certain rules and prompt corrective action requirements.

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In addition, the FDIC has the ability to downgrade a bank's classification (but not to "critically undercapitalized") based on other considerations even if the bank meets the capital guidelines. According to these guidelines, the Bank was classified as "well capitalized" at June 30, 2014.

In addition, if a bank is classified as "undercapitalized," the bank is required to submit a capital restoration plan to the federal banking regulators. Pursuant to FDICIA, an "undercapitalized" bank is prohibited from increasing its assets, engaging in a new line of business, acquiring any interest in any company or insured depository institution, or opening or acquiring a new branch office, except under certain circumstances, including the acceptance by the federal banking regulators of a capital restoration plan for the bank.

Furthermore, if a bank is classified as "undercapitalized," the federal banking regulators may take certain actions to correct the capital position of the bank; if a bank is classified as "significantly undercapitalized" or "critically undercapitalized," the federal banking regulators would be required to take one or more prompt corrective actions. These actions would include, among other things, requiring: sales of new securities to bolster capital, improvements in management, limits on interest rates paid, prohibitions on transactions with affiliates, termination of certain risky activities and restrictions on compensation paid to executive officers. If a bank is classified as "critically undercapitalized," FDICIA requires the bank to be placed into conservatorship or receivership within 90 days, unless the federal banking regulators determines that other action would better achieve the purposes of FDICIA regarding prompt corrective action with respect to undercapitalized banks.

The capital classification of a bank affects the frequency of examinations of the bank and impacts the ability of the bank to engage in certain activities and affects the deposit insurance premiums paid by such bank. Under FDICIA, the federal banking regulators are required to conduct a full-scope, on-site examination of every bank at least once every 12 months. An exception to this rule is made, however, that provides that banks (i) with assets of less than $100 million, (ii) that are categorized as "well capitalized," (iii) that were found to be well managed and composite rating was outstanding and (iv) have not been subject to a change in control during the last 12 months, need only be examined once every 18 months.

Brokered Deposits. Under FDICIA, banks may be restricted in their ability to accept brokered deposits, depending on their capital classification. "Well capitalized" banks are permitted to accept brokered deposits, but banks that are not "well capitalized" are not permitted to accept such deposits. The FDIC may, on a case-by-case basis, permit banks that are "adequately capitalized" to accept brokered deposits if the FDIC determines that acceptance of such deposits would not constitute an unsafe or unsound banking practice with respect to the bank. At June 30, 2014, the Bank was "well capitalized" and therefore not subject to any limitations with respect to its brokered deposits. Brokered deposits are the subject of a study under the Dodd-Frank Act.

Federal limitations on activities and investments. The equity investments and activities, as a principle of FDIC-insured state-chartered banks, are generally limited to those that are permissible for national banks. Under regulations dealing with equity investments, an insured state bank generally may not directly or indirectly acquire or retain any equity investment of a type, or in an amount, that is not permissible for a national bank.

Check Clearing for the 21st Century Act. The Check Clearing for the 21st Century Act gives "substitute checks," such as a digital image of a check and copies made from that image, the same legal standing as the original paper check.

Federal Home Loan Bank System. The Federal Home Loan Bank, or FHLB, system, of which the Bank is a member, consists of 12 regional FHLBs governed and regulated by the Federal Housing Finance Board. The FHLBs serve as reserve or credit facilities for member institutions within their assigned regions. The reserves are funded primarily from proceeds derived from the sale of consolidated obligations of the FHLB system. The FHLBs make loans (i.e., advances) to members in accordance with policies and procedures established by the FHLB and the boards of directors of each regional FHLB.

As a system member, according to currently existing policies and procedures, the Bank is entitled to borrow from the FHLB of its respective region and is required to own a certain amount of capital stock in the FHLB. The Bank is in compliance with the stock ownership rules with respect to such advances, commitments and letters of credit and home mortgage loans and similar obligations. All loans, advances and other extensions of credit made by the FHLB to the Bank are secured by a portion of the respective mortgage loan portfolio, certain other investments and the capital stock of the FHLB held by the Bank.

Anti-terrorism and Money Laundering Legislation. The Bank is subject to the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism of 2001 (the "USA PATRIOT Act"), the Bank Secrecy Act and rules and regulations of the Office of Foreign Assets Control. These statutes and related rules and regulations impose requirements and limitations on specific financial transactions and account relationships intended to guard against money laundering and terrorism financing. The Bank has established a customer identification program pursuant to Section 326 of the USA PATRIOT Act and the Bank Secrecy Act, and otherwise has implemented policies and procedures intended to comply with the foregoing rules.

PrimeLending

PrimeLending and the Bank are subject to the rules and regulations of the CFPB, FHA, VA, the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation and Government National Mortgage Association with respect to originating, processing, selling and servicing mortgage loans and the issuance and sale of mortgage-backed securities. Those rules and regulations, among other things, prohibit discrimination and establish underwriting guidelines which include provisions for inspections and appraisals, require credit reports on prospective borrowers and fix maximum loan amounts, and, with respect to VA loans, fix maximum interest rates. Mortgage origination activities are subject to, among others, the Equal Credit Opportunity Act, Federal Truth-in-Lending Act, Secure and Fair Enforcement of Mortgage Licensing Act, Home Mortgage Disclosure Act, Fair Credit Reporting Act and the Real Estate Settlement Procedures Act and the regulations promulgated thereunder which, among other things, prohibit discrimination and require the disclosure of certain basic information to borrowers concerning credit terms and settlement costs. PrimeLending and the Bank are also subject to regulation by the Texas Department of Banking with respect to, among other things, the establishment of maximum origination fees on certain types of mortgage loan products. PrimeLending and the Bank are also subject to the provisions of the Dodd-Frank Act. Among other things, the Dodd-Frank Act established the CFPB and provides mortgage reform provisions regarding a customer's ability to repay, restrictions on variable-rate lending, loan officers' compensation, risk retention, and new disclosure requirements. The Dodd-Frank Act also clarifies that applicable state laws, rules and regulations related to the origination, processing, selling and servicing of mortgage loans continue to apply to PrimeLending. The additional regulatory requirements affecting our mortgage origination operations will result in increased compliance costs and may impact revenue.

On August 16, 2010, the Federal Reserve Board published a final rule on loan broker compensation, pursuant to the Dodd-Frank Act, which prohibits certain compensation payments to loan brokers and the practice of steering consumers to loans not in their interest when it will result in greater compensation for a loan broker. This final rule became effective on April 1, 2011, however, the Federal Reserve Board noted in the final rule that the CFPB may clarify the rule in the future pursuant to the CFPB's authority granted under the Dodd-Frank Act. The CFPB's final rule addressing mortgage loan originator compensation is discussed in more detail below.

In addition, the Dodd-Frank Act directed the Federal Reserve Board to promulgate regulations requiring lenders and securitizers to retain an economic interest in the credit risk relating to loans the lender sells and other asset-backed securities that the securitizer issues if the loans have not complied with the ability to repay standards spelled out in the Dodd-Frank Act and its implementing regulations. The risk retention requirement has not become effective to date but is expected to be 5%, subject to increase or decrease by regulation. Final regulations have not yet been issued.

On March 2, 2011, the Federal Reserve Board published a final rule implementing a provision in the Dodd-Frank Act that provides a separate, higher rate threshold for determining when the escrow requirements apply to higher-priced mortgage loans that exceed the maximum principal obligation eligible for purchase by Freddie Mac.

In January 2013, the CFPB published final rules that will impact mortgage origination and servicing. Had these final rules not been published, many of the statutory requirements in Title XIV of the Dodd-Frank Act would have become effective on January 21, 2013 without any implementing regulations. Unless noted below, these final rules became effective in January 2014.

The final rules concerning mortgage origination and servicing address the following topics:

Ability to Repay. This final rule implements the Dodd-Frank Act provisions requiring that for residential mortgages, creditors must make a reasonable and good faith determination based on verified and documented information that the consumer has a reasonable ability to repay the loan according to its terms. The final rule also establishes a presumption of compliance with the ability to repay determination for a certain category of mortgages called "qualified mortgages" meeting a series of detailed requirements. The final rule also provides a rebuttable presumption for higher-priced mortgage loans.

High-Cost Mortgage. This final rule strengthens consumer protections for high-cost mortgages (generally bans balloon payments and prepayment penalties, subject to exceptions and bans or limits certain fees and practices) and requires consumers to receive information about homeownership counseling prior to taking out a high-cost mortgage.

Appraisals for High-Risk Mortgages. The final rule permits a creditor to extend a higher-priced (subprime) mortgage loan ("HPML) only if the following conditions are met (subject to exceptions): (i) the creditor obtains a written appraisal; (ii) the appraisal is performed by a certified or licensed appraiser; and (iii) the appraiser conducts a physical property visit of the interior of the property. The rule also requires that during the application process, the applicant receives a notice regarding the appraisal process and their right to receive a free copy of the appraisal.

Copies of Appraisals. This final rule amends Regulation B that implements the Equal Credit Opportunity Act. It requires a creditor to provide a free copy of appraisal or valuation reports prepared in connection with any closed-end loan secured by a first lien on a dwelling. The final rule requires notice to applicants of the right to receive copies of any appraisal or valuation reports and creditors must send copies of the reports whether or not the loan transaction is consummated. Creditors must provide the copies of the appraisal or evaluation reports for free, however, the creditors may charge reasonable fees for the cost of the appraisal or valuation unless applicable law provides otherwise.

Escrow Requirements. This final rule implements Dodd-Frank Act changes that generally extend the required duration of an escrow account on certain higher-priced mortgage loans from a minimum of one year to a minimum of five years, subject to certain exemptions for loans made by certain creditors that operate predominantly in rural or underserved areas, as long as certain other criteria are met. This final rule became effective on June 1, 2013.

Servicing. Two final rules were published to implement laws to protect consumers from detrimental actions by mortgage servicers and to provide consumers with better tools and information when dealing with mortgage servicers. One final rule amends Regulation Z, which implements the Truth in Lending Act, and a second final rule amends Regulation X, which implements the Real Estate Settlement Procedures Act. The rules cover nine major topics implementing the Dodd-Frank Act provisions related to mortgage servicing. The final rules include a number of exemptions and other adjustments for small servicers, defined as servicers that service 5,000 or fewer mortgage loans and service only mortgage loans that they or an affiliate originated or own.

Mortgage Loan Originator Compensation. This final rule implements Dodd-Frank Act requirements, as well as revises and clarifies existing regulations and commentary on loan originator compensation. The rule also prohibits, among other things: (i) certain arbitration agreements; (ii) financing certain credit insurance in connection with a mortgage loan; (iii) compensation based on a term of a transaction or a proxy for a term of a transaction; and (iv) dual compensation from a consumer and another person in connection with the transaction. The final rule also imposes a duty on individual loan officers, mortgage brokers and creditors to be "qualified" and, when applicable, registered or licensed to the extent required under applicable State and Federal law.

Additional rules and regulations are expected including risk retention rules which would require lenders and securitizers to retain an economic interest in the credit risk relating to loans the lender sells and other asset-backed securities that the securitizer issues if the loans have not complied with the ability to repay standards spelled out in the Dodd-Frank Act and its implementing regulations. The risk retention requirement has not become effective to date but is expected to be 5%, subject to increase or decrease by regulation. Any additional regulatory requirements affecting PrimeLending mortgage origination operations will result in increased compliance costs and may impact revenue.

NLC

NLC's insurance subsidiaries, NLIC and ASIC, are subject to regulation and supervision in each state where they are licensed to do business. This regulation and supervision is vested in state agencies having broad administrative power over the various aspects of the business of NLIC and ASIC.

State insurance holding company regulation. NLC controls two operating insurance companies, NLIC and ASIC, and is subject to the insurance holding company laws of Texas, the state in which those insurance companies are domiciled. These laws generally require NLC to register with the Texas Department of Insurance and periodically to furnish financial and other information about the operations of companies within its holding company structure. Generally under these laws, all transactions between an insurer and an affiliated company in its holding company structure, including sales, loans, reinsurance agreements and service agreements, must be fair and reasonable and, if satisfying a specified threshold amount or of a specified category, require prior notice and approval or non-objection by the Texas Department of Insurance.

National Association of Insurance Commissioners. The National Association of Insurance Commissioners, or NAIC, is a group consisting of state insurance commissioners that discuss issues and formulate policy with respect to regulation, reporting and accounting for insurance companies. Although the NAIC has no legislative authority and insurance companies are at all times subject to the laws of their respective domiciliary states and, to a lesser extent, other states in which they conduct business, the NAIC is influential in determining the form in which such laws are enacted. Certain Model Insurance Laws, Regulations and Guidelines, or Model Laws, have been promulgated by the NAIC as a minimum standard by which state regulatory systems and regulations are measured. Adoption of state laws that provide for substantially similar regulations to those described in the Model Laws is a requirement for accreditation by the NAIC.

The NAIC provides authoritative guidance to insurance regulators on current statutory accounting issues by promulgating and updating a codified set of statutory accounting practices in its Accounting

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Practices and Procedures Manual. The Texas Department of Insurance has generally adopted these codified statutory accounting practices.

Texas also has adopted laws substantially similar to the NAIC's risk based capital, or RBC laws, which require insurers to maintain minimum levels of capital based on their investments and operations. Domestic property and casualty insurers are required to report their RBC based on a formula that attempts to measure statutory capital and surplus needs based on the risks in the insurer's mix of products and investment portfolio. The formula is designed to allow the Texas Department of Insurance to identify potential inadequately capitalized companies. Under the formula, a company determines its RBC by taking into account certain risks related to its assets (including risks related to its investment portfolio and ceded reinsurance) and its liabilities (including underwriting risks related to the nature and experience of its insurance business). Among other requirements, an insurance company must maintain capital and surplus of at least 200% of the RBC computed by the NAIC's RBC model (known as the "Authorized Control Level" of RBC). At December 31, 2013, the most recent date for which the RBC calculation was performed, NLIC and ASIC capital and surplus levels exceeded the minimum RBC requirements that would trigger regulatory attention. In their 2013 statutory financial statements, both NLIC and ASIC complied with the NAIC's RBC reporting requirements. As of June 30, 2014, management was not aware of any changes in financial condition or structure that would cause NLIC or ASIC to not be in compliance with the required RBC ratio.

The NAIC's Insurance Regulatory Information System, or IRIS, was developed to assist state insurance departments in executing their statutory mandates to oversee the financial condition of insurance companies. IRIS identifies twelve industry ratios and specifies a range of "usual values" for each ratio. Departure from the usual values on four or more of these ratios can lead to inquiries from state insurance commissioners as to certain aspects of an insurer's business. For 2013, all ratios for both NLIC and ASIC were within the usual values with two exceptions. Both companies fell below the indicated minimum investment yield range of 3%, with NLIC at 2.0% and ASIC at 1.4%, due to the concentration in cash at each company. We expect improvement in the yields at both companies as appropriate investment opportunities are identified. Additionally, NLIC's two-year operating ratio was calculated at 100%, which equals the threshold of 100%, primarily due to the significant weather events experienced over the past two year period.

The NAIC adopted an amendment to its "Model Audit Rule" in response to the passage of the Sarbanes-Oxley Act of 2002, or SOX. The amendment is effective for financial statements for accounting periods after January 1, 2010. This amendment addresses auditor independence, corporate governance and, most notably, the application of certain provisions of Section 404 of SOX regarding internal control reporting. The rules relating to internal controls apply to insurers with gross direct and assumed written premiums of $500 million or more, measured at the legal entity level (rather than at the insurance holding company level), and to insurers that the domiciliary commissioner selects from among those identified as in hazardous condition, but exempts SOX compliant entities. Neither NLIC nor ASIC currently has direct and assumed written premiums of at least $500 million, but it is conceivable that this may change in the future; however, NLC must be SOX compliant because it is wholly owned by Hilltop, a public company subject to SOX compliance.

Legislative changes. From time to time, various regulatory and legislative changes have been, or are, proposed that would adversely affect the insurance industry. Among the proposals that have been, or are being, considered are the possible introduction of Federal regulation in addition to, or in lieu of, the current system of state regulation of insurers and proposals in various state legislatures (some of which proposals have been enacted) to conform portions of their insurance laws and regulations to various Model Laws adopted by the NAIC. NLC is unable to predict whether any of these laws and regulations will be adopted, the form in which any such laws and regulations would be adopted, or the effect, if any, these developments would have on its financial condition or results of operations.

In November 2002, in response to the tightening supply in certain insurance and reinsurance markets resulting from, among other things, the September 11, 2001 terrorist attacks, the Terrorism Risk Insurance Act, or TRIA, was enacted. TRIA was modified and extended by the Terrorism Risk Insurance Extension Act of 2005 and extended again by the Terrorism Risk Insurance Program Reauthorization Act of 2007. These Acts created a Federal Program designed to ensure the availability of commercial insurance coverage for terrorist acts in the United States. This Program helped the commercial property and casualty insurance industry cover claims related to terrorism-related losses and requires such companies to offer coverage for certain acts of terrorism. As a result, NLC is prohibited from adding certain terrorism exclusions to the policies written by its insurance company subsidiaries. The 2005 Act extended the Program through 2007, but eliminated commercial auto, farm-owners and certain other commercial coverages from its scope. The Reauthorization Act further extended the Program through December 31, 2014 and fixed the reimbursement percentage at 85% and the deductible at 20%. Although NLC is protected by federally funded terrorism reinsurance as provided for in the TRIA, there is a substantial deductible that must be met, the payment of which could have an adverse effect on its financial condition and results of operations. NLC's deductible under the Program was $1.7 million for 2013 and is estimated to be $1.2 million in 2014. Potential future changes to the TRIA could also adversely affect NLC by causing its reinsurers to increase prices or withdraw from certain markets where terrorism coverage is required. NLC had no terrorism-related losses in 2013.

State insurance regulations. State insurance authorities have broad powers to regulate U.S. insurance companies. The primary purposes of these powers are to promote insurer solvency and to protect individual policyholders. The extent of regulation varies, but generally has its source in statutes that delegate regulatory, supervisory and administrative power to state insurance departments. These powers relate to, among other things, licensing to transact business, accreditation of reinsurers, admittance of assets to statutory surplus, regulating unfair trade and claims practices, establishing actuarial requirements and solvency standards, regulating investments and dividends, and regulating policy forms, related materials and premium rates. State insurance laws and regulations require insurance companies to file financial statements prepared in accordance with accounting principles prescribed by insurance departments in states in which they conduct insurance business, and their operations are subject to examination by those departments.

As part of the broad authority that state insurance commissioners hold, they may impose periodic rules or regulations related to local issues or events. An example is the State of Oklahoma's prohibition on the cancellation of policies for nonpayment of premium in the wake of severe tornadic activity. Due to the extent of damage and displacement of people, inability of mail to reach policyholders and inaccessibility of entire neighborhoods, the State of Oklahoma prohibited insurance companies from canceling or non-renewing policies for a period of time following the specific event.

Periodic financial and market conduct examinations. The insurance departments in every state in which NLC's insurance companies do business may conduct on-site visits and examinations of its insurance companies at any time to review the insurance companies' financial condition, market conduct and relationships and transactions with affiliates. In addition, the Texas Department of Insurance will conduct comprehensive examinations of insurance companies domiciled in Texas every three to five years. Examinations are generally carried out in cooperation with the insurance departments of other licensing states under guidelines promulgated by the NAIC.

The Texas Department of Insurance completed their last examinations of NLIC and ASIC through December 31, 2010 in an examination report dated May 12, 2012. This examination report contained no information of any significant compliance issues and there is no indication of any significant changes to our financial statements as a result of the examination by the domiciliary state.

State dividend limitations. The Texas Department of Insurance must approve any dividend declared or paid by an insurance company domiciled in the state if the dividend, together with all dividends declared or distributed by that insurance company during the preceding twelve months, exceeds the greater of (1) 10% of its policyholders' surplus as of December 31 of the preceding year or (2) 100% of its net income for the preceding calendar year. The greater number is known as the insurer's extraordinary dividend limit. At December 31, 2013, the extraordinary dividend limit for NLIC and ASIC was $9.9 million and $2.6 million, respectively. In addition, NLC's insurance companies may only pay dividends out of their earned surplus.

Statutory accounting principles. Statutory accounting principles, or SAP, are a comprehensive basis of accounting developed to assist insurance regulators in monitoring and regulating the solvency of insurance companies. SAP rules are different from GAAP, and are intended to reflect a more conservative view of the insurer. SAP is primarily concerned with measuring an insurer's surplus to policyholders. Accordingly, SAP focuses on valuing assets and liabilities of insurers at financial reporting dates in accordance with insurance laws and regulatory provisions applicable in each insurer's domiciliary state.

While GAAP is concerned with a company's solvency, it also stresses other financial measurements, such as income and cash flows. Accordingly, GAAP gives more consideration to appropriate matching of revenues and expenses and accounting for management's stewardship of assets than does SAP. As a direct result, different amounts of assets and liabilities will be reflected in financial statements prepared in accordance with GAAP as opposed to SAP. SAP, as established by the NAIC and adopted by Texas regulators, determines the statutory surplus and statutory net income of the NLC insurance companies and, thus, determines the amount they have available to pay dividends.

Guaranty associations. In Texas, and in all of the jurisdictions in which NLIC and ASIC are, or in the future may be, licensed to transact business, there is a requirement that property and casualty insurers doing business within the jurisdiction must participate in guaranty associations, which are organized to pay limited covered benefits owed pursuant to insurance policies issued by impaired, insolvent or failed insurers. These associations levy assessments, up to prescribed limits, on all member insurers in a particular state on the basis of the proportionate share of the premiums written by member insurers in the lines of business in which the impaired, insolvent or failed insurer was engaged. States generally permit member insurers to recover assessments paid through full or partial premium tax offsets.

NLC did not incur any levies in 2013, 2012 or 2011. Property and casualty insurance company insolvencies or failures may, however, result in additional guaranty fund assessments at some future date. At this time NLC is unable to determine the impact, if any, that these assessments may have on its financial condition or results of operations. NLC has established liabilities for guaranty fund assessments with respect to insurers that are currently subject to insolvency proceedings.

National Flood Insurance Program. NLC's insurance subsidiaries voluntarily participate as Write Your Own carriers in the National Flood Insurance Program, or NFIP. The NFIP is administered and regulated by the Federal Emergency Management Agency (FEMA). NLIC and ASIC operates as a fiscal agent of the Federal government in the selling and administering of the Standard Flood Insurance Policy. This involves writing the policy, the collection of premiums and the paying of covered claims. All pricing is set by FEMA and all collections are made by NLIC and ASIC.

NLIC and ASIC cede 100% of the policies written by NLIC and ASIC on the Standard Flood Insurance Policy to FEMA; however, if FEMA were unable to perform, NLIC and ASIC would have a legal obligation to the policyholders. The terms of the reinsurance agreement are standard terms, which require NLIC and ASIC to maintain its rating criteria, determine policyholder eligibility, issue policies on NLIC and ASIC's paper, endorse and cancel policies, collect from insureds and process claims. NLIC and ASIC receive ceding commissions from NFIP for underwriting administration, claims management, commission and adjuster fees.

Participation in involuntary risk plans. NLC's insurance companies are required to participate in residual market or involuntary risk plans in various states where they are licensed that provide insurance to individuals or entities that otherwise would be unable to purchase coverage from private insurers. If these plans experience losses in excess of their capitalization, they may assess participating insurers for proportionate shares of their financial deficit. These plans include the Georgia Underwriting Association, Texas FAIR Plan Association, Texas Windstorm Insurance Agency, or TWIA, the Louisiana Citizens Property Insurance Corporation, the Mississippi Residential Property Insurance Underwriting Association and the Mississippi Windstorm Underwriting Association. For example in 2005, following Hurricanes Katrina and Rita, the above plans levied collective assessments totaling $10.4 million on NLC's insurance subsidiaries. Additional assessments, including emergency assessments, may follow. In some of these instances, NLC's insurance companies should be able to recover these assessments through policyholder surcharges, higher rates or reinsurance. The ultimate impact hurricanes have on the Texas and Louisiana facilities is currently uncertain and future assessments can occur whenever the involuntary facilities experience financial deficits.

Other. Insurance activities are subject to state insurance laws and regulations as determined by the particular insurance commissioner for each state in accordance with the McCarran-Ferguson Act, as well as subject to the Gramm-Leach-Bliley Act and the privacy regulations promulgated by the Federal Trade Commission.

Changes in any of the laws governing our conduct could have an adverse impact on our ability to conduct our business or could materially affect our financial position, operating income, expense or cash flow.

First Southwest

FSC is a broker-dealer registered with the SEC, FINRA, all 50 U.S. states, the District of Columbia and Puerto Rico. Much of the regulation of broker-dealers, however, has been delegated to self-regulatory organizations, principally FINRA, the Municipal Securities Rulemaking Board and national securities exchanges. These self-regulatory organizations adopt rules (which are subject to approval by the SEC) for governing its members and the industry. Broker-dealers are also subject to the laws and rules of the states in which a broker-dealer conducts business. FSC is a member of, and is primarily subject to regulation, supervision and regular examination by, FINRA.

The regulations to which broker-dealers are subject cover all aspects of the securities business, including, but not limited to, sales and trade practices, capital structure, record keeping and reporting procedures, relationships and conflicts with customers, the handling of cash and margin accounts, and the conduct of registered persons, directors, officers and employees. Broker-dealers are also subject to the privacy and anti-money laundering laws and regulations discussed previously. Additional legislation, changes in rules promulgated by the SEC and by self-regulatory organizations or changes in the interpretation or enforcement of existing laws and rules often directly affects the method of operation and profitability of broker-dealers. The SEC, the self-regulatory organizations and states may conduct administrative and enforcement proceedings that can result in censure, fine, suspension or expulsion of a broker-dealer, its registered persons, officers or employees. The principal purpose of regulation and discipline of broker-dealers is the protection of customers and the securities markets rather than protection of creditors and stockholders of broker-dealers.

Limitation on Businesses. The businesses that FSC may conduct are limited by its agreements with, and its oversight by, FINRA and by federal and state law. Participation in new business lines, including trading of new products or participation on new exchanges or in new countries often requires governmental and/or exchange approvals, which may take significant time and resources. In addition, FSC is an operating subsidiary of the Bank, which means its activities are further limited by those that are permissible for the Bank. As a result, FSC may be prevented from entering new businesses that may be profitable in a timely manner, if at all.

Net Capital Requirements. The SEC, FINRA and various other regulatory authorities have stringent rules and regulations with respect to the maintenance of specific levels of net capital by regulated entities. Rule 15c3-1 of the Exchange Act (the "Net Capital Rule") requires that a broker-dealer maintain minimum net capital. Generally, a broker-dealer's net capital is net worth plus qualified subordinated debt less deductions for non-allowable (or non-liquid) assets and other adjustments and operational charges. At December 31, 2013, FSC was in compliance with applicable net capital requirements.

The SEC and FINRA impose rules that require notification when net capital falls below certain predefined criteria. These rules also dictate the ratio of debt-to-equity in the regulatory capital composition of a broker-dealer, and constrain the ability of a broker-dealer to expand its business under certain circumstances. If a broker-dealer fails to maintain the required net capital, it may be subject to suspension or revocation of registration by the SEC or applicable regulatory authorities, and suspension or expulsion by these regulators could ultimately lead to the broker-dealer's liquidation. Additionally, the Net Capital Rule and certain FINRA rules impose requirements that may have the effect of prohibiting a broker-dealer from distributing or withdrawing capital and requiring prior notice to, and approval from, the SEC and FINRA for certain capital withdrawals.

Securities Investor Protection Corporation. FSC is required by federal law to belong to SIPC, whose primary function is to provide financial protection for the customers of failing brokerage firms. SIPC provides protection for customers up to $500,000, of which a maximum of $250,000 may be in cash.

Changing Regulatory Environment. The regulatory environment in which FSC operates is subject to frequent change. Its business, financial condition and operating results may be adversely affected as a result of new or revised legislation or regulations imposed by the U.S. Congress, the SEC or other U.S. and state governmental regulatory authorities, or FINRA. FSC's business, financial condition and operating results also may be adversely affected by changes in the interpretation and enforcement of existing laws and rules by these governmental and regulatory authorities. In the current era of heightened regulation of financial institutions, FSC can expect to incur increasing compliance costs, along with the industry as a whole.

Properties

Hilltop leases office space for its principal executive offices in Dallas, Texas. In addition to its principal office, Hilltop's various business segments conduct business at various locations.

Banking. At June 30, 2014, Hilltop's banking segment conducted business at 86 locations throughout Texas, including seven support facilities. Hilltop's banking segment's principal executive offices are located in Dallas, Texas, in space leased by PlainsCapital. Hilltop leases 29 banking locations including its principal offices and owns the remaining 57 banking locations. Hilltop has options to renew leases at most locations.

Mortgage Origination. Hilltop's mortgage origination segment is headquartered in Dallas, Texas and at June 30, 2014 conducted business from approximately 300 locations in 42 states. Each of these locations is leased by PrimeLending.

Insurance. At June 30, 2014, Hilltop's insurance segment leases office space in Waco, Texas for all corporate, claims, customer service and data center operations.

Financial Advisory. Hilltop's financial advisory segment is headquartered in Dallas, Texas and at June 30, 2014 conducted business at 25 locations in 14 states. Each of these offices is leased by First Southwest.

Legal Proceedings

On August 20, 2014, PrimeLending received a Civil Investigative Demand from the United States Department of Justice (the "DOJ") related to the Inquiry being conducted by the Office of Inspector General of the U.S. Department of Housing and Urban Development regarding mortgage-related practices. According to the Civil Investigative Demand, the DOJ is conducting an investigation to determine whether PrimeLending has violated the False Claims Act in connection with originating and underwriting single-family residential mortgage loans insured by the Federal Housing Administration (FHA). PrimeLending is cooperating with this investigation and continues to respond to the Civil Investigative Demand.

For a description of other material pending legal proceedings relating to Hilltop's business, see the discussion set forth under the heading "Legal Matters" in Note 18 to Hilltop's audited consolidated financial statements included in this proxy statement/prospectus and Note 11 to Hilltop's unaudited consolidated financial statements also included in this proxy statement/prospectus. See also "The Merger Litigation Relating to the Merger."

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

Securities, Stockholder and Dividend Information

Our common stock is listed on the New York Stock Exchange under the symbol "HTH". Our common stock has no public trading history prior to February 12, 2004. Our common stock closed at $19.76 per share on October 13, 2014 and at $23.79 per share on March 31, 2014, the date immediately prior to the public announcement of the merger. At October 13, 2014, there were 90,182,915 shares of our common stock outstanding with 526 stockholders of record.

In connection with the PlainsCapital Merger, on November 29, 2012, we filed with the State Department of Assessments and Taxation of the State of Maryland articles supplementary for the Series B Preferred Stock, setting forth its terms. Holders of the Series B Preferred Stock are entitled to noncumulative cash dividends at a fluctuating dividend rate based on the Bank's level of qualified small business lending. The Series B Preferred Stock is non-voting, except in limited circumstances, and ranks senior to our common stock with respect to the payment of dividends and distribution of assets upon any liquidation, dissolution or winding up of Hilltop.

Subject to the restrictions discussed below, our stockholders are entitled to receive dividends when, as, and if declared by our board of directors out of funds legally available for that purpose. Our board of directors exercises discretion with respect to whether we will pay dividends and the amount of such dividend, if any. Factors that affect our ability to pay dividends on our common stock in the future include, without limitation, our earnings and financial condition, liquidity and capital resources, the general economic and regulatory climate, our ability to service any equity or debt obligations senior to our common stock and other factors deemed relevant by our board of directors. We have not declared or paid any dividends over the past two completed fiscal years.

As a holding company, we are ultimately dependent upon our subsidiaries to provide funding for our operating expenses, debt service and dividends. Various laws limit the payment of dividends and other distributions by our subsidiaries to us, and may therefore limit our ability to pay dividends on our common stock. In addition, as long as shares of Series B Preferred Stock remain outstanding, we may not pay dividends to our common stockholders (nor may we repurchase or redeem any shares of our common stock) during any quarter in which we fail to declare and pay dividends on the Series B Preferred Stock and for the next three quarters following such failure. In addition, under the terms of the Series B Preferred Stock, we may only declare and pay dividends on our common stock (or repurchase shares of our common stock), if, after payment of such dividend, the dollar amount of our Tier 1 capital would be at least ninety percent (90%) of Tier 1 capital as of September 27, 2011, excluding any charge-offs and redemptions of the Series B Preferred Stock.

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If required payments on our outstanding junior subordinated debentures held by our unconsolidated subsidiary trusts are not made or suspended, we may be prohibited from paying dividends on our common stock. Regulatory authorities could impose administratively stricter limitations on the ability of our subsidiaries to pay dividends to us if such limits were deemed appropriate to preserve certain capital adequacy requirements. See " Management's Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources Restrictions on Dividends and Distributions."

The high and low sales prices per quarter for Hilltop's common stock during 2014, 2013 and 2012 are included in the section of this proxy statement/prospectus entitled "Comparative Market Prices and Dividends."

Securities Authorized for Issuance under Equity Compensation Plans

The following table sets forth information at December 31, 2013 with respect to compensation plans under which shares of our common stock may be issued. Additional information concerning our stock-based compensation plans is presented in Note 20, Stock-Based Compensation, in the notes to our audited consolidated financial statements included in this proxy statement/prospectus.

Equity Compensation Plan Information

Plan Category	**Number of securities to be issued upon exercise of outstanding options, warrants and rights**	**Weighted-average exercise price of outstanding options, warrants and rights**	**Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in first column)**
Equity compensation plans approved by security holders*	600,000	$ 7.70	3,519,657
Total	600,000	$ 7.70	3,519,657

* Excludes shares of restricted stock granted under the 2003 equity incentive plan (the "2003 Plan"), as all such shares are vested. No exercise price is required to be paid upon the vesting of the restricted shares of common stock granted. In September 2012, our stockholders approved the Hilltop Holdings Inc. 2012 Equity Incentive Plan (the "2012 Plan"), which allows for the granting of nonqualified stock options, stock appreciation rights, restricted stock, restricted stock units, performance awards, dividend equivalent rights and other awards to employees of Hilltop, its subsidiaries and outside directors of Hilltop. Upon the effectiveness of the 2012 Plan, no additional awards are permissible under the 2003 Plan. In the aggregate, 4,000,000 shares of common stock may be delivered pursuant to awards granted under the 2012 Plan. At December 31, 2013, 480,343 awards had been granted pursuant to the 2012 Plan. All shares outstanding under the 2003 Plan and the 2012 Plan, whether vested or unvested, are entitled to receive dividends and to vote, unless forfeited. No participant in our 2012 Plan may be granted awards in any fiscal year covering more than 1,250,000 shares of our common stock.

Issuer Repurchases of Equity Securities

There were no repurchases of shares of common stock by Hilltop during the six months ended June 30, 2014 or the twelve months ended December 31, 2013.

Recent Sales of Unregistered Securities

On January 17, 2014, April 17, 2014 and July 14, 2014 Hilltop issued an aggregate of 2,303, 2,708 and 2,216 shares of common stock under the Hilltop Holdings 2012 Equity Incentive Plan to certain non-employee directors as compensation for their service on Hilltop's Board of Directors during the

fourth quarter of 2013 and first and second quarters of 2014, respectively. The shares were issued pursuant to the exemption from registration under Section 4(a)(2) of the Securities Act.

Selected Financial Data

See "Selected Historical Consolidated Financial Data for Hilltop" beginning on page 11 of this proxy statement/prospectus.

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

The following discussion is intended to help the reader understand Hilltop's results of operations and financial condition and is provided as a supplement to, and should be read in conjunction with, Hilltop's unaudited and audited consolidated financial statements and the accompanying notes thereto commencing on page F-1. In addition to historical financial information, the following discussion and analysis contains forward-looking statements that involve risks, uncertainties and assumptions. Hilltop's results and the timing of selected events may differ materially from those anticipated in these forward-looking statements as a result of many factors, including those discussed under "Risk Factors" and elsewhere in this proxy statement/prospectus. See "Forward-Looking Statements." All dollar amounts in the following discussion are in thousands, except per share amounts.

OVERVIEW

Beginning in 1995, we operated as several companies under the name "Affordable Residential Communities" or "ARC," now known as Hilltop Holdings Inc., a Maryland corporation. We engaged in the business of acquiring, renovating, repositioning and operating manufactured home communities, as well as certain related businesses.

In January 2007, we acquired NLC. NLC owns National Lloyds Insurance Company, or NLIC, and American Summit Insurance Company, or ASIC, both of which are licensed property and casualty insurers operating in multiple states. In addition, NLC also owns NALICO GA, a general agency that operates in Texas. NLIC commenced business in 1949 and currently operates in 14 states, with its largest market being the state of Texas. NLIC carries a financial strength rating of "A" (Excellent) by A.M. Best. ASIC was formed in 1955 and currently operates in 13 states, its largest market being the state of Arizona. ASIC carries a financial strength rating of "A" (Excellent) by A.M. Best. Both of these companies are regulated by the Texas Department of Insurance.

On July 31, 2007, we sold substantially all of the operating assets used in our manufactured home communities business and our retail sales and financing business to American Residential Communities LLC. We received gross proceeds of approximately $890 million in cash, which represents the aggregate purchase price of $1.8 billion, less the indebtedness assumed by the buyer. After giving effect to expenses, taxes and our preferred stock and senior notes that remained outstanding following the sale, our net cash balance was approximately $550 million. As a result of the sale, our primary operations through November 2012 were limited to providing fire and homeowners insurance to low value dwellings and manufactured homes primarily in Texas and other areas of the southern United States through NLC.

On November 30, 2012, we acquired PlainsCapital Corporation in a stock and cash transaction, whereby PlainsCapital Corporation merged with and into our wholly owned subsidiary, which continued as the surviving entity under the name "PlainsCapital Corporation" (the "PlainsCapital Merger"). Based on Hilltop's closing stock price on November 30, 2012, the total purchase price was $813.5 million, consisting of 27.1 million shares of common stock, $311.8 million in cash and the issuance of 114,068 shares of Hilltop Non-Cumulative Perpetual Preferred Stock, Series B ("Hilltop Series B Preferred Stock"). The fair value of assets acquired, excluding goodwill, totaled $6.5 billion, including $3.2 billion of loans, $730.8 million of investment securities and $70.7 million of identifiable intangibles. The fair value of the liabilities assumed was $5.9 billion, including $4.5 billion of deposits.

Concurrent with the consummation of the PlainsCapital Merger, we became a financial holding company registered under the Bank Holding Company Act of 1956, as amended by the Gramm-Leach-Bliley Act of 1999.

On September 13, 2013 (the "Bank Closing Date"), the Bank assumed substantially all of the liabilities, including all of the deposits, and acquired substantially all of the assets of Edinburg, Texas-based FNB from the Federal Deposit Insurance Corporation (the "FDIC"), as receiver, and reopened former branches of FNB acquired from the FDIC under the "PlainsCapital Bank" name (the "FNB Transaction"). Pursuant to the Purchase and Assumption Agreement by and among the FDIC as receiver for FNB, the FDIC and the Bank (the "P&A Agreement"), the Bank and the FDIC entered into loss-share agreements whereby the FDIC agreed to share in the losses of certain covered loans and covered other real estate owned ("OREO") that the Bank acquired in the FNB Transaction. The fair value of the assets acquired was $2.2 billion, including $1.1 billion in covered loans, $286.2 million in securities, $135.2 million in covered OREO and $42.9 million in non-covered loans. The Bank also assumed $2.2 billion in liabilities, consisting primarily of deposits.

Following the PlainsCapital Merger, our primary line of business has been to provide business and consumer banking services from offices located throughout central, north and west Texas through the Bank. Further, the acquisition of FNB's expansive branch network allows the Bank to further develop its Texas footprint through expansion into the Rio Grande Valley, Houston, Corpus Christi, Laredo and El Paso markets, among others. In addition to the Bank, our other subsidiaries have specialized areas of expertise that allow us to provide an array of financial products and services such as mortgage origination, insurance and financial advisory services.

On March 31, 2014, we entered into a definitive merger agreement with SWS providing for the merger of SWS with and into a subsidiary of Hilltop formed for the purpose of facilitating this transaction (see "The Merger Agreement" included elsewhere in this proxy statement/prospectus). Under the terms of the merger agreement, SWS stockholders will receive per share consideration of 0.2496 shares of Hilltop common stock and $1.94 of cash, equating to $7.25 per share based on Hilltop's closing price on June 30, 2014. The value of the merger consideration will fluctuate with the market price of Hilltop common stock. We intend to fund the cash portion of the consideration through available cash. The merger is subject to customary closing conditions, including regulatory approvals and approval of the stockholders of SWS, and is expected to be completed prior to the end of 2014.

At June 30, 2014, on a consolidated basis, we had total assets of $9.4 billion, total deposits of $6.2 billion, total loans, including loans held for sale, of $6.0 billion and stockholders' equity of $1.4 billion. At December 31, 2013, on a consolidated basis, we had total assets of $8.9 billion, total deposits of $6.7 billion, total loans, including loans held for sale, of $5.6 billion and stockholders' equity of $1.3 billion. Our operating results beginning December 1, 2012 include the banking, mortgage origination and financial advisory operations acquired in the PlainsCapital Merger. Accordingly, our operating results and financial condition for the year ended December 31, 2013 are not comparable to prior years. Additionally, the presentation of our historical consolidated financial statements for 2011 has been modified and certain items have been reclassified to conform to the 2012 and 2013 presentation, which is more consistent with that of a financial institution that provides an array of financial products and services. Our banking operations include the operations acquired in the FNB Transaction since September 14, 2013.

Segment Information

We have two primary operating business units, PlainsCapital (financial services and products) and NLC (insurance). Within the PlainsCapital unit are three primary wholly owned operating subsidiaries: the Bank, PrimeLending and First Southwest. Under accounting principles generally accepted in the United States ("GAAP"), our business units are comprised of four reportable business segments organized primarily by the core products offered to the segments' respective customers: banking, mortgage origination, insurance and financial advisory. During the fourth quarter of 2013, we began presenting certain amounts previously allocated to the four reportable business segments under the heading Corporate to better reflect our internal organizational structure. This change had no impact on our consolidated results of operations. Our historical segment disclosures and Management's Discussion and Analysis of Financial Condition and Results of Operations have been revised to conform to the current presentation. Consistent with the segment operating results during 2013, we anticipate that future revenues will be driven primarily from the banking segment, with the remainder being generated by our mortgage origination, insurance and financial advisory segments. Based on historical results of PlainsCapital Corporation, which we acquired on November 30, 2012, the relative share of total revenue provided by our banking and mortgage origination segments fluctuates depending on market conditions, and operating results for the mortgage origination segment tend to be more volatile than operating results for the banking segment.

The banking segment includes the operations of the Bank and, since September 14, 2013, the operations acquired in the FNB Transaction. The banking segment primarily provides business and consumer banking products and services from offices located throughout Texas and generates revenue from its portfolio of earning assets. The Bank's results of operations are primarily dependent on net interest income, while also deriving revenue from other sources, including service charges on customer deposit accounts and trust fees.

The mortgage origination segment includes the operations of PrimeLending, which offers a variety of loan products from offices in 42 states and generates revenue predominantly from fees charged on the origination of loans and from selling these loans in the secondary market.

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

The financial advisory segment generates a majority of its revenues from fees and commissions earned from investment advisory and securities brokerage services at First Southwest. The principal subsidiaries of First Southwest are FSC, a broker-dealer registered with the SEC and Financial Industry Regulatory Authority, and a member of the New York Stock Exchange, and First Southwest Asset Management, Inc., a registered investment advisor under the Investment Advisors Act of 1940. FSC holds trading securities to support sales, underwriting and other customer activities. These securities are marked to market through other noninterest income. FSC uses derivatives to support mortgage origination programs of certain non-profit housing organization clients. FSC hedges its related exposure to interest rate risk from these programs with U.S. Agency to-be-announced, or TBA, mortgage-backed securities. These derivatives are marked to market through other noninterest income.

Corporate includes certain activities not allocated to specific business segments. These activities include holding company financing and investing activities, and management and administrative services to support the overall operations of the Company including, but not limited to, certain executive management, corporate relations, legal, finance, and acquisition costs not allocated to business segments. Balance sheet amounts for remaining subsidiaries not discussed previously and the elimination of intercompany transactions are included in "All Other and Eliminations."

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Additional information concerning our reportable segments is presented in Note 30, Segment and Related Information, in the notes to our audited consolidated financial statements included in this proxy statement/prospectus and Note 20 of our unaudited consolidated financial statements also included in this proxy statement/prospectus. The following tables present certain information about the operating results of Hilltop's reportable segments (in thousands).

Three Months Ended June 30, 2014	Banking	Mortgage Origination	Insurance	Financial Advisory	Corporate	All Other and Eliminations	Hilltop Consolidated
Net interest income (expense)	$ 90,828	$ (2,389)	$ 838	$ 3,178	$ 1,695	$ 4,296	$ 98,446
Provision for loan losses	5,516			17			5,533
Noninterest income	16,392	122,820	43,123	25,838		(4,892)	203,281
Noninterest expense	60,240	111,224	49,420	28,359	2,565	(596)	251,212
Income (loss) before income taxes	$ 41,464	$ 9,207	$ (5,459)	$ 640	$ (870)	$	$ 44,982

Six Months Ended June 30, 2014	Banking	Mortgage Origination	Insurance	Financial Advisory	Corporate	All Other and Eliminations	Hilltop Consolidated
Net interest income (expense)	$ 170,401	$ (6,528)	$ 1,817	$ 5,808	$ 3,387	$ 8,982	$ 183,867
Provision for loan losses	8,744			31			8,775
Noninterest income	32,621	214,583	85,896	50,435		(10,154)	373,381
Noninterest expense	120,917	201,857	81,762	55,724	4,753	(1,172)	463,841
Income (loss) before income taxes	$ 73,361	$ 6,198	$ 5,951	$ 488	$ (1,366)	$	$ 84,632

Three Months Ended June 30, 2013	Banking	Mortgage Origination	Insurance	Financial Advisory	Corporate	All Other and Eliminations	Hilltop Consolidated
Net interest income (expense)	$ 68,597	$ (11,847)	$ 873	$ 3,511	$ (105)	$ 7,396	$ 68,425
Provision for loan losses	11,300			(11)			11,289
Noninterest income	11,928	165,257	40,777	28,863		(7,592)	239,233
Noninterest expense	31,919	134,487	62,144	30,373	1,673	(196)	260,400
Income (loss) before income taxes	$ 37,306	$ 18,923	$ (20,494)	$ 2,012	$ (1,778)	$	$ 35,969

Six Months Ended June 30, 2013	Banking	Mortgage Origination	Insurance	Financial Advisory	Corporate	All Other and Eliminations	Hilltop Consolidated
Net interest income (expense)	$ 136,268	$ (23,850)	$ 1,886	$ 6,754	$ (236)	$ 14,864	$ 135,686
Provision for loan losses	24,266			28			24,294

Noninterest income	24,132	311,785	80,202	51,641		(15,249)	452,511
Noninterest expense	62,599	256,758	96,410	56,099	3,910	(385)	475,391
Income (loss) before income taxes	$ 73,535	$ 31,177	$ (14,322)	$ 2,268	$ (4,146)	$	$ 88,512

Year Ended December 31, 2013	**Banking**	**Mortgage Origination**	**Insurance**	**Financial Advisory**	**Corporate**	**All Other and Eliminations**	**Hilltop Consolidated**
Net interest income (expense)	$ 293,254	$ (37,840)	$ 7,442	$ 12,064	$ (1,597)	$ 22,878	$ 296,201
Provision for loan losses	37,140			18			37,158
Noninterest income	71,045	537,497	166,163	102,714		(27,334)	850,085
Noninterest expense	155,102	472,284	166,006	112,360	10,439	(4,456)	911,735
Income (loss) before income taxes	$ 172,057	$ 27,373	$ 7,599	$ 2,400	$ (12,036)	$	$ 197,393

Year Ended December 31, 2012	**Banking**	**Mortgage Origination**	**Insurance**	**Financial Advisory**	**Corporate**	**All Other and Eliminations**	**Hilltop Consolidated**
Net interest income (expense)	$ 24,885	$ (4,987)	$ 4,730	$ 1,191	$ 39	$ 2,984	$ 28,842
Provision for loan losses	3,670			130			3,800
Noninterest income	4,601	57,618	154,147	10,909		(3,043)	224,232
Noninterest expense	16,130	50,296	163,585	11,078	14,487	(59)	255,517
Income (loss) before income taxes	$ 9,686	$ 2,335	$ (4,708)	$ 892	$ (14,448)	$	$ (6,243)

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Year Ended December 31, 2011	Banking	Mortgage Origination	Insurance	Financial Advisory	Corporate	All Other and Eliminations	Hilltop Consolidated
Net interest income (expense)	$	$	$ 4,915	$	$ (2,851)	$	$ 2,064
Provision for loan losses							
Noninterest income			141,650				141,650
Noninterest expense			146,386		8,868		155,254
Income (loss) before income taxes	$	$	$ 179	$	$ (11,719)	$	$ (11,540)

How We Generate Revenue

We generate revenue from net interest income and from noninterest income. Net interest income represents the difference between the income earned on our assets, including our loans and investment securities, and our cost of funds, including the interest paid on the deposits and borrowings that are used to support our assets. Net interest income is a significant contributor to our operating results. Fluctuations in interest rates, as well as the amounts and types of interest-earning assets and interest-bearing liabilities we hold, affect net interest income. We generated $183.9 million in net interest income during the six months ended June 30, 2014, compared with net interest income of $135.7 million during the same period in 2013. The year-over-year increase in net interest income was primarily due to the inclusion of those operations acquired as a part of the FNB Transaction within our banking segment. We generated $296.2 million in net interest income during the year ended December 31, 2013, compared with net interest income of $28.8 million in 2012 and net interest income of $2.1 million in 2011. The significant year-over-year increases in net interest income were primarily due to $267.5 million and $21.1 million in net interest income during the year ended December 31, 2013 and the month ended December 31, 2012, respectively, generated by those operations acquired as part of the PlainsCapital Merger.

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

(i) *Income from mortgage operations.* Through our wholly owned subsidiary, PrimeLending, we generate noninterest income by originating and selling mortgage loans. During the six months ended June 30, 2014 and 2013, we generated $214.5 million and $311.7 million, respectively, in net gains from the sale of loans, other mortgage production income (including income associated with retained mortgage servicing rights), and mortgage loan origination fees. During the year ended December 31, 2013, we generated $537.3 million in net gains from the sale of loans, other mortgage production income (including income associated with retained mortgage servicing rights), and mortgage loan origination fees, compared with $57.6 million during the month ended December 31, 2012.

(ii) *Net insurance premiums earned.* Through our wholly owned insurance subsidiary, NLC, we provide fire and limited homeowners insurance for low value dwellings and manufactured homes. We generated $81.1 million in net insurance premiums earned during the six months ended June 30, 2014, compared with $76.1 million during the same period in the prior year. We generated $157.5 million, $146.7 million and $134.0 million in net insurance premiums earned during 2013, 2012 and 2011, respectively.

(iii) *Investment advisory fees and commissions and securities brokerage fees and commissions.* Through our wholly owned subsidiary, First Southwest, we provide public finance advisory and various investment banking and brokerage services. We generated $43.6 million and $48.0 million in investment advisory fees and commissions and securities brokerage fees and commissions during the six months ended June 30, 2014 and 2013, respectively. We generated $93.1 million in investment advisory fees and commissions and securities brokerage fees and commissions during the year ended December 31, 2013, compared with $11.2 million during the month ended December 31, 2012.

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In the aggregate, we generated $373.4 million and $452.5 million in noninterest income during the six months ended June 30, 2014 and 2013, respectively. The significant year-over-year decrease in noninterest income was primarily due to the decrease in loan origination volume within our mortgage origination segment, partially offset by increases in noninterest income in our banking and insurance segments. In the aggregate, we generated $850.1 million, $224.2 million and $141.7 million in noninterest income during 2013, 2012 and 2011, respectively. The significant year-over-year increases in noninterest income during 2013 and 2012 were primarily due to the inclusion of the mortgage origination and financial advisory operations that we acquired as a part of the PlainsCapital Merger.

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

Three and Six Months ended June 30, 2014 and 2013

Consolidated Operating Results

Net income applicable to common stockholders for the three months ended June 30, 2014 was $27.1 million, or $0.30 per diluted share, compared to net income applicable to common stockholders of $20.9 million, or $0.24 per diluted share, for the three months ended June 30, 2013. Net income applicable to common stockholders for the six months ended June 30, 2014 was $50.8 million, or $0.56 per diluted share, compared to net income applicable to common stockholders of $53.3 million, or $0.61 per diluted share, for the six months ended June 30, 2013.

Certain items included in net income for 2013 and 2014 resulted from purchase accounting associated with the merger of PlainsCapital Corporation with and into a wholly owned subsidiary of Hilltop on November 30, 2012 (the "PlainsCapital Merger") and the FNB Transaction. Income before taxes for the three months ended June 30, 2014 includes net accretion of $17.0 million and $10.4 million on earning assets and liabilities acquired in the PlainsCapital Merger and FNB Transaction, respectively, offset by amortization of identifiable intangibles of $2.3 million and $0.3 million, respectively. During the three months ended June 30, 2013, income before taxes includes net accretion of $15.9 million on earning assets and liabilities acquired in the PlainsCapital Merger, offset by amortization of identifiable intangibles of $2.5 million. Income before taxes for the six months ended June 30, 2014 includes net accretion of $27.0 million and $19.9 million on earning assets and liabilities acquired in the PlainsCapital Merger and FNB Transaction, respectively, offset by amortization of identifiable intangibles of $4.6 million and $0.5 million, respectively. During the six months ended June 30, 2013, income before taxes includes net accretion of $31.9 million on earning assets and liabilities acquired in the PlainsCapital Merger, offset by amortization of identifiable intangibles of $4.9 million.

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

	Three Months Ended June 30,		Six Months Ended June 30,		Year Ended
	2014	2013	2014	2013	December 31, 2013
Performance Ratios:					
Return on average stockholders' equity	7.99%	7.29%	7.82%	9.46%	10.48%
Return on average assets	1.24%	1.24%	1.19%	1.58%	1.66%
Net interest margin (taxable equivalent)(1)	5.18%	4.33%	4.90%	4.34%	4.47%

(1) Taxable equivalent net interest income divided by average interest-earning assets.

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During the three months ended June 30, 2014, the consolidated taxable equivalent net interest margin of 5.18% was impacted by PlainsCapital Merger related accretion of discount on loans of $17.8 million, amortization of premium on acquired securities of $1.0 million and amortization of premium on acquired time deposits of $0.2 million. Additionally, FNB Transaction related accretion of discount on loans of $8.1 million and amortization of premium on acquired time deposits of $2.3 million also impacted the consolidated taxable equivalent net interest margin during the three months ended June 30, 2014. These items increased the consolidated taxable equivalent net interest margin by 140 basis points for the three months ended June 30, 2014. The consolidated taxable equivalent net interest margin was 4.33% for the three months ended June 30, 2013. The taxable equivalent net interest margin for the second quarter of 2013 was impacted by PlainsCapital Merger related accretion of discount on loans of $16.7 million, amortization of premium on acquired securities of $1.4 million and amortization of premium on acquired time deposits of $0.6 million. These items increased the consolidated taxable equivalent interest margin by 98 basis points for the three months ended June 30, 2013.

During the six months ended June 30, 2014, the consolidated taxable equivalent net interest margin of 4.90% was impacted by PlainsCapital Merger related accretion of discount on loans of $28.6 million, amortization of premium on acquired securities of $1.9 million and amortization of premium on acquired time deposits of $0.3 million. Additionally, FNB Transaction related accretion of discount on loans of $15.3 million and amortization of premium on acquired time deposits of $4.6 million also impacted the consolidated taxable equivalent net interest margin during the six months ended June 30, 2014. These items increased the consolidated taxable equivalent net interest margin by 121 basis points for the six months ended June 30, 2014. The consolidated taxable equivalent net interest margin was 4.34% for the six months ended June 30, 2013. The taxable equivalent net interest margin for the six months ended June 30, 2013 was impacted by PlainsCapital Merger related accretion of discount on loans of $33.6 million, amortization of premium on acquired securities of $3.4 million and amortization of premium on acquired time deposits of $1.7 million. These items increased the consolidated taxable equivalent interest margin by 97 basis points for the six months ended June 30, 2013.

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

	Three Months Ended June 30,					
	2014			2013		
	Average Outstanding Balance	Interest Earned or Paid	Annualized Yield or Rate	Average Outstanding Balance	Interest Earned or Paid	Annualized Yield or Rate
Assets						
Interest-earning assets						
Loans, gross(1)	$ 5,526,869	$ 92,204	6.63%	$ 4,352,489	$ 65,213	5.95%
Investment securities taxable	1,144,269	7,618	2.66%	996,624	6,480	2.60%
Investment securities non-taxable(2)	185,533	1,772	3.82%	201,383	1,772	3.52%
Federal funds sold and securities purchased under agreements to resell	20,308	14	0.28%	34,594	35	0.40%
Interest-bearing deposits in other financial institutions	575,653	317	0.22%	581,676	242	0.25%
Other	218,413	3,068	5.62%	164,754	3,009	7.31%
Interest-earning assets, gross	7,671,045	104,993	5.44%	6,331,520	76,751	4.82%
Allowance for loan losses	(38,909)			(20,588)		
Interest-earning assets, net	7,632,136			6,310,932		
Noninterest-earning assets	1,304,522			818,914		
Total assets	$ 8,936,658			$ 7,129,846		
Liabilities and Stockholders' Equity						
Interest-bearing liabilities						
Interest-bearing deposits	$ 4,523,194	$ 3,096	0.27%	$ 3,379,302	$ 3,406	0.40%
Notes payable and other borrowings	966,143	2,866	1.18%	1,044,784	4,337	1.66%
Total interest-bearing liabilities	5,489,337	5,962	0.43%	4,424,086	7,743	0.70%
Noninterest-bearing liabilities						
Noninterest-bearing deposits	1,761,194			1,179,264		
Other liabilities	307,846			341,929		
Total liabilities	7,558,377			5,945,279		
Stockholders' equity	1,377,769			1,183,830		
Noncontrolling interest	512			737		
Total liabilities and stockholders' equity	$ 8,936,658			$ 7,129,846		
Net interest income(2)		$ 99,031			$ 69,008	

Net interest spread(2)	5.01%	4.12%
Net interest margin(2)	5.18%	4.33%

	Six Months Ended June 30,					
	2014			2013		
	Average Outstanding Balance	Interest Earned or Paid	Annualized Yield or Rate	Average Outstanding Balance	Interest Earned or Paid	Annualized Yield or Rate
Assets						
Interest-earning assets						
Loans, gross(1)	$ 5,299,145	$ 171,948	6.47%	$ 4,280,580	$ 130,099	6.06%
Investment securities taxable	1,133,315	15,206	2.69%	948,789	12,392	2.61%
Investment securities non-taxable(2)	184,345	3,633	3.94%	209,816	3,794	3.62%
Federal funds sold and securities purchased under agreements to resell	23,305	33	0.28%	22,462	56	0.50%
Interest-bearing deposits in other financial institutions	770,206	912	0.24%	664,002	575	0.25%
Other	203,428	5,708	5.64%	159,685	5,114	6.45%
Interest-earning assets, gross	7,613,744	197,440	5.17%	6,285,334	152,030	4.83%
Allowance for loan losses	(37,891)			(13,720)		
Interest-earning assets, net	7,575,853			6,271,614		
Noninterest-earning assets	1,336,127			845,500		
Total assets	$ 8,911,980			$ 7,117,114		
Liabilities and Stockholders' Equity						
Interest-bearing liabilities						
Interest-bearing deposits	$ 4,735,026	$ 6,855	0.29%	$ 3,468,202	$ 6,856	0.40%
Notes payable and other borrowings	815,942	5,514	1.35%	948,138	8,230	1.74%
Total interest-bearing liabilities	5,550,968	12,369	0.45%	4,416,340	15,086	0.69%
Noninterest-bearing liabilities						
Noninterest-bearing deposits	1,741,409			1,184,990		
Other liabilities	264,504			343,915		
Total liabilities	7,556,881			5,945,245		
Stockholders' equity	1,354,635			1,171,132		
Noncontrolling interest	464			737		
Total liabilities and stockholders' equity	$ 8,911,980			$ 7,117,114		
Net interest income(2)		$ 185,071			$ 136,944	

Net interest spread(2)	4.72%	4.14%
Net interest margin(2)	4.90%	4.34%

(1) Average balance includes non-accrual loans.

(2) Annualized taxable equivalent adjustments are based on a 35% tax rate. The adjustment to interest income was $0.6 million for each of the three months ended June 30, 2014 and 2013, respectively, and $1.2 million and $1.3 million for the six months ended June 30, 2014 and 2013, respectively.

On a consolidated basis, net interest income increased $30.0 million and $48.2 million during the three and six months ended June 30, 2014, compared with the same periods in 2013. These increases were primarily due to the inclusion of those operations acquired as a part of the FNB Transaction within our banking segment.

The provision for loan losses is determined by management as the amount to be added to the allowance for loan losses after net charge-offs have been deducted to bring the allowance to a level which, in management's best estimate, is necessary to absorb probable losses within the existing loan portfolio. The consolidated provision for loan losses, primarily in the banking segment, was $5.5 million and $11.3 million during the three months ended June 30, 2014 and 2013, respectively. During the three months ended June 30, 2014 and 2013, the provision for loan losses was comprised of charges relating to newly originated loans and acquired loans without credit impairment at acquisition of $3.9 million and $11.0 million, respectively, and purchased credit impaired ("PCI") loans of $1.6 million and $0.3 million, respectively. During the six months ended June 30, 2014 and 2013, the consolidated provision for loan losses, primarily in the banking segment, was $8.8 million and $24.3 million, respectively. The provision for loan losses during the six months ended June 30, 2014 and 2013 was comprised of charges relating to newly originated loans and acquired loans without credit impairment at acquisition of $5.3 million and $23.6 million, respectively, and PCI loans of $3.5 million and $0.7 million, respectively.

Consolidated noninterest income decreased $36.0 million and $79.1 million during the three and six months ended June 30, 2014, compared with the same periods in 2013. These year-over-year decreases were primarily related to the reduction in net gains from sale of loans, other mortgage production income and mortgage loan origination fees within our mortgage origination segment of $42.2 million and $97.2 million, respectively, slightly offset by increases in noninterest income in our banking and insurance segments.

Our consolidated noninterest expense during the three and six months ended June 30, 2014 decreased $9.2 million and $11.6 million, respectively, compared with the same periods in 2013. These year-over-year decreases included significant increases in noninterest expenses within our banking segment of $28.3 million and $58.3 million, respectively, primarily due to the inclusion of those operations acquired as part of the FNB Transaction, which were offset by significant decreases in noninterest expenses within our mortgage origination segment of $23.3 million and $54.9 million, respectively, primarily due to reductions in variable compensation tied to mortgage loan originations. Changes between the six months ended June 30, 2014 and 2013 within the major components of noninterest expense included decreases of $18.0 million in employees' compensation and benefits and $15.7 million in loss and loss adjustment expenses, partially offset by increases of $12.5 million in occupancy and equipment and $8.8 million in other expenses.

Consolidated income tax expense during the three months ended June 30, 2014 and 2013 was $16.3 million and $13.3 million, respectively, reflecting effective rates of 36.2% and 37.0%, respectively. During the six months ended June 30, 2014 and 2013, consolidated income tax expense was $30.6 million and $32.5 million, respectively, reflecting effective rates of 36.2% and 36.7%, respectively.

Segment Results

Banking Segment

Income before income taxes in our banking segment for the three months ended June 30, 2014 and 2013 was $41.5 million and $37.3 million, respectively. Income before income taxes increased in the three months ended June 30, 2014, compared with the same period in 2013, due to increases in net interest income and noninterest income, and a decrease in the provision for loan losses, all of which were partially offset by increases in noninterest expense. Income before income taxes in our banking segment for the six months ended June 30, 2014 and 2013 was $73.4 million and $73.5 million, respectively. Income before taxes in the six months ended June 30, 2014 was comparable to the same period in 2013. The operations acquired as a part of the FNB Transaction had a significant effect on each of the components of income before income taxes during both the three and six months ended June 30, 2014, compared to the same periods in 2013.

At June 30, 2014, the Bank exceeded all regulatory capital requirements with a total capital to risk weighted assets ratio of 13.90%, Tier 1 capital to risk weighted assets ratio of 13.22% and a Tier 1 capital to average assets, or leverage, ratio of 9.97%. At June 30, 2014, the Bank was also considered to be "well-capitalized" under regulatory requirements without giving effect to the final capital rules adopted by the Federal Reserve Board on July 2, 2013 ("Basel III"). For additional discussion of the final Basel III capital rules and their impact on our Company, see the section entitled "Liquidity and Capital Resources Regulatory Capital" below.

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

	Three Months Ended June 30,		Six Months Ended June 30,		Year Ended
	2014	2013	2014	2013	December 31, 2013
Performance Ratios:					
Efficiency ratio(1)	56.18%	39.64%	59.56%	39.03%	42.58%
Return on average assets	1.36%	1.62%	1.20%	1.65%	1.78%
Net interest margin (taxable equivalent)(2)	5.52%	5.20%	5.16%	5.21%	5.17%

(1) Noninterest expenses divided by the sum of total noninterest income and net interest income for the period.

(2) Taxable equivalent net interest income divided by average interest-earning assets.

During the three months ended June 30, 2014, the banking segment's taxable equivalent net interest margin of 5.52% was impacted by PlainsCapital Merger related accretion of discount on loans of $17.8 million, amortization of premium on acquired securities of $1.0 million and amortization of premium on acquired time deposits of $0.2 million. Additionally, FNB Transaction related accretion of discount on loans of $8.1 million and amortization of premium on acquired time deposits of $2.3 million also impacted the banking segment's taxable equivalent net interest margin during the three months ended June 30, 2014. These items increased the banking segment's taxable equivalent net interest margin by 162 basis points for the three months ended June 30, 2014. The banking segment's taxable equivalent net interest margin for the three months ended June 30, 2013 of 5.20% was impacted by PlainsCapital Merger related accretion of discount on loans of $16.7 million, amortization of premium on acquired securities of $1.4 million and amortization of premium on acquired time deposits of $0.6 million. These items increased the banking segment's taxable equivalent interest margin by 119 basis points for three months ended June 30, 2013.

During the six months ended June 30, 2014, the banking segment's taxable equivalent net interest margin of 5.16% was impacted by PlainsCapital Merger related accretion of discount on loans of $28.6 million, amortization of premium on acquired securities of $1.9 million and amortization of premium on acquired time deposits of $0.3 million. Additionally, FNB Transaction related accretion of discount on loans of $15.3 million and amortization of premium on acquired time deposits of $4.6 million also impacted the banking segment's taxable equivalent net interest margin during the six months ended June 30, 2014.

These items increased the banking segment's taxable equivalent net interest margin by 138 basis points for the six months ended June 30, 2014. The banking segment's taxable equivalent net interest margin for the six months ended June 30, 2013 of 5.21% was impacted by PlainsCapital Merger related accretion of discount on loans of $33.6 million, amortization of premium on acquired securities of $3.4 million and amortization of premium on acquired time deposits of $1.7 million. These items increased the banking segment's taxable equivalent interest margin by 120 basis points for six months ended June 30, 2013.

The tables below provide additional details regarding our banking segment's net interest income (dollars in thousands).

	Three Months Ended June 30,					
	2014			2013		
	Average Outstanding Balance	Interest Earned or Paid	Annualized Yield or Rate	Average Outstanding Balance	Interest Earned or Paid	Annualized Yield or Rate
Assets						
Interest-earning assets						
Loans, gross(1)	$ 4,216,648	$ 80,173	7.55%	$ 2,949,314	$ 53,435	7.18%
Subsidiary warehouse lines of credit	901,125	8,229	3.61%	1,002,847	14,328	5.65%
Investment securities taxable	913,494	4,561	2.00%	797,472	3,461	1.74%
Investment securities non-taxable(2)	152,042	1,476	3.88%	158,075	1,383	3.50%
Federal funds sold and securities purchased under agreements to resell	20,308	14	0.28%	31,348	22	0.28%
Interest-bearing deposits in other financial institutions	406,773	256	0.25%	323,095	211	0.26%
Other	42,871	411	3.84%	42,304	385	3.64%
Interest-earning assets, gross	6,653,261	95,120	5.68%	5,304,455	73,225	5.47%
Allowance for loan losses	(38,745)			(20,421)		
Interest-earning assets, net	6,614,516			5,284,034		
Noninterest-earning assets	1,260,740			783,049		
Total assets	$ 7,875,256			$ 6,067,083		
Liabilities and Stockholders' Equity						
Interest-bearing liabilities						
Interest-bearing deposits	$ 4,500,603	$ 3,112	0.28%	$ 3,354,713	$ 3,384	0.40%
Notes payable and other borrowings	597,977	392	0.26%	537,821	376	0.28%
Total interest-bearing liabilities(3)	5,098,580	3,504	0.28%	3,892,534	3,760	0.39%
Noninterest-bearing liabilities						
Noninterest-bearing deposits	1,706,187			1,264,331		
Other liabilities	31,748			34,929		
Total liabilities	6,836,515			5,191,794		
Stockholders' equity	1,038,741			875,289		
Total liabilities and stockholders' equity	$ 7,875,256			$ 6,067,083		
Net interest income(2)		$ 91,616			$ 69,465	

Net interest spread(2)	5.40%	5.08%
Net interest margin(2)	5.52%	5.20%

	Six Months Ended June 30,					
	2014			2013		
	Average Outstanding Balance	Interest Earned or Paid	Annualized Yield or Rate	Average Outstanding Balance	Interest Earned or Paid	Annualized Yield or Rate
Assets						
Interest-earning assets						
Loans, gross(1)	$ 4,231,309	$ 150,894	7.11%	$ 2,924,774	$ 107,244	7.30%
Subsidiary warehouse lines of credit	769,643	15,161	3.92%	992,244	28,215	5.66%
Investment securities taxable	905,127	8,956	1.98%	742,512	6,178	1.66%
Investment securities non-taxable(2)	153,048	2,971	3.88%	162,290	2,812	3.47%
Federal funds sold and securities purchased under agreements to resell	23,305	33	0.28%	20,020	28	0.28%
Interest-bearing deposits in other financial institutions	600,960	769	0.26%	403,745	524	0.26%
Other	36,016	812	4.51%	31,269	550	3.52%
Interest-earning assets, gross	6,719,408	179,596	5.33%	5,276,854	145,551	5.49%
Allowance for loan losses	(37,733)			(13,568)		
Interest-earning assets, net	6,681,675			5,263,286		
Noninterest-earning assets	1,265,809			798,492		
Total assets	$ 7,947,484			$ 6,061,778		
Liabilities and Stockholders' Equity						
Interest-bearing liabilities						
Interest-bearing deposits	$ 4,724,047	$ 6,897	0.29%	$ 3,425,592	$ 6,816	0.40%
Notes payable and other borrowings	474,797	717	0.30%	452,542	729	0.32%
Total interest-bearing liabilities(3)	5,198,844	7,614	0.30%	3,878,134	7,545	0.39%
Noninterest-bearing liabilities						
Noninterest-bearing deposits	1,703,019			1,264,024		
Other liabilities	25,169			58,639		
Total liabilities	6,927,032			5,200,797		
Stockholders' equity	1,020,452			860,981		
Total liabilities and stockholders' equity	$ 7,947,484			$ 6,061,778		
Net interest income(2)		$ 171,982			$ 138,006	

Net interest spread(2)	5.03%	5.10%
Net interest margin(2)	5.16%	5.21%

(1) Average balance includes non-accrual loans.

(2)

Annualized taxable equivalent adjustments are based on a 35% tax rate. The adjustment to interest income was $0.5 million for each of the three months ended June 30, 2014 and 2013, respectively, and $1.0 million for each of the six months ended June 30, 2014 and 2013, respectively.

(3)

Excludes the allocation of interest expense on PlainsCapital debt of $0.3 million for each of the three months ended June 30, 2014 and 2013 and $0.6 million and $0.5 million for the six months ended June 30, 2014 and 2013.

The banking segment's net interest margin shown above exceeds our consolidated net interest margin. Our consolidated net interest margin includes the yields and costs associated with certain items within interest-earning assets and interest-bearing liabilities in the financial advisory segment, as well as the borrowing costs of Hilltop and PlainsCapital, both of which reduce our consolidated net interest margin. In addition, the banking segment's interest earning assets include lines of credit extended to subsidiaries, the yields on which increase the banking segment's net interest margin. Such yields and costs are eliminated from the consolidated financial statements.

The following tables summarize the changes in the banking segment's net interest income for the periods indicated below, including the component changes in the volume of average interest-earning assets and interest-bearing liabilities and changes in the rates earned or paid on those items (in thousands).

	Three Months Ended June 30, 2014 v. 2013			Six Months Ended June 30, 2014 v. 2013		
	Change Due To(1)			Change Due To(1)		
	Volume	Yield/Rate	Change	Volume	Yield/Rate	Change
Interest income						
Loans, gross	$ 22,749	$ 3,989	$ 26,738	$ 47,692	$ (4,042)	$ 43,650
Subsidiary warehouse lines of credit	(1,437)	(4,662)	(6,099)	(6,295)	(6,759)	(13,054)
Investment securities taxable	504	596	1,100	1,353	1,425	2,778
Investment securities non-taxable(2)	(53)	146	93	(160)	319	159
Federal funds sold and securities purchased under agreements to resell	(8)		(8)	5		5
Interest-bearing deposits in other financial institutions	55	(10)	45	258	(13)	245
Other	5	21	26	83	179	262
Total interest income(2)	21,815	80	21,895	42,936	(8,891)	34,045
Interest expense						
Deposits	$ 1,159	$ (1,431)	$ (272)	$ 2,605	$ (2,524)	$ 81
Notes payable and other borrowings	42	(26)	16	36	(48)	(12)
Total interest expense	1,201	(1,457)	(256)	2,641	(2,572)	69
Net interest income(2)	$ 20,614	$ 1,537	$ 22,151	$ 40,295	$ (6,319)	$ 33,976

(1)

Changes attributable to both volume and yield/rate are included in yield/rate column.

(2)

Annualized taxable equivalent.

Taxable equivalent net interest income increased $22.2 million and $34.0 million during the three and six months ended June 30, 2014, respectively, compared with the same periods in 2013. Increases in the volume of interest-earning assets, primarily loans acquired in the FNB Transaction, increased taxable equivalent net interest income by $21.8 million and $42.9 million during the three and six months ended June 30, 2014, respectively, compared with the same periods in 2013, while increases in the volume of interest-bearing liabilities, primarily deposits assumed in the FNB Transaction, reduced taxable equivalent interest income by $1.2 million and $2.6 million during these same respective periods. Increases in accretable yields on loans, particularly accretable yield on loans acquired in the PlainsCapital Merger, as well as increased yields on the investment portfolio, were offset by a lower yield on subsidiary warehouse lines of credit, resulting in a net minimal effect on taxable equivalent net interest income due to yield on interest-earning assets for the three months ended June 30, 2014, compared to the same period in 2013. Changes in the yields earned on interest-earning assets decreased taxable equivalent net interest income by $8.9 million during the six months ended June 30, 2014, compared with the same period in 2013, primarily due to lower yields on the loan portfolio and the subsidiary warehouse lines of credit. Changes in rates paid on interest-bearing liabilities increased taxable equivalent interest income by $1.5 million and $2.6 million during the three and six months ended June 30, 2014, respectively, compared with the same periods in 2013, primarily due to the amortization of premiums on time deposits acquired in the FNB Transaction.

The banking segment's noninterest income was $16.4 million and $11.9 million during the three months ended June 30, 2014 and 2013, respectively, and $32.6 million and $24.1 million during the six months ended June 30, 2014 and 2013, respectively. These year-over-year increases in noninterest income were primarily due to service charges and fees on deposits assumed in the FNB Transaction, as well as accretion on the amounts receivable under the loss-share agreements with the FDIC ("FDIC Indemnification Asset") associated with the FNB Transaction. Noninterest income was also negatively affected by decreases in intercompany financing charges associated with the lending commitment on the PrimeLending warehouse line of credit.

The banking segment's noninterest expenses were $60.2 million and $31.9 million during the three months ended June 30, 2014 and 2013, respectively, and $120.9 million and $62.6 million during the six months ended June 30, 2014 and 2013, respectively. Noninterest expenses were primarily comprised of employees' compensation and benefits, and occupancy expenses. The significant year-over-year increase in noninterest expenses was primarily due to the inclusion of the operations acquired in the FNB Transaction.

Mortgage Origination Segment

Income before income taxes in our mortgage origination segment for the three months ended June 30, 2014 and 2013 was $9.2 million and $18.9 million, respectively, while income before income taxes in our mortgage origination segment for the six months ended June 30, 2014 and 2013 was $6.2 million and $31.2 million, respectively. These decreases in income before income taxes for the three and six months ended June 30, 2014 compared to the same periods in 2013 were primarily due to the decreases in noninterest income driven by the reduction in loan origination volume, partially offset by the decreases in noninterest expense primarily due to the reductions in compensation expense that varies with the volume of mortgage loan originations, and to a lesser extent, reductions in segment operating costs made to address the reduction in loan origination volume. Additionally, net interest expense of $2.4 million and $11.8 million during the three months ended June 30, 2014 and 2013, respectively, and net interest expense of $6.5 million and $23.9 million during the six months ended June 30, 2014 and 2013, respectively, resulted from interest incurred on a warehouse line of credit held at the Bank as well as related intercompany financing costs, partially offset by interest income earned on loans held for sale.

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The mortgage origination segment originates all of its mortgage loans through a retail channel. The following table provides certain details regarding our mortgage loan originations (dollars in thousands).

	Three Months Ended June 30,				Six Months Ended June 30,			
	2014	% of Total	2013	% of Total	2014	% of Total	2013	% of Total
Mortgage Loan Originations units	13,373		16,508		22,525		30,954	
Mortgage Loan Originations volume	$ 2,838,731		$ 3,549,670		$ 4,704,884		$ 6,595,933	
Mortgage Loan Originations:								
Conventional	$ 1,777,589	62.62%	$ 2,251,378	63.43%	$ 2,971,726	63.16%	$ 4,176,149	63.31%
Government	818,158	28.82%	1,022,069	28.79%	1,370,486	29.13%	1,945,788	29.50%
Jumbo	238,991	8.42%	267,063	7.52%	355,725	7.56%	452,451	6.86%
Other	3,993	0.14%	9,160	0.26%	6,947	0.15%	21,545	0.33%
	$ 2,838,731	100.00%	$ 3,549,670	100.00%	$ 4,704,884	100.00%	$ 6,595,933	100.00%
Home purchases	$ 2,396,094	84.41%	$ 2,377,871	66.99%	$ 3,864,805	82.14%	$ 3,987,732	60.46%
Refinancings	442,637	15.59%	1,171,799	33.01%	840,079	17.86%	2,608,201	39.54%
	$ 2,838,731	100.00%	$ 3,549,670	100.00%	$ 4,704,884	100.00%	$ 6,595,933	100.00%
Texas	$ 692,878	24.41%	$ 788,996	22.23%	$ 1,123,033	23.87%	$ 1,446,257	21.93%
California	387,445	13.65%	673,388	18.97%	679,017	14.43%	1,225,206	18.57%
Florida	135,701	4.78%	116,419	3.28%	229,075	4.87%	226,592	3.43%
North Carolina	123,930	4.37%	181,365	5.11%	215,662	4.58%	356,206	5.40%
Ohio	117,026	4.12%	121,378	3.42%	184,106	3.91%	230,734	3.50%
Virginia	93,538	3.29%	149,027	4.20%	144,417	3.07%	281,514	4.27%
Arizona	85,268	3.00%	123,473	3.48%	164,753	3.50%	230,734	3.50%
Missouri	84,962	2.99%	56,728	1.60%	137,209	2.92%	102,343	1.55%
South Carolina	84,190	2.97%	96,326	2.71%	130,107	2.77%	172,104	2.61%
All other states	1,033,793	36.42%	1,242,570	35.00%	1,697,505	36.08%	2,324,243	35.24%
	$ 2,838,731	100.00%	$ 3,549,670	100.00%	$ 4,704,884	100.00%	$ 6,595,933	100.00%

The mortgage lending business is subject to variables that can impact loan origination volume, including seasonal and interest rate fluctuations. Historically, we have typically experienced increased loan origination volume from purchases of homes during the spring and summer, when more people tend to move and buy or sell homes. An increase in mortgage interest rates tends to result in decreased loan origination volume from refinancings, while a decrease in mortgage interest rates tends to result in increased refinancings. Changes in interest rates have historically had a lesser impact on home purchases volume than on refinancing volume.

Beginning in May 2013 and continuing through the fourth quarter of 2013, mortgage interest rates increased at a pace that, along with other factors, resulted in decreases of 20.0% and 28.7% in the mortgage origination segment's total loan origination volume during the three and six months ended June 30, 2014 when compared to the same periods in 2013. Home purchases volume of $2.4 billion during the three months ended

June 30, 2014 was virtually unchanged from the three months ended June 30, 2013, while the mortgage origination segment experienced a $927.4 million increase, or 63.1%, in home purchases volume between the three months ended March 31, 2014 and three months ended June 30, 2014. Refinancing volume decreased from $1.2 billion during the three months ended June 30, 2013 (33% of total loan origination volume) to $442.6 million during the three months ended June 30, 2014 (16% of total loan origination volume). For each quarter subsequent to the second quarter of 2013, the mortgage origination segment's refinancing volume as a percentage of total loan origination volume has ranged between 16% and 21%. We anticipate that this trend will continue throughout the remainder of 2014, and total mortgage loan origination volumes in 2014 will more closely follow seasonal trends historically experienced by the mortgage origination segment.

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While the mortgage origination segment's total loan origination volume decreased 20.0% during the three months ended June 30, 2014, compared to the same period in 2013, income before income taxes decreased 51.3% between the same periods ($9.2 million income compared to $18.9 million income). Income before income taxes decreased at a greater rate primarily because segment operating costs included in noninterest expenses, such as employee related (salaries and benefits), occupancy, and administrative expenses, decreased at a lesser rate, approximately 11%, than loan origination volume decreased between the two periods. To address negative trends in loan origination volume resulting from changes in interest rates that began in May 2013, the mortgage origination segment reduced its non-origination employee headcount approximately 22% during the third and fourth quarters of 2013. Salaries and benefits expenses for the three and six months ended June 30, 2014 decreased approximately 11% and 13% respectively, as compared to the same periods in 2013 as the benefits of the headcount reductions in the third and fourth quarters of 2013 were realized. We also engaged in other initiatives to reduce segment operating costs during the third and fourth quarters of 2013 that were primarily responsible for the decrease of approximately 11% in non-employee related expenses for both the three and six months ended June 30, 2014 as compared to the same periods in 2013. The benefits of the employee reductions and other cost savings initiatives include a decrease in recurring quarterly operating costs of approximately $8 million since the third quarter of 2013. Also impacting the trend in income before taxes, to a lesser extent, was a decrease in loan revenue margins resulting from increased pricing competition.

The mortgage origination segment sells substantially all mortgage loans it originates to various investors in the secondary market, the majority servicing released. During the six months ended June 30, 2013, the mortgage origination segment retained servicing on approximately 8% of loans sold. This rate was increased to approximately 22% during the third and fourth quarters of 2013, and approximately 31% during the six months ended June 30, 2014. The related mortgage servicing rights ("MSR") asset was valued at $35.9 million on $3.3 billion of serviced loan volume at June 30, 2014, compared to a value of $20.1 million on $2.0 billion of serviced loan volume at December 31, 2013. All income related to retained servicing, including changes in the value of the MSR asset, is included in noninterest income. The mortgage origination segment's determination on whether to retain or release servicing on mortgage loans it sells is impacted by changes in mortgage interest rates, and refinancing and market activity. We may, from time to time, manage our MSR asset through different strategies, including varying the percentage of mortgage loans sold servicing released and opportunistically selling MSR assets. In July 2014, the mortgage origination segment sold MSR assets of $11.4 million, which represented approximately $1.0 billion of its serviced loan volume.

Noninterest income was $122.8 million and $165.3 million for the three months ended June 30, 2014 and 2013, respectively, and $214.6 million and $311.8 million for the six months ended June 30, 2014 and 2013, respectively. Noninterest income was comprised of net gains on the sale of loans and other mortgage production income, and mortgage origination fees. Noninterest income decreased 25.7% and 31.2% during the three and six months ended June 30, 2014 when compared to the same periods in 2013, which were comparable to the decreases of 20.0% and 28.7% in loan origination volume experienced during the same respective periods.

Gains and losses resulting from changes in the fair value of the mortgage origination segment's interest rate lock commitments ("IRLCs") and loans held for sale, and the related activity associated with forward commitments used by the mortgage origination segment to mitigate interest rate risk associated with its IRLCs and mortgage loans held for sale, are included in noninterest income. Related net gains totaled $25.7 million and $6.9 million during the three months ended June 30, 2014 and 2013, respectively, and net gains totaled $29.0 million and $3.4 million during the six months ended June 30, 2014 and 2013, respectively. During the three and six months ended June 30, 2014, the net gains were primarily the result of an increase in the volume of IRLCs and mortgage loans held during these respective periods.

Noninterest expenses were $111.2 million and $134.5 million for the three months ended June 30, 2014 and 2013, respectively, and $201.9 million and $256.8 million for the six months ended June 30, 2014 and 2013, respectively. Employees' compensation and benefits accounted for the majority of the noninterest expenses incurred. Compensation that varies with the volume of mortgage loan originations and overall segment profitability decreased $14.1 million and $31.4 million during the three and six months ended June 30, 2014, as compared to the same periods in 2013, and comprised approximately 60% and 64% of the total employees' compensation and benefits expenses during the three months ended June 30, 2014 and 2013, respectively, and 56% and 62% during the six months ended June 30, 2014 and 2013, respectively. In addition, employee salaries and benefits decreased $3.7 million and $8.5 million during the three and six months ended June 30, 2014, as compared to the same periods in 2013, primarily as a result of headcount reductions in the third and fourth quarters of 2013. The mortgage origination segment records unreimbursed closing costs as noninterest expense when it pays a customer's closing costs in return for the customer choosing to accept a higher interest rate on the customer's mortgage loan. Unreimbursed closing costs during the three months ended June 30, 2014 and 2013 were $8.7 million and $9.8 million, respectively, and $13.9 million and $20.3 million for the six months ended June 30, 2014 and 2013, respectively.

Between January 1, 2005, and June 30, 2014, the mortgage origination segment sold mortgage loans totaling $59.9 billion. These loans were sold under sales contracts that generally include provisions which hold the mortgage origination segment responsible for errors or omissions relating to its representations and warranties that loans sold meet certain requirements, including representations as to underwriting standards and the validity of certain borrower representations in connection with the loan. In addition, the sales contracts typically require the refund of purchased servicing rights plus certain investor servicing costs if a loan experiences an early payment default. While the mortgage origination segment sold loans prior to 2005, it has not experienced, nor does it anticipate experiencing, significant losses on loans originated prior to 2005 as a result of investor claims under these provisions of its sales contracts.

When an investor claim for indemnification of a loan sold is made, we evaluate the claim and determine if the claim can be satisfied through additional documentation or other deliverables. If the claim cannot be satisfied in that matter, we negotiate with the investor to reach a settlement of the claim. Settlements typically result in either the repurchase of a loan or reimbursement to the investor for losses incurred on the loan. Following is a summary of the mortgage origination segment's claims resolution activity relating to loans sold between January 1, 2005 and June 30, 2014 (dollars in thousands).

	Original Loan Balance		Loss Recognized	
	Amount	**% of Loans Sold**	**Amount**	**% of Loans Sold**
Claims resolved with no payment	$ 145,524	0.24%	$	0.00%
Claims resolved as a result of a loan repurchase or payment to an investor for losses incurred(1)	185,178	0.31%	24,291	0.04%
	$ 330,702	0.55%	$ 24,291	0.04%

(1) Losses incurred include refunded purchased servicing rights.

At June 30, 2014 and December 31, 2013, the mortgage origination segment's indemnification liability reserve totaled $19.7 million and $21.1 million, respectively. The related provision for indemnification losses was $0.9 million and $1.0 million for the three months ended June 30, 2014 and

2013, respectively, and $1.4 million and $2.0 million for the six months ended June 30, 2014 and 2013, respectively.

Insurance Segment

Losses before income taxes in our insurance segment were $5.5 million and $20.5 million during the three months ended June 30, 2014 and 2013. Income before income taxes in our insurance segment was $6.0 million during the six months ended June 30, 2014, compared with a loss before income taxes of $14.3 million during the same period in 2013. The insurance segment is subject to claims arising out of severe weather, the incidence and severity of which are inherently unpredictable. Generally, the insurance segment's insured risks exhibit higher losses in the second and third calendar quarters due to a seasonal concentration of weather-related events in its primary geographic markets. Although weather-related losses (including hail, high winds, tornadoes and hurricanes) can occur in any calendar quarter, the second calendar quarter, historically, has experienced the highest frequency of losses associated with these events. Hurricanes, however, are more likely to occur in the third calendar quarter of the year.

The significant year-over-year improvements in operating results in our insurance segment were primarily a result of growth of earned premium and improved claims loss experience associated with the significant decline in the severity of severe weather-related events during 2014. Based on our estimates of the ultimate losses, claims associated with these storms totaled $14.3 million through June 30, 2014. The significant loss during the three months ended June 30, 2013 was primarily driven by the severity of three tornado, wind and hail storms during the second quarter of 2013. Based on estimates of the ultimate cost, two of these storms are considered catastrophic losses as they exceeded our $8 million reinsurance retention during the third quarter of 2013. The estimate of ultimate losses from these storms totaled $20.9 million through June 30, 2013 with a net loss, after reinsurance, of $20.7 million.

During 2013, the insurance segment initiated a review of the pricing of its primary products in each state of operation utilizing a consulting actuarial firm to supplement normal review processes. Rate filings have been made for certain products in several states for increases effective in 2014, and the process will continue through the remainder of the insurance segment's products and states in which it operates. Concurrently, business concentrations were reviewed and actions initiated, including cancellation of agents, non-renewal of policies and cessation of new business writing on certain products in problematic geographic areas. These actions have reduced the rate of premium growth for the first six months of 2014 when compared with the patterns exhibited in prior years. However, we expect the reduced exposure to volatile weather through a lower number of insureds in these areas to improve our loss experience during 2014.

The insurance segment's operations resulted in combined ratios of 118.2% and 158.2% during the three months ended June 30, 2014 and 2013, respectively, and 97.9% and 124.0% during the six months ended June 30, 2014 and 2013, respectively. The year-over-year improvement in the combined ratios was primarily driven by the increase in earned premiums and improvement in our claims loss experience. The combined ratio is a measure of overall insurance underwriting profitability, and represents the sum of the loss and LAE ratio and the underwriting expense ratio, which are discussed in more detail below.

Noninterest income of $43.1 million during the three months ended June 30, 2014 included net insurance premiums earned of $40.8 million, compared to $38.6 million for the same period in 2013, while noninterest income of $85.9 million during the six months ended June 30, 2014 included net insurance premiums earned of $81.1 million, compared to $76.1 million for the same period in 2013. The increase in earned premiums during both periods is primarily attributable to rate and volume increases in homeowners and mobile home products.

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

	Three Months Ended June 30, 2014	Three Months Ended June 30, 2013	Variance 2014 vs 2013	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013	Variance 2014 vs 2013
Direct Insurance Premiums Written:						
Homeowners	$ 21,431	$ 21,980	$ (549)	$ 40,016	$ 40,524	$ (508)
Fire	15,125	14,959	166	28,960	28,011	949
Mobile Home	10,280	9,646	634	20,499	18,729	1,770
Commercial	1,075	1,264	(189)	2,161	2,398	(237)
Other	88	101	(13)	134	145	(11)
	$ 47,999	$ 47,950	$ 49	$ 91,770	$ 89,807	$ 1,963

Total direct insurance premiums written for our three largest insurance product lines increased by $0.3 million and $2.2 million during the three and six months ended June 30, 2014, respectively, compared to the same periods in 2013. These increases were due to growth in our core insurance products.

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

	Three Months Ended June 30, 2014	Three Months Ended June 30, 2013	Variance 2014 vs 2013	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013	Variance 2014 vs 2013
Net Insurance Premiums Earned:						
Homeowners	$ 18,243	$ 17,721	$ 522	$ 35,361	$ 34,322	$ 1,039
Fire	12,847	12,039	808	25,592	23,724	1,868
Mobile Home	8,701	7,730	971	18,114	15,862	2,252
Commercial	909	1,015	(106)	1,910	2,031	(121)
Other	77	85	(8)	119	124	(5)
	$ 40,777	$ 38,590	$ 2,187	$ 81,096	$ 76,063	$ 5,033

Net insurance premiums earned for the three and six months ended June 30, 2014 increased compared to the same periods in 2013, primarily due to increases in net insurance premiums written of $0.5 million and $3.3 million, respectively.

Noninterest expenses of $49.4 million and $62.1 million during the three months ended June 30, 2014 and 2013, respectively, and $81.8 million and $96.4 million during the six months ended June 30, 2014 and 2013, respectively, include both loss and LAE expenses and policy acquisition and other underwriting expenses, as well as other noninterest expenses. Loss and LAE are recognized based on formula and case basis estimates for losses reported with respect to direct business, estimates of unreported losses based on past experience and deduction of amounts for reinsurance placed with reinsurers. Loss and LAE during the three months ended June 30, 2014 was $35.3 million, compared to $48.2 million during the same period in 2013, resulting in loss and LAE ratios of 86.5% and 124.8% during the three months ended June 30, 2014 and 2013, respectively. Loss and LAE during the six months ended June 30, 2014 was $53.6 million, compared to $69.3 million during the same period in 2013. As a result, the loss and LAE ratios during the six months ended June 30, 2014 and 2013 were 66.1% and 91.2%, respectively. These year-over-year ratio improvements were primarily a result of growth of earned premium and improved claims loss experience associated with the significant decline in the severity of severe weather-related events during 2014.

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

Policy acquisition and other underwriting expenses were as follows (dollars in thousands).

	Three Months Ended June 30,		Variance	Six Months Ended June 30,		Variance
	2014	2013	2014 vs 2013	2014	2013	2014 vs 2013
Amortization of deferred policy acquisition costs	$ 10,402	$ 10,273	$ 129	$ 20,599	$ 19,887	$ 712
Other underwriting expenses	3,325	3,273	52	6,705	6,304	401
Total	13,727	13,546	181	27,304	26,191	1,113
Agency expenses	(813)	(658)	(155)	(1,503)	(1,226)	(277)
Total less agency expenses	$ 12,914	$ 12,888	$ 26	$ 25,801	$ 24,965	$ 836
Net insurance premiums earned	$ 40,777	$ 38,590	$ 2,187	$ 81,096	$ 76,063	$ 5,033
Expense ratio	31.7%	33.4%	-1.7%	31.8%	32.8%	-1.0%

Financial Advisory Segment

Income before income taxes in our financial advisory segment during the three months ended June 30, 2014 and 2013 was $0.6 million and $2.0 million, respectively, while income before income taxes in our financial advisory segment during the six months ended June 30, 2014 and 2013 was $0.5 million and $2.3 million, respectively. Continuing uncertainty in fixed income markets as a result of increased regulations, uncertainty in the direction of future interest rates and a lack of liquidity in the market have resulted in reduced sales of fixed income securities to institutional customers.

The financial advisory segment had net interest income of $3.2 million and $3.5 million during the three months ended June 30, 2014 and 2013, respectively, and $5.8 million and $6.8 million during the six months ended June 30, 2014 and 2013, respectively, consisting of securities lending activity, customer margin loan balances and investment securities used to support sales, underwriting and other customer activities.

Noninterest income was $25.8 million and $28.9 million during the three months ended June 30, 2014 and 2013, respectively, and $50.4 million and $51.6 million during the six months ended June 30, 2014 and 2013, respectively. The majority of the financial advisory segment's noninterest income was generated from fees and commissions earned from investment advisory and securities brokerage activities of $22.3 million and $26.0 million during the three months ended June 30, 2014 and 2013, respectively, and $43.6 million and $48.0 million during the six months ended June 30, 2014 and 2013, respectively. The financial advisory segment participates in programs in which it issues forward purchase commitments of mortgage-backed securities to certain clients and sells TBAs. Changes in the fair values of these derivative instruments produced net gains of $3.2 million and $3.8 million during the three months ended June 30, 2014 and 2013, respectively, and $6.1 million and $5.6 million during the six months ended June 30, 2014 and 2013, respectively. Changes in the fair value of the financial advisory segment's trading portfolio, which is used to support sales, underwriting and other customer activities, produced gains of $0.3 million and losses of $1.9 million during the three months ended June 30, 2014 and 2013, respectively, and gains of $0.7 million and losses of $0.9 million during the six months ended June 30, 2014 and 2013, respectively.

Noninterest expenses were $28.4 million and $30.4 million during the three months ended June 30, 2014 and 2013, respectively, and $55.7 million and $56.1 million during the six months ended June 30, 2014 and 2013, respectively. Employees' compensation and benefits accounted for the majority of the

decrease in noninterest expenses primarily due to decreases in compensation costs that vary with noninterest income.

Corporate

Corporate includes certain activities not allocated to specific business segments. These activities include holding company financing and investing activities, and management and administrative services to support the overall operations of the Company including, but not limited to, certain executive management, corporate relations, legal, finance, and acquisition costs not allocated to business segments.

As a holding company, Hilltop's primary investment objectives are to preserve capital and have available cash resources to utilize in making acquisitions. Investment and interest income earned, primarily from available cash and available-for-sale securities, including our note receivable from SWS, was $1.7 million and $1.6 million during the three months ended June 30, 2014 and 2013, respectively, and $3.4 million and $3.3 million during the six months ended June 30, 2014 and 2013, respectively.

Interest expense of $1.7 million and $3.5 million during the three and six months ended June 30, 2013, respectively, was due to interest costs associated with the 7.50% Senior Exchangeable Notes due 2025 of HTH Operating Partnership LP, a wholly owned subsidiary of Hilltop, which were called for redemption during the fourth quarter of 2013.

Noninterest expenses were $2.6 million and $1.7 million during the three months ended June 30, 2014 and 2013, respectively, and $4.8 million and $3.9 million during the six months ended June 30, 2014 and 2013, respectively. Noninterest expenses were primarily comprised of employees' compensation and benefits and professional fees. The increases in noninterest expenses were primarily due to year-over-year increases in headcount and related costs.

Financial Condition

The following discussion contains a more detailed analysis of our financial condition at June 30, 2014 as compared to December 31, 2013.

Securities Portfolio

At June 30, 2014, investment securities consisted of securities of the U.S. Treasury, U.S. government and its agencies, obligations of municipalities and other political subdivisions, primarily in the State of Texas, mortgage-backed, corporate debt, and equity securities, a note receivable and a warrant. We have the ability to categorize investments as trading, available for sale, and held to maturity.

Trading securities are bought and held principally for the purpose of selling them in the near term and are carried at fair value, marked to market through operations and held at the Bank and First Southwest. Securities that may be sold in response to changes in market interest rates, changes in securities' prepayment risk, increases in loan demand, general liquidity needs and other similar factors are classified as available for sale and are carried at estimated fair value, with unrealized gains and losses recorded in accumulated other comprehensive income (loss). Securities are classified as held to maturity based on the intent and ability of our management, at the time of purchase, to hold such securities to maturity. These securities are carried at amortized cost.

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

	June 30, 2014	December 31, 2013
Trading securities, at fair value	$ 61,663	$ 58,846
Securities available for sale, at fair value		
U.S. Treasury securities	63,822	43,528
U.S. government agencies:		
Bonds	635,099	662,732
Residential mortgage-backed securities	57,504	60,087
Collateralized mortgage obligations	107,130	120,461
Corporate debt securities	101,255	76,608
States and political subdivisions	147,831	156,835
Commercial mortgage-backed securities	665	760
Equity securities	24,653	22,079
Note receivable	49,921	47,909
Warrant	13,898	12,144
	1,201,778	1,203,143
Securities held to maturity, at amortized cost		
U.S. government agencies:		
Residential mortgage-backed securities	31,048	
Collateralized mortgage obligations	29,821	
States and political subdivisions	4,406	
	65,275	
Total securities portfolio	$ 1,328,716	$ 1,261,989

We had net unrealized losses of $4.1 million and $53.7 million related to the available for sale investment portfolio at June 30, 2014 and December 31, 2013, respectively. The significant decrease in the net unrealized loss position of our available for sale investment portfolio during 2014 was due to the effects of a decrease in market interest rates since December 31, 2013 that resulted in an increase in the fair value of our debt securities.

The market value of securities held to maturity at June 30, 2014 approximated book value.

Banking Segment

The banking segment's securities portfolio plays a role in the management of our interest rate sensitivity and generates additional interest income. In addition, the securities portfolio is used to meet collateral requirements for public and trust deposits, securities sold under agreements to repurchase and other purposes. The available for sale securities portfolio serves as a source of liquidity. Historically, the Bank's policy has been to invest primarily in securities of the U.S. government and its agencies, obligations of municipalities in the State of Texas and other high grade fixed income securities to minimize credit risk. At June 30, 2014, the banking segment's securities portfolio of $1.1 billion was comprised of trading securities of $21.1 million, available for sale securities of $974.1 million and held to maturity securities of $65.3 million.

Insurance Segment

Our insurance segment's primary investment objective is to preserve capital and manage for a total rate of return. NLC's strategy is to purchase securities in sectors that represent the most attractive relative value. Our insurance segment invests the premiums it receives from policyholders until they are

needed to pay policyholder claims or other expenses. At June 30, 2014, the insurance segment's securities portfolio was comprised of $153.1 million in available for sale securities and $5.5 million of other investments included in other assets within the consolidated balance sheet.

Financial Advisory Segment

Our financial advisory segment holds securities to support sales, underwriting and other customer activities. Because FSC is a broker-dealer, it is required to carry its securities at fair value and record changes in the fair value of the portfolio in operations. Accordingly, FSC classifies its securities portfolio of $40.5 million at June 30, 2014 as trading.

Corporate

Available for sale securities of Hilltop at June 30, 2014 include the note receivable from, and warrant to purchase shares of SWS, of $63.8 million, and equity securities of $10.7 million representing those shares of SWS common stock held by Hilltop.

Non-Covered Loan Portfolio

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

June 30, 2014	Loans, excluding PCI Loans	PCI Loans	Total Loans
Commercial and industrial	$ 1,660,181	$ 21,474	$ 1,681,655
Real estate	1,560,314	26,221	1,586,535
Construction and land development	381,608	10,003	391,611
Consumer	51,947	3,089	55,036
Non-covered loans, gross	3,654,050	60,787	3,714,837
Allowance for loan losses	(32,857)	(3,574)	(36,431)
Non-covered loans, net of allowance	$ 3,621,193	$ 57,213	$ 3,678,406

December 31, 2013	Loans, excluding PCI Loans	PCI Loans	Total Loans
Commercial and industrial	$ 1,600,450	$ 36,816	$ 1,637,266
Real estate	1,418,003	39,250	1,457,253
Construction and land development	344,734	19,817	364,551
Consumer	51,067	4,509	55,576
Non-covered loans, gross	3,414,254	100,392	3,514,646
Allowance for loan losses	(30,104)	(3,137)	(33,241)
Non-covered loans, net of allowance	$ 3,384,150	$ 97,255	$ 3,481,405

Banking Segment

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

The banking segment's total non-covered loans, net of the allowance for non-covered loan losses, were $4.2 billion and $4.3 billion at June 30, 2014 and December 31, 2013, respectively. The banking segment's non-covered loan portfolio includes a $1.5 billion warehouse line of credit extended to PrimeLending, of which $1.3 billion and $1.0 billion was drawn at June 30, 2014 and December 31, 2013, respectively, as well as term loans to First Southwest that had an outstanding balance of $23.0 million at June 30, 2014 and December 31, 2013. Prior to June 2014, the warehouse line of credit had $1.3 billion of availability. Amounts advanced against the warehouse line of credit and the First Southwest term loans are eliminated from net loans on our consolidated balance sheets.

The banking segment does not generally participate in syndicated loan transactions and has no foreign loans in its portfolio. The areas of concentration within our covered real estate portfolio were construction and land development loans, non-construction residential real estate loans, and non-construction commercial real estate loans. At June 30, 2014, the banking segment's non-covered loan concentrations (loans to borrowers engaged in similar activities) that exceeded 10% of its total non-covered loans included construction and land development loans and non-construction commercial real estate loans within the non-covered real estate portfolio. At June 30, 2014, construction and land development loans and non-construction commercial real estate loans were 10.39% and 29.40%, respectively, of the banking segment's total non-covered loans. The banking segment's non-covered loan concentrations were within regulatory guidelines at June 30, 2014.

Mortgage Origination Segment

The loan portfolio of the mortgage origination segment consists of loans held for sale, primarily single-family residential mortgages funded through PrimeLending, and pipeline loans, which are loans in various stages of the application process, but not yet closed and funded. Pipeline loans may not close if potential borrowers elect in their sole discretion not to proceed with the loan application. Total loans held for sale were $1.4 billion and $1.1 billion at June 30, 2014 and December 31, 2013, respectively.

The components of the mortgage origination segment's loans held for sale and pipeline loans are as follows (in thousands).

	June 30, 2014	December 31, 2013
Loans held for sale:		
Unpaid principal balance	$ 1,348,551	$ 1,066,850
Fair value adjustment	61,723	21,555
	$ 1,410,274	$ 1,088,405
Pipeline loans:		
Unpaid principal balance	$ 981,330	$ 602,467
Fair value adjustment	28,584	12,151
	$ 1,009,914	$ 614,618

Financial Advisory Segment

The loan portfolio of the financial advisory segment consists primarily of margin loans to customers and correspondents. These loans are collateralized by the securities purchased or by other securities owned by the clients and, because of collateral coverage ratios, are believed to present minimal collectability exposure. Additionally, these loans are subject to a number of regulatory

requirements as well as FSC's internal policies. The financial advisory segment's total non-covered loans, net of the allowance for non-covered loan losses, were $356.7 million and $281.6 million at June 30, 2014 and December 31, 2013, respectively. This increase was primarily attributable to increased borrowings in margin accounts held by FSC customers and correspondents.

Covered Loan Portfolio

Banking Segment

Loans acquired in the FNB Transaction that are subject to loss-share agreements with the FDIC are referred to as "covered loans" and reported separately in our consolidated balance sheets. Under the terms of the loss-share agreements, the FDIC has agreed to reimburse the Bank the following amounts with respect to the covered assets (including covered loans): (i) 80% of losses on the first $240.4 million of losses incurred; (ii) 0% of losses in excess of $240.4 million up to and including $365.7 million of losses incurred; and (iii) 80% of losses in excess of $365.7 million of losses incurred. The Bank has also agreed to reimburse the FDIC for any subsequent recoveries. The loss-share agreements for commercial and single family residential loans are in effect for 5 years and 10 years, respectively, and the loss recovery provisions to the FDIC are in effect for 8 years and 10 years, respectively, from the Bank Closing Date. In accordance with the loss-share agreements, the Bank may be required to make a "true-up" payment to the FDIC approximately ten years following the Bank Closing Date if the FDIC's initial estimate of losses on covered assets is greater than the actual realized losses. The "true-up" payment is calculated using a defined formula set forth in the P&A Agreement.

In connection with the FNB Transaction, the Bank acquired loans both with and without evidence of credit quality deterioration since origination. The banking segment's portfolio of acquired covered loans had a fair value of $1.1 billion as of the Bank Closing Date, with no carryover of any allowance for loan losses.

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

June 30, 2014	**Loans, excluding PCI Loans**	**PCI Loans**	**Total Loans**
Commercial and industrial	$ 23,892	$ 26,124	$ 50,016
Real estate	208,870	489,355	698,225
Construction and land development	17,033	79,739	96,772
Consumer			
Covered loans, gross	249,795	595,218	845,013
Allowance for loan losses	(201)	(3,914)	(4,115
Covered loans, net of allowance	$ 249,594	$ 591,304	$ 840,898

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

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At June 30, 2014, the banking segment had covered loan concentrations (loans to borrowers engaged in similar activities) that exceeded 10% of total covered loans in its real estate portfolio. The areas of concentration within our covered real estate portfolio were construction and land development loans, non-construction residential real estate loans, and non-construction commercial real estate loans. At June 30, 2014, construction and land development loans, non-construction residential real estate loans, and non-construction commercial real estate loans were 13.45%, 34.09% and 41.98%, respectively, of the banking segment's total covered loans. The banking segment's covered loan concentrations were within regulatory guidelines at June 30, 2014.

Allowance for Loan Losses

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

It is management's responsibility at the end of each quarter, or more frequently as deemed necessary, to analyze the level of the allowance for loan losses to ensure that it is appropriate for the estimated credit losses in the portfolio consistent with the Interagency Policy Statement on the Allowance for Loan and Lease Losses and the Receivables and Contingencies Topics of the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC"). Estimated credit losses are the probable current amount of loans that we will be unable to collect given facts and circumstances as of the evaluation date. When management determines that a loan, or portion thereof, is uncollectible, the loan, or portion thereof, is charged-off against the allowance for loan losses, or for acquired loans accounted for in pools, charged against the pool discount. Recoveries on charge-offs that occurred prior to the PlainsCapital Merger represent contractual cash flows not expected to be collected and are recorded as accretion income. Recoveries on loans charged-off subsequent to the PlainsCapital Merger are credited to the allowance for loan loss, except for recoveries on loans accounted for in pools, which are credited to the pool discount.

We have developed a methodology that seeks to determine an allowance within the scope of the Receivables and Contingencies Topics of the ASC. Each of the loans that has been determined to be impaired is within the scope of the Receivables Topic. Impaired loans that are equal to or greater than $0.5 million are individually evaluated for impairment using one of three impairment measurement methods as of the evaluation date: (1) the present value of expected future discounted cash flows on the loan, (2) the loan's observable market price, or (3) the fair value of the collateral if the loan is collateral dependent. Specific reserves are provided in our estimate of the allowance based on the measurement of impairment under these three methods, except for collateral dependent loans, which require the fair value method. All non-impaired loans are within the scope of the Contingencies Topic. Estimates of loss for the Contingencies Topic are calculated based on historical loss, adjusted for qualitative or environmental factors. The Bank uses a rolling three year average net loss rate to calculate historical loss factors. The analysis is conducted by call report category, and further disaggregates commercial and industrial loans by collateral type. The analysis considers charge-offs and recoveries in determining the loss rate; therefore net charge-off experience is used. The historical loss calculation for the quarter is calculated by dividing the current quarter net charge-offs for each loan category by the quarter ended loan category balance. The Bank utilizes a weighted average loss rate to better represent recent trends. The Bank weights the most recent four quarter average at 120% versus the oldest four quarters at 80%.

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

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

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

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

Homogeneous loans, such as consumer installment loans, residential mortgage loans and home equity loans, are not individually reviewed and are generally risk graded at the same levels. The risk grade and reserves are established for each homogeneous pool of loans based on the expected net charge-offs from current trends in delinquencies, losses or historical experience and general economic conditions. At June 30, 2014, we had no material delinquencies in these types of loans.

The allowance is subject to regulatory examination and determination as to adequacy, which may take into account such factors as the methodology used to calculate the allowance and the size of the allowance. While we believe we have an appropriate allowance for our existing non-covered and covered portfolios at June 30, 2014, additional provisions for losses on existing loans may be necessary in the future. Within our non-covered portfolio, we recorded net charge-offs of $2.3 million and $1.7 million for the three months ended June 30, 2014 and 2013, respectively, and $2.3 million and $1.5 million for the six months ended June 30, 2014 and 2013, respectively. Our allowance for non-covered loan losses totaled $36.4 million and $33.2 million at June 30, 2014 and December 31, 2013, respectively. The ratio of the allowance for non-covered loan losses to total non-covered loans held for investment at June 30, 2014 and December 31, 2013 was 0.98% and 0.95%, respectively.

In connection with the PlainsCapital Merger and the FNB Transaction, we acquired loans both with and without evidence of credit quality deterioration since origination. PCI loans acquired in the PlainsCapital Merger are accounted for on an individual loan basis, while PCI loans acquired in the FNB Transaction are accounted for in pools as well as on an individual loan basis. We have established under our PCI accounting policy a framework to aggregate certain acquired loans into various loan pools based on a minimum of two layers of common risk characteristics for the purpose of determining their respective fair values as of their acquisition dates, and for applying the subsequent recognition and measurement provisions for income accretion and impairment testing. The common risk characteristics used for the pooling of the FNB PCI loans are risk grade and loan collateral type. The acquired loans were initially recorded at fair value with no carryover of any allowance for loan losses. Within our covered portfolio, we recorded net charge-offs of $0.3 million for the six months ended June 30, 2014. Our allowance for covered loan losses totaled $4.1 million and $1.1 million at June 30, 2014 and December 31, 2013, respectively. The ratio of the allowance for covered loan losses to total covered loans held for investment at June 30, 2014 and December 31, 2013 was 0.49% and 0.11%, respectively.

Provisions for loan losses are charged to operations to record the total allowance for loan losses at a level deemed appropriate by the banking segment's management based on such factors as the volume and type of lending it conducted, the amount of non-performing loans and related collateral security, the present level of the allowance for loan losses, the results of recent regulatory examinations, generally accepted accounting principles, general economic conditions and other factors related to the ability to collect loans in its portfolio. The provision for loan losses, primarily in the banking segment, within our non-covered and covered portfolios was $5.5 million and $11.3 million for the three months ended June 30, 2014 and 2013, respectively, and $8.8 million and $24.3 million for the six months ended June 30, 2014 and 2013, respectively.

The following tables present the activity in our allowance for loan losses within our non-covered and covered loan portfolios for the periods presented (in thousands). Substantially all of the activity shown below occurred within the banking segment.

	Three Months Ended June 30,		**Six Months Ended June 30,**	
Non-Covered Portfolio	**2014**	**2013**	**2014**	**2013**
Balance, beginning of period	$ 34,645	$ 16,637	$ 33,241	$ 3,409
Provisions charged to operating expenses	4,083	11,289	5,471	24,294
Recoveries of non-covered loans previously charged off:				
Commercial and industrial	629	1,921	1,354	2,415
Real estate	82	62	114	201
Construction and land development	41	44	163	151
Consumer	32	20	50	28
Total recoveries	784	2,047	1,681	2,795
Non-covered loans charged off:				
Commercial and industrial	2,924	3,656	3,731	4,094
Real estate	72	65	72	96
Construction and land development				
Consumer	85	15	159	71
Total charge-offs	3,081	3,736	3,962	4,261
Net charge-offs	(2,297)	(1,689)	(2,281)	(1,466)
Balance, end of period	$ 36,431	$ 26,237	$ 36,431	$ 26,237

Covered Portfolio	Three Months Ended June 30, 2014	Six Months Ended June 30, 2014
Balance, beginning of period	$ 2,665	$ 1,061
Provisions charged to operating expenses	1,450	3,304
Recoveries of covered loans previously charged off:		
Commercial and industrial		
Real estate		
Construction and land development		
Consumer		
Total recoveries		
Covered loans charged off:		
Commercial and industrial		91
Real estate		44
Construction and land development		115
Consumer		
Total charge-offs		250
Net charge-offs		(250)
Balance, end of period	$ 4,115	$ 4,115

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

	June 30, 2014		December 31, 2013	
Non-Covered Portfolio	Reserve	% of Gross Non-Covered Loans	Reserve	% of Gross Non-Covered Loans
Commercial and industrial	$ 18,062	45.27%	$ 16,865	46.58%
Real estate (including construction and land development)	18,084	53.25%	16,288	51.84%
Consumer	285	1.48%	88	1.58%
Total	$ 36,431	100.00%	$ 33,241	100.00%

	June 30, 2014	December 31, 2013
Covered Portfolio	Reserve	Reserve

			% of Gross Covered Loans			% of Gross Covered Loans
Commercial and industrial	$	1,146	5.92%	$	1,053	6.65%
Real estate (including construction and land development)		2,551	94.08%		8	93.35%
Consumer		418	0.00%			0.00%
Total	$	4,115	100.00%	$	1,061	100.00%

Potential Problem Loans

Potential problem loans consist of loans that are performing in accordance with contractual terms but for which management has concerns about the ability of an obligor to continue to comply with repayment terms because of the obligor's potential operating or financial difficulties. Management monitors these loans and reviews their performance on a regular basis. Potential problem loans contain potential weaknesses that could improve, persist or further deteriorate. If such potential weaknesses persist without improving, the loan is subject to downgrade, typically to substandard, in three to six months. Within our non-covered loan portfolio at June 30, 2014, we had nine credit relationships totaling $22.9 million of potential problem loans, which are assigned a grade of special mention within our risk grading matrix. At December 31, 2013, we had ten credit relationships totaling $24.7 million of non-covered potential problem loans. Within our covered loan portfolio at June 30, 2014, we had two credit relationship totaling $1.7 million of potential problem loans assigned a grade of special mention within our risk grading matrix, compared with two credit relationships totaling $3.3 million at December 31, 2013.

Non-Performing Assets

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

	June 30, 2014	December 31, 2013
Non-covered loans accounted for on a non-accrual basis:		
Commercial and industrial	$ 14,762	$ 16,730
Real estate	6,296	6,511
Construction and land development	863	112
Consumer		
	$ 21,921	$ 23,353
Non-covered non-performing loans as a percentage of total non-covered loans	0.43%	0.51%
Non-covered other real estate owned	$ 4,353	$ 4,805
Other repossessed assets	$ 1,719	$ 13
Non-covered non-performing assets	$ 27,993	$ 28,171
Non-covered non-performing assets as a percentage of total assets	0.30%	0.32%
Non-covered loans past due 90 days or more and still accruing	$ 1	$ 534

Troubled debt restructurings included in accruing non-covered loans	$ 406	$ 1,055

At June 30, 2014, total non-covered non-performing assets decreased $0.2 million to $28.0 million, compared with $28.2 million at December 31, 2013. Non-covered non-performing loans totaled $21.9 million at June 30, 2014 and $23.4 million at December 31, 2013. At June 30, 2014, non-covered non-accrual loans included 17 commercial and industrial relationships with loans of $12.0 million secured by accounts receivable, inventory, oil and gas properties, aircraft and life insurance, and a total of $1.5 million in lease financing receivables. Non-covered non-accrual loans at June 30, 2014 also included $6.3 million characterized as real estate loans, including two commercial real estate loan relationships of $0.5 million and loans secured by residential real estate of $5.8 million, $3.9 million of which were classified as loans held for sale, as well as construction and land development loans of $0.9 million. At December 31, 2013, non-covered non-accrual loans included five commercial and industrial relationships with loans of $14.0 million secured by accounts receivable, inventory, aircraft and life insurance, and a total of $1.0 million in lease financing receivables. Non-covered non-accrual loans at December 31, 2013 also included $6.5 million characterized as real estate loans, including three commercial real estate loan relationships of $2.5 million and loans secured by residential real estate of $3.5 million, substantially all of which were classified as loans held for sale, as well as construction and land development loans of $0.1 million.

Non-covered OREO decreased $0.4 million to $4.4 million at June 30, 2014, compared with $4.8 million at December 31, 2013. Changes in non-covered OREO included the disposal of seven properties totaling $2.4 million and the addition of five properties totaling $2.4 million. At June 30, 2014, non-covered OREO included commercial properties of $0.4 million, commercial real estate property consisting of parcels of unimproved land of $2.1 million and residential lots under development of $1.9 million. At December 31, 2013, non-covered OREO included commercial properties of $4.2 million, commercial real estate property consisting of parcels of unimproved land of $0.5 million and residential lots under development of $0.1 million.

At June 30, 2014, troubled debt restructurings ("TDRs") granted on non-covered loans totaled $10.3 million, of which $0.4 million relate to non-covered PCI loans that are considered to be performing due to the application of the accretion method and non-covered non-performing loans of $9.9 million for which discount accretion has been suspended. At December 31, 2013, TDRs granted on non-covered loans totaled $11.4 million. These TDRs were comprised of $1.1 million of non-covered PCI loans that are considered to be performing due to the application of the accretion method and non-covered non-performing loans of $10.3 million for which discount accretion has been suspended.

Non-covered loans past due 90 days or more and still accruing were de minimis at June 30, 2014, compared to a total of $0.5 million at December 31, 2013 that included secured commercial and industrial loans, and a real estate loan.

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

	June 30, 2014	December 31, 2013
Covered loans accounted for on a non-accrual basis:		
Commercial and industrial	$ 2,095	$ 973
Real estate	12,620	249
Construction and land development	1,919	575
Consumer		
	$ 16,634	$ 1,797
Covered non-performing loans as a percentage of total covered loans	1.97%	0.18%
Covered other real estate owned	$ 142,174	$ 142,833
Other repossessed assets	$	$
Covered non-performing assets	$ 158,808	$ 144,630
Covered non-performing assets as a percentage of total assets	1.69%	1.62%

Covered loans past due 90 days or more and still accruing	$ 272	$
Troubled debt restructurings included in accruing covered loans	$	$

At June 30, 2014, covered non-performing assets increased by $14.2 million to $158.8 million, compared with $144.6 million at December 31, 2013, primarily due to an increase in covered non-accrual loans of $14.8 million. Covered non-performing loans totaled $16.6 million at June 30, 2014 and $1.8 million at December 31, 2013. At June 30, 2014, covered non-performing loans included seven commercial and industrial relationships with loans of $1.0 million secured by accounts receivable and inventory, two commercial real estate loan relationships of $10.9 million, eleven residential real estate loan relationships of $1.7 million, as well as construction and land development loans of $1.9 million. At December 31, 2013, covered non-performing loans of $1.8 million included one commercial and industrial relationship with loans of $1.0 million secured by accounts receivable, inventory and equipment. Covered non-accrual loans at December 31, 2013 also included one commercial real estate loan relationship of $0.2 million, as well as construction and land development loans of $0.6 million.

OREO acquired in the FNB Transaction that is subject to the FDIC loss-share agreements is referred to as "covered OREO" and reported separately in our consolidated balance sheets. Covered OREO decreased $0.6 million to $142.2 million at June 30, 2014, compared with $142.8 million at December 31, 2013. The decrease was primarily due to the disposal of 125 properties totaling $34.7 million, partially offset by the addition of 87 properties totaling $34.5 million. At June 30, 2014, covered OREO included commercial properties of $93.9 million, commercial real estate property consisting of parcels of unimproved land of $21.4 million and residential lots under development of $26.9 million. At December 31, 2013, covered OREO included commercial properties of $90.5 million, commercial real estate property consisting of parcels of unimproved land of $21.4 million and residential lots under development of $30.9 million.

Covered loans past due 90 days or more and still accruing totaled $0.3 million at June 30, 2014 and included secured commercial and industrial loans, a construction and land development loan, and commercial and residential real estate loans.

Insurance Losses and Loss Adjustment Expenses

At June 30, 2014 and December 31, 2013, our reserves for unpaid losses and LAE were $35.1 million and $27.5 million, respectively. The liability for insurance losses and LAE represents estimates of the ultimate unpaid cost of all losses incurred, including losses for claims that have not yet been reported. Separately for each of NLIC and ASIC and each line of business, our actuaries estimate the liability for unpaid losses and LAE by first estimating ultimate losses and LAE amounts for each year, prior to recognizing the impact of reinsurance.

Insured losses for a given accident year change in value over time as additional information on claims is received, as claim conditions change and as new claims are reported. This process is commonly referred to as loss development. To project ultimate losses and LAE, our actuaries examine the paid and reported losses and LAE for each accident year and multiply these values by a loss development factor. The selected loss development factors are based upon a review of the loss development patterns indicated in the companies' historical loss triangles and applicable insurance industry loss development factors.

The reserve analysis performed by our actuaries provides preliminary central estimates of the unpaid losses and LAE. At each quarter-end, the results of the reserve analysis are summarized and discussed with our senior management. The senior management group considers many factors in determining the amount of reserves to record for financial statement purposes. These factors include the extent and timing of any recent catastrophic events, historical pattern and volatility of the actuarial indications, the sensitivity of the actuarial indications to changes in paid and reported loss patterns, the consistency of claims handling processes, the consistency of case reserving practices, changes in our pricing and underwriting, and overall pricing and underwriting trends in the insurance market.

Deposits

The banking segment's major source of funds and liquidity is its deposit base. Deposits provide funding for its investment in loans and securities. Interest paid for deposits must be managed carefully to control the level of interest expense and overall net interest margin. The composition of the deposit base (time deposits versus interest-bearing demand deposits and savings), as discussed in more detail within the section entitled "Liquidity and Capital Resources Banking Segment" below, is constantly changing due to the banking segment's needs and market conditions. Overall, average deposits totaled $6.5 billion for the six months ended June 30, 2014, an increase from average deposits of $4.7 billion for the six months ended June 30, 2013. The significant year-over-year increase in average deposits was primarily due to those deposits assumed as a part of the FNB Transaction. The table below presents the average balance of deposits and the average rate paid on those deposits (dollars in thousands).

	Six Months Ended June 30,				Year Ended December 31, 2013	
	2014		2013			
	Average Balance	Average Rate Paid	Average Balance	Average Rate Paid	Average Balance	Average Rate Paid
Noninterest-bearing demand deposits	$ 1,741,409	0.00%	$ 1,184,990	0.00%	$ 1,370,029	0.00%
Interest-bearing demand deposits	2,310,167	0.22%	1,813,333	0.25%	1,930,622	0.24%
Savings deposits	286,734	0.21%	179,302	0.36%	247,789	0.32%
Certificates of deposit	2,138,125	0.38%	1,475,567	0.59%	1,745,483	0.54%
	$ 6,476,435	0.21%	$ 4,653,192	0.30%	$ 5,293,923	0.28%

Borrowings

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

	June 30, 2014		December 31, 2013	
	Balance	Average Rate Paid	Balance	Average Rate Paid
Short-term borrowings	$ 1,187,193	0.32%	$ 342,087	0.36%
Notes payable	55,584	4.62%	56,327	6.33%
Junior subordinated debentures	67,012	3.52%	67,012	3.59%
	$ 1,309,789	0.97%	$ 465,426	2.10%

Short-term borrowings consist of federal funds purchased, securities sold under agreements to repurchase and short-term bank loans. The $845.1 million increase in short-term borrowings at June 30, 2014 compared with December 31, 2013 included increases of $750.0 million in borrowings at the FHLB, $68.2 million in federal funds purchased and $22.3 million in securities sold under agreements to repurchase. These increases were the result of higher funding requirements associated with the increase in our mortgage origination segment's balance on its warehouse line of credit with the Bank, a decrease in deposits, and a slight increase in loans. Notes payable at June 30, 2014 of $55.6 million is comprised of insurance segment term notes and nonrecourse notes owed by First Southwest.

Twelve months ended December 31, 2013, 2012 and 2011

Consolidated Operating Results

The income applicable to common stockholders for the year ended December 31, 2013 was $121.0 million, or $1.40 per diluted share, compared to losses applicable to common stockholders of $5.9 million, or $0.10 per diluted share for the year ended December 31, 2012, and $6.5 million, or $0.12 per diluted share, for the year ended December 31, 2011.

As a result of the PlainsCapital Merger on November 30, 2012, the net income of PlainsCapital is included in our operating results for the year ended December 31, 2013 and the month ended December 31, 2012. The operations acquired in the FNB Transaction are included in our operating results beginning September 14, 2013, and are therefore not fully reflected in our consolidated statement of operations for the year ended December 31, 2013. FNB's results of operations prior to September 14, 2013 are not included in our consolidated operating results. We expect the operations acquired in the FNB Transaction to have a significant effect on the Bank's operating results in future periods.

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The FNB Transaction was accounted for using the purchase method of accounting, and accordingly, purchased assets, including identifiable intangible assets and assumed liabilities, were recorded at their respective Bank Closing Date fair values using significant estimates and assumptions to value certain identifiable assets acquired and liabilities assumed. During the quarter ended December 31, 2013, the estimated fair values of certain identifiable assets acquired and liabilities assumed as of the Bank Closing Date were adjusted as a result of additional information obtained primarily related to the fair values of loans, covered OREO, amounts receivable under the loss-share agreements with the FDIC ("FDIC Indemnification Asset"), premises and equipment and other intangible assets. These adjustments resulted in a preliminary bargain purchase gain associated with the FNB Transaction during 2013 of $12.6 million, before taxes of $4.5 million, which is included within noninterest income. Due to the short time period between the Bank Closing Date and December 31, 2013, the real estate appraisal validation exercise remains outstanding and the Bank Closing Date valuations related to covered OREO and FDIC Indemnification Asset are considered preliminary and could differ significantly when finalized.

Certain items included in net income for 2012 and 2013 resulted from purchase accounting associated with the PlainsCapital Merger and FNB Transaction. Income before taxes for 2013 includes net accretion of $58.5 million and $10.2 million on earning assets and liabilities acquired in the PlainsCapital Merger and FNB Transaction, respectively, offset by amortization of identifiable intangibles of $9.8 million and $0.3 million, respectively. Loss before taxes for 2012 includes net accretion of $5.9 million on earning assets and liabilities acquired in the PlainsCapital Merger and amortization of identifiable intangibles of $0.8 million.

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

	Year ended December 31, 2013
Performance Ratios(1):	
Return on average stockholders' equity	10.48%
Return on average assets	1.66%
Net interest margin (taxable equivalent)(2)	4.47%

(1) Noted measures are typically used for measuring the performance of banking and financial institutions. Our operations prior to the acquisition of PlainsCapital are limited to our insurance operations. Therefore, noted measures for periods prior to 2013 are not useful measures and have been excluded.

(2) Taxable equivalent net interest income divided by average interest-earning assets.

During the year ended December 31, 2013, the consolidated taxable equivalent net interest margin of 4.47% was impacted by PlainsCapital Merger related accretion of discount on loans of $61.8 million, amortization of premium on acquired securities of $5.7 million and amortization of premium on acquired time deposits of $2.4 million. Additionally, FNB Transaction related accretion of discount on loans of $7.5 million and amortization of premium on acquired time deposits of $2.7 million also impacted the consolidated taxable equivalent net interest margin during the year ended December 31, 2013. These items increased the consolidated taxable equivalent net interest margin by 103 basis points for the year ended December 31, 2013. The consolidated taxable equivalent net interest margin was 4.64% for the month ended December 31, 2012. The taxable equivalent net interest margin was impacted by PlainsCapital Merger related accretion of discount on loans of $6.3 million, amortization of premium on acquired securities of $0.7 million and amortization of premium on acquired time deposits of $0.4 million. These items increased the consolidated taxable equivalent interest margin by 110 basis points for the month ended December 31, 2012.

The table below provides additional details regarding our consolidated net interest income (dollars in thousands). Our operations prior to the PlainsCapital Merger were limited to our insurance operations. Therefore, the consolidated net interest income for 2012 reflects details for the month ended December 31, 2012.

	Year Ended December 31, 2013			Month Ended December 31, 2012		
	Average Outstanding Balance	**Interest Earned or Paid**	**Annualized Yield or Rate**	**Average Outstanding Balance**	**Interest Earned or Paid**	**Annualized Yield or Rate**
Assets						
Interest-earning assets						
Loans, gross(1)	$ 4,584,079	$ 284,782	6.21%	$ 4,513,214	$ 23,900	6.21%
Investment securities taxable	993,389	27,078	2.72%	719,910	1,604	2.63%
Investment securities non-taxable(2)	192,933	7,150	3.71%	230,733	698	2.51%
Federal funds sold and securities purchased under agreements to resell	27,996	113	0.40%	54,017	106	2.35%
Interest-bearing deposits in other financial institutions	727,284	1,848	0.25%	574,913	80	0.25%
Other	160,320	10,479	6.58%	159,181	651	4.84%
Interest-earning assets, gross	6,686,001	331,450	4.96%	6,251,968	27,039	5.04%
Allowance for loan losses	(22,906)			(159)		
Interest-earning assets, net	6,663,095			6,251,809		
Noninterest-earning assets	986,272			747,284		
Total assets	$ 7,649,367			$ 6,999,093		
Liabilities and Stockholders' Equity						
Interest-bearing liabilities						
Interest-bearing deposits	$ 3,923,894	$ 14,877	0.38%	$ 3,233,503	$ 1,013	0.37%
Notes payable and other borrowings	823,477	17,997	2.19%	1,048,114	1,351	1.51%
Total interest-bearing liabilities	4,747,371	32,874	0.69%	4,281,617	2,364	0.65%
Noninterest-bearing liabilities						
Noninterest-bearing deposits	1,370,029			1,321,011		
Other liabilities	335,362			498,375		
Total liabilities	6,452,762			6,101,003		
Stockholders' equity	1,195,961			896,567		
Noncontrolling interest	644			1,523		
Total liabilities and stockholders' equity	$ 7,649,367			$ 6,999,093		
Net interest income(2)		$ 298,576			$ 24,675	

Net interest spread(2)	4.27%	4.39%
Net interest margin(2)	4.47%	4.64%

(1) Average balance includes non-accrual loans.

(2) Taxable equivalent adjustments are based on a 35% tax rate. The adjustment to interest income was $2.4 million and $0.2 million for the year ended December 31, 2013 and the month ended December 31, 2012, respectively.

On a consolidated basis, net interest income increased $267.4 million during 2013, compared with 2012, while net interest income increased $26.8 million during 2012, compared with 2011. These increases were primarily due to the inclusion of the results of operations of the banking segment, which was acquired in the PlainsCapital Merger on November 30, 2012. Net interest income prior to December 2012 was limited to interest income on securities and interest expense on notes payable of the insurance segment.

The provision for loan losses is determined by management as the amount to be added to the allowance for loan losses after net charge-offs have been deducted to bring the allowance to a level which, in management's best estimate, is necessary to absorb probable losses within the existing loan portfolio. The consolidated provision for loan losses, primarily in the banking segment, was $37.2 million during 2013. During 2013, the provision for loan losses was comprised of charges relating to newly originated loans and acquired loans without credit impairment at acquisition of $33.1 million and purchased credit impaired ("PCI") loans of $4.1 million.

Consolidated noninterest income increased $625.9 million during 2013, compared with 2012, while consolidated noninterest income increased $82.6 million during 2012, compared with 2011. These increases were primarily due to the inclusion of $640.2 million and $68.5 million during the year ended December 31, 2013 and the month ended December 31, 2012, respectively, of noninterest income generated from the operations of the mortgage origination and financial advisory segments acquired in the PlainsCapital Merger. Consolidated noninterest income during 2013 also included an increase in net insurance premiums earned of $10.8 million, compared with 2012, and an increase of $12.7 million during 2012, compared with 2011. In addition, as previously discussed, the FNB Transaction resulted in the recognition of a preliminary pre-tax bargain purchase gain of $12.6 million during 2013.

Our consolidated noninterest expense during 2013 increased $656.2 million, compared with 2012, while consolidated noninterest expense during 2012 increased $100.3 million, compared with 2011. The increases primarily resulted from the inclusion of $739.7 million and $77.5 million during the year ended December 31, 2013 and month ended December 31, 2012, respectively, in employees' compensation and benefits, occupancy and equipment and other expenses specifically attributable to those segments acquired as a part of the PlainsCapital Merger. Included in employee's compensation and benefits expense during 2012 includes an $8.9 million expense related to the separate retention agreements between Hilltop and two executive officers of PlainsCapital entered into in connection with the PlainsCapital Merger. Other noninterest expenses during 2012 include PlainsCapital Merger related expenses of $6.6 million. The balance of increases in our consolidated noninterest expenses during 2013 and 2012 were primarily related to loss and LAE and policy acquisition and other underwriting expenses specific to our insurance segment.

Consolidated income tax expense during 2013 was $70.7 million, reflecting an effective rate of 35.8%. During 2012 and 2011, we recorded income tax benefits, due to losses from operations, of $1.1 million and $5.0 million, respectively, reflecting effective rates of 18.3% and 43.4%, respectively. The increase in income tax expense during 2013 was due to the operating income generated by our business segments. The effective income tax rates for 2012 and 2011 are not indicative of future effective income tax rates as a result of the PlainsCapital Merger.

Segment Results

Banking Segment

Income before income taxes in our banking segment for the year ended December 31, 2013 and the month ended December 31, 2012 was $172.1 million and $9.7 million, respectively, and was primarily driven by net interest income of $293.3 million and $24.9 million, respectively, partially offset by noninterest expenses of $155.1 million and $16.1 million, respectively.

At December 31, 2013, the Bank exceeded all regulatory capital requirements with a total capital to risk weighted assets ratio of 14.00%, Tier 1 capital to risk weighted assets ratio of 13.38% and a Tier 1 capital to average assets, or leverage, ratio of 9.29%. At December 31, 2013, the Bank was also considered to be "well-capitalized" under regulatory requirements without giving effect to the final Basel III capital rules adopted by the Federal Reserve Board on July 2, 2013. For additional discussion of the final Basel III capital rules, see "Information About the Companies Hilltop Business Government Supervision and Regulation PlainsCapital Bank Basel III."

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

	Year ended December 31, 2013
Performance Ratios(1):	
Efficiency ratio(2)	42.58%
Return on average assets	1.78%
Net interest margin (taxable equivalent)(3)	5.17%

(1) The banking segment was acquired on November 30, 2012. Therefore, noted measures for periods prior to 2013 are not useful measures and have been excluded.

(2) Noninterest expenses divided by the sum of total noninterest income and net interest income for the period.

(3) Taxable equivalent net interest income divided by average interest-earning assets.

During the year ended December 31, 2013, the banking segment's taxable equivalent net interest margin of 5.17% was impacted by PlainsCapital Merger related accretion of discount on loans of $61.8 million, amortization of premium on acquired securities of $5.7 million and amortization of premium on acquired time deposits of $2.4 million. Additionally, FNB Transaction related accretion of discount on loans of $7.5 million and amortization of premium on acquired time deposits of $2.7 million also impacted the banking segment's taxable equivalent net interest margin during the year ended December 31, 2013. These items increased the banking segment's taxable equivalent net interest margin by 120 basis points for the year ended December 31, 2013. The banking segment's taxable equivalent net interest margin for the month ended December 31, 2012 of 5.83% was impacted by PlainsCapital Merger related accretion of discount on loans of $6.3 million, amortization of premium on acquired securities of $0.7 million and amortization of premium on acquired time deposits of $0.4 million. These items increased the banking segment's taxable equivalent interest margin by 140 basis points for the month ended December 31, 2012.

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The table below provides additional details regarding our banking segment's net interest income (dollars in thousands).

	Year Ended December 31, 2013			Month Ended December 31, 2012		
	Average Outstanding Balance	Interest Earned or Paid	Annualized Yield or Rate	Average Outstanding Balance	Interest Earned or Paid	Annualized Yield or Rate
Assets						
Interest-earning assets						
Loans, gross(1)	$ 3,279,228	$ 238,314	7.27%	$ 2,886,549	$ 19,228	7.99%
Subsidiary warehouse lines of credit	947,064	51,114	5.40%	1,261,768	5,984	5.69%
Investment securities taxable	792,860	14,625	1.84%	494,285	444	1.08%
Investment securities non-taxable(2)	158,739	5,715	3.60%	175,850	479	3.27%
Federal funds sold and securities purchased under agreements to resell	26,373	75	0.28%	33,180	48	1.74%
Interest-bearing deposits in other financial institutions	494,220	1,319	0.27%	299,464	68	0.27%
Other	31,794	1,311	4.12%	33,594	57	2.04%
Interest-earning assets, gross	5,730,278	312,473	5.45%	5,184,690	26,308	6.09%
Allowance for loan losses	(22,752)			248		
Interest-earning assets, net	5,707,526			5,184,938		
Noninterest-earning assets	940,880			814,461		
Total assets	$ 6,648,406			$ 5,999,399		
Liabilities and Stockholders' Equity						
Interest-bearing liabilities						
Interest-bearing deposits	$ 3,900,867	$ 14,889	0.38%	$ 3,161,312	$ 1,009	0.38%
Notes payable and other borrowings	391,111	1,340	0.34%	560,572	123	0.26%
Total interest-bearing liabilities(3)	4,291,978	16,229	0.38%	3,721,884	1,132	0.36%
Noninterest-bearing liabilities						
Noninterest-bearing deposits	1,419,594			1,396,295		
Other liabilities	39,028			58,492		
Total liabilities	5,750,600			5,176,671		
Stockholders' equity	897,806			822,728		
Total liabilities and stockholders' equity	$ 6,648,406			$ 5,999,399		
Net interest income(2)		$ 296,244			$ 25,176	

Net interest spread(2)	5.07%	5.73%
Net interest margin(2)	5.17%	5.83%

(1) Average balance includes non-accrual loans.

(2) Taxable equivalent adjustments are based on a 35% tax rate. The adjustment to interest income was $2.0 million and $0.2 million for the year ended December 31, 2013 and the month ended December 31, 2012, respectively.

(3) Excludes the allocation of interest expense on PlainsCapital debt of $1.0 million and $0.1 million for the year ended December 31, 2013 and the month ended December 31, 2012, respectively.

The banking segment's net interest margin shown above exceeds our consolidated net interest margin. Our consolidated net interest margin includes the yields and costs associated with certain items within interest-earning assets and interest-bearing liabilities in the financial advisory segment, as well as the borrowing costs of Hilltop and PlainsCapital, both of which reduce our consolidated net interest margin. In addition, the banking segment's interest earning assets include lines of credit extended to subsidiaries, the yields on which increase the banking segment's net interest margin. Such yields and costs are eliminated from the consolidated financial statements.

Because the operations of the banking segment acquired in the PlainsCapital Merger are not included in our results of operations for the full fiscal year ended December 31, 2012, the table summarizing the changes in our net interest income due to variances in the volume of our interest-earning assets and interest-bearing liabilities would not be meaningful and has therefore been omitted.

The banking segment's noninterest income was $71.0 million and $4.6 million during the year ended December 31, 2013 and the month ended December 31, 2012, respectively, and primarily related to intercompany financing charges associated with the lending commitment on the PrimeLending warehouse line of credit. Noninterest income during the year ended December 31, 2013 also included the recognition of a preliminary pre-tax bargain purchase gain of $12.6 million in connection with the FNB Transaction.

The banking segment's noninterest expenses were $155.1 million and $16.1 million during the year ended December 31, 2013 and the month ended December 31, 2012, respectively, and were primarily comprised of employees' compensation and benefits, and occupancy expenses.

Mortgage Origination Segment

Income before income taxes in our mortgage origination segment for the year ended December 31, 2013 and the month ended December 31, 2012 was $27.4 million and $2.3 million, respectively. Income before income taxes was primarily driven by noninterest income of $537.5 million and $57.6 million during the year ended December 31, 2013 and the month ended December 31, 2012, respectively, partially offset by noninterest expense of $472.3 million and $50.3 million during the year ended December 31, 2013 and the month ended December 31, 2012, respectively. Additionally, net interest expense of $37.8 million and $5.0 million during the year ended December 31, 2013 and the month ended December 31, 2012, respectively, resulted from interest incurred on a warehouse line of credit held at the Bank as well as related intercompany financing costs, partially offset by interest income earned on loans held for sale.

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PrimeLending originates all of its mortgage loans through a retail channel. The following table provides certain details regarding our mortgage loan originations for the year ended December 31, 2013 (dollars in thousands).

	Volume	% of Total
Mortgage Loan Originations units	55,781	
Mortgage Loan Originations volume	$ 11,792,562	
Mortgage Loan Originations:		
Conventional	$ 7,505,437	63.65%
Government	3,465,078	29.38%
Jumbo	780,604	6.62%
Other	41,443	0.35%
	$ 11,792,562	100.00%
Home purchases	$ 8,178,970	69.36%
Refinancings	3,613,592	30.64%
	$ 11,792,562	100.00%
Texas	$ 2,660,810	22.56%
California	2,082,184	17.66%
North Carolina	618,802	5.25%
Virginia	466,531	3.96%
Florida	456,643	3.87%
Arizona	392,006	3.32%
Maryland	385,215	3.27%
Ohio	383,518	3.25%
Washington	360,100	3.05%
All other states	3,986,753	33.81%
	$ 11,792,562	100.00%

The mortgage lending business is subject to variables that can impact loan origination volume, including seasonal and interest rate fluctuations. Historically, we have typically experienced increased loan origination volume from purchases of homes during the spring and summer, when more people tend to move and buy or sell homes. An increase in mortgage interest rates tends to result in decreased loan origination volume from refinancings, while a decrease in mortgage interest rates tends to result in increased refinancings. Changes in interest rates have historically had a lesser impact on home purchases volume than on refinancing volume.

Beginning in May 2013 and continuing through the fourth quarter of 2013, mortgage interest rates increased at a pace that, along with other factors, resulted in a 21.2% decrease in the mortgage origination segment's total loan origination volume during the third and fourth quarters of 2013 when compared to the first and second quarters of 2013. Home purchases volume during the six months ended June 30, 2013 and December 31, 2013 was $4.0 billion and $4.2 billion, respectively, reflecting a 5.1% increase, while refinancing volume decreased from $2.6 billion (39.5% of total loan origination volume) to $1.0 billion (19.3% of total loan origination volume) between the same periods. Due to recent volatility in mortgage interest rates and uncertain consumer confidence, 2014 mortgage loan origination volume may vary from origination trends historically experienced by the mortgage origination segment.

While PrimeLending's total loan origination volume decreased 21.2% during the third and fourth quarters of 2013 compared to the first and second quarters of 2013, income before income taxes decreased 107.4% between the same periods ($29.6 million income compared to a $2.2 million loss). Income before income taxes decreased at a greater rate primarily because segment operating costs included in noninterest expenses, such as employee related (salaries and benefits), occupancy and administrative expenses, decreased at a lesser rate, approximately 4%, than loan origination volume decreased between the two periods. To address negative trends in loan origination volume resulting from changes in interest rates that began in May 2013, the mortgage origination segment reduced its non-origination employee headcount approximately 22% during the third and fourth quarters of 2013. Third quarter segment operating costs were not significantly impacted by the headcount reductions, because the decreases in employees' salaries and benefits resulting from the reductions were mostly offset by related severance expenses incurred during the quarter. Salaries and benefits expenses decreased approximately 9% between the third and fourth quarters, as the benefits of the headcount reductions in the third quarter of 2013 began to be realized. We are also engaged in other initiatives to reduce segment operating costs that were primarily responsible for the decrease of approximately 4% in non-employee related expenses between the third and fourth quarters noted above. We anticipate that we will begin to realize the full benefits of the employee reductions and the other cost savings initiatives during the first quarter of 2014. Also impacting the trend in income before taxes, to a lesser extent, was a decrease in loan revenue margins resulting from increased competition.

PrimeLending sells substantially all mortgage loans it originates to various investors in the secondary market, the majority servicing released. During the first and second quarters of 2013, PrimeLending retained servicing on approximately 8% of loans sold. This rate was increased to approximately 22% during the third and fourth quarters of 2013. The related mortgage servicing rights asset was valued at $20.1 million on $2.0 billion of serviced loan volume as of December 31, 2013, compared to a value of $2.1 million at December 31, 2012. All income related to retained servicing, including changes in the value of the mortgage servicing rights asset, is included in noninterest income.

Noninterest income of $537.5 million and $57.6 million for the year ended December 31, 2013 and the month ended December 31, 2012, respectively, was comprised of net gains on the sale of loans and other mortgage production income, and mortgage origination fees. As a result of increased competition, noninterest income decreased at a greater rate, 27.6%, during the third and fourth quarters of 2013 when compared to the first and second quarters of 2013 than the decrease in loan origination volume experienced during the same periods, which was 21.2%. Noninterest income during the year ended December 31, 2013 included $11.1 million of net losses resulting from changes in the fair value of the mortgage origination segment's interest rate lock commitments ("IRLCs") and loans held for sale, and the related activity associated with forward commitments used by PrimeLending to mitigate interest rate risk associated with its IRLCs and mortgage loans held for sale. The loss was primarily the result of a decrease in the volume of IRLCs and mortgage loans held for sale between December 31, 2012 and December 31, 2013.

Noninterest expenses were $472.3 million and $50.3 million for the year ended December 31, 2013 and the month ended December 31, 2012, respectively. Employees' compensation and benefits accounted for the majority of the noninterest expenses incurred. Compensation that varies with the volume of mortgage loan originations and overall segment profitability comprised approximately 59% of the total employees' compensation and benefits expenses during the year ended December 31, 2013. PrimeLending records unreimbursed closing costs when it pays a customer's closing costs in return for the customer choosing to accept a higher interest rate on the customer's mortgage loan. Unreimbursed closing costs during the year ended December 31, 2013 and the month ended December 31, 2012 were $30.1 million and $5.9 million, respectively.

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Between January 1, 2005, and December 31, 2013, the mortgage origination segment sold mortgage loans totaling $55.5 billion. These loans were sold under sales contracts that generally include provisions which hold the mortgage origination segment responsible for errors or omissions relating to its representations and warranties that loans sold meet certain requirements, including representations as to underwriting standards and the validity of certain borrower representations in connection with the loan. In addition, the sales contracts typically require the refund of purchased servicing rights plus certain investor servicing costs if a loan experiences an early payment default. While the mortgage origination segment sold loans prior to 2005, it has not experienced, nor does it anticipate experiencing, significant losses on loans originated prior to 2005 as a result of investor claims under these provisions of its sales contracts.

When an investor claim for indemnification of a loan sold is made, we evaluate the claim and determine if the claim can be satisfied through additional documentation or other deliverables. If the claim cannot be satisfied in that manner, we negotiate with the investor to reach a settlement of the claim. Settlements typically result in either the repurchase of a loan or reimbursement to the investor for losses incurred on the loan. The following table summarizes the mortgage origination segment's claims resolution activity relating to loans sold between January 1, 2005, and December 31, 2013 (dollars in thousands).

	Original Loan Balance		Loss Recognized	
	Amount	% of Loans Sold	Amount	% of Loans Sold
Claims resolved with no payment	$ 130,917	0.24%	$	0.00%
Claims resolved as a result of a loan repurchase or payment to an investor for losses incurred(1)	172,006	0.31%	21,929	0.04%
	$ 302,923	0.55%	$ 21,929	0.04%

(1) Losses incurred include refunded purchased servicing rights.

At December 31, 2013 and 2012, the mortgage origination segment's indemnification liability reserve totaled $21.1 million and $19.0 million, respectively. The related provision for indemnification losses was $3.5 million and $0.4 million for the year ended December 31, 2013 and the month ended December 31, 2012, respectively.

Insurance Segment

Income before income taxes in our insurance segment was $7.6 million during 2013, compared with a loss before income taxes of $4.7 million during 2012 and income before income taxes of $0.2 million during 2011. Included within noninterest income of the insurance segment during 2013 is the recognition of a non-recurring gain of $3.7 million. This non-recurring gain, which is eliminated upon consolidation, is due to our redemption during the fourth quarter of 2013 of $6.9 million in aggregate principal amount of 7.50% Senior Exchangeable Notes due 2025 (the "Notes") of HTH Operating Partnership LP ("OP"), a wholly owned subsidiary of Hilltop, which were held by our insurance subsidiaries. The insurance segment is subject to claims arising out of severe weather, the incidence and severity of which are inherently unpredictable. Generally, the insurance segment's insured risks exhibit higher losses in the second and third calendar quarters due to a seasonal concentration of weather-related events in its primary geographic markets. Although weather-related losses (including hail, high winds, tornadoes and hurricanes) can occur in any calendar quarter, the second calendar quarter, historically, has experienced the highest frequency of losses associated with these events. Hurricanes, however, are more likely to occur in the third calendar quarter of the year.

The insurance segment had positive results during 2013, despite experiencing three tornado, wind and hail storms during the second quarter of 2013. Based on estimates of the ultimate cost, two of these storms are now considered catastrophic losses as they exceeded our $8.0 million reinsurance retention during the third quarter of 2013. The estimate of ultimate losses from these storms totaled $26.5 million at December 31, 2013 with a net loss, after reinsurance, of $22.1 million during 2013. These net costs compare favorably to the prior year given our improved containment of expected losses from the weather events in May 2013 at June 30, 2013 compared to prior year activity. This year-over-year improvement contributed to a combined ratio of 102.6% during 2013, compared with 108.8% and 106.2% during 2012 and 2011, respectively. The 6.2% decrease in the combined ratio in 2013 compared to 2012 was primarily driven by the increase in earned premiums and improved containment of expected losses as previously noted. The 2.6% increase in the combined ratio in 2012 compared to 2011 was primarily driven by higher incurred losses associated with wind and hail losses and storms that occurred in Texas during 2012 compared to the prior year, offset slightly by the increase in earned premiums. The combined ratio is a measure of overall insurance underwriting profitability, and represents the sum of the loss and LAE ratio and the underwriting expense ratio, which are discussed in more detail below.

Noninterest income of $166.2 million, $154.1 million and $141.7 million during 2013, 2012 and 2011, respectively, included net insurance premiums earned of $157.5 million, $146.7 million and $134.0 million, respectively. The increases in earned premiums are primarily attributable to volume and, to a lesser extent, rate increases in homeowners and mobile home products.

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

	Year Ended December 31,			Variance	
	2013	**2012**	**2011**	**2013 vs 2012**	**2012 vs 2011**
Direct Insurance Premiums Written:					
Homeowners	$ 79,711	$ 73,943	$ 70,177	$ 5,768	$ 3,766
Fire	54,566	51,345	49,812	3,221	1,533
Mobile Home	34,940	30,123	26,353	4,817	3,770
Commercial	4,489	8,043	8,380	(3,554)	(337)
Other	276	326	332	(50)	(6)
	$ 173,982	$ 163,780	$ 155,054	$ 10,202	$ 8,726

Total direct insurance premiums written for Hilltop's three largest insurance product lines increased by $13.8 million during 2013, compared to 2012, and by $9.1 million during 2012, compared to 2011. These increases were due to growth in Hilltop's core insurance products, partially offset by decreases of $3.5 million and $0.3 million in 2013 and 2012, respectively, related to a commercial product line that was non-renewed.

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

	Year Ended December 31,			Variance	
	2013	2012	2011	2013 vs 2012	2012 vs 2011
Net Insurance Premiums Earned:					
Homeowners	$ 72,175	$ 66,233	$ 60,671	$ 5,942	$ 5,562
Fire	49,407	45,990	43,063	3,417	2,927
Mobile Home	31,636	26,982	22,783	4,654	4,199
Commercial	4,065	7,204	7,244	(3,139)	(40)
Other	250	292	287	(42)	5
	$ 157,533	$ 146,701	$ 134,048	$ 10,832	$ 12,653

Net insurance premiums earned during 2013 and 2012 increased compared to 2012 and 2011, respectively, primarily due to the increases in net insurance premiums written of $13.0 million and $8.7 million in 2013 and 2012, respectively. These increases were offset by increases in unearned insurance premiums of $2.1 million and $3.9 million during 2013 and 2012, respectively, in each case as compared to the prior year.

Noninterest expenses of $166.0 million, $163.6 million and $146.4 million during 2013, 2012 and 2011, respectively, include both loss and LAE expenses and policy acquisition and other underwriting expenses, as well as other noninterest expenses. Loss and LAE are recognized based on formula and case basis estimates for losses reported with respect to direct business, estimates of unreported losses based on past experience and deduction of amounts for reinsurance placed with reinsurers. Loss and LAE during 2013 was $110.8 million, as compared to $109.2 million and $96.7 million during 2012 and 2011, respectively. As a result, the loss and LAE ratio during 2013, 2012 and 2011 was 70.3%, 74.4% and 72.2%, respectively. The ratio improvement during 2013, compared to 2012, was primarily a result of growth of earned premium and the improved containment of expected losses from the prior year weather events as previously discussed. The increase in the loss and LAE ratio during 2012, compared to 2011, was primarily due to increased severity of wind and hail storms from April, May and June 2012 weather events, partially offset by earned premium growth.

We seek to generate underwriting profitability through our insurance segment. Management evaluates NLC's loss and LAE ratio by bifurcating the losses to derive catastrophic and non-catastrophic loss ratios. The non-catastrophic loss ratio excludes Property Claims Services events that exceed $1.0 million of losses to NLC. Catastrophic events, including those that do not exceed our reinsurance retention, affect insurance segment loss ratios. During 2013, catastrophic events that did not exceed our reinsurance retention accounted for $22.3 million of the total loss and loss adjustment expense, as compared to $23.3 million and $20.3 million during 2012 and 2011, respectively. Excluding catastrophic events, our combined ratios during 2013, 2012 and 2011 would have improved by 14.3%, 15.8% and 15.2%, respectively.

Policy acquisition and other underwriting expenses encompass all expenses incurred relative to NLC operations, and include elements of multiple categories of expense otherwise reported as noninterest expense in the consolidated statements of operations. Included in other underwriting expenses during 2012 is a $1.7 million write down of a policy administration system NLC was unable to successfully implement. Excluding this 2012 write down, the expense ratio during 2012 would have decreased by 1.1%.

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

	Year Ended December 31,			Variance	
	2013	2012	2011	2013 vs 2012	2012 vs 2011
Amortization of deferred policy acquisition costs	$ 40,592	$ 38,757	$ 34,755	$ 1,835	$ 4,002
Other underwriting expenses	12,859	13,829	12,670	(970)	1,159
Total	53,451	52,586	47,425	865	5,161
Agency expenses	(2,571)	(2,073)	(1,789)	(498)	(284)
Total less agency expenses	$ 50,880	$ 50,513	$ 45,636	$ 367	$ 4,877
Net insurance premiums earned	$ 157,533	$ 146,701	$ 134,048	$ 10,832	$ 12,653
Expense ratio	32.3%	34.4%	34.0%	-2.1%	0.4%

During 2013, the insurance segment initiated a review of the pricing of its primary products in each state of operation utilizing a consulting actuarial firm to supplement normal review processes. Rate filings have been made for certain products in several states for increases effective in 2014, and the process will continue through the remainder of its products and states in which it operates. Concurrently, business concentrations were reviewed and actions initiated, including cancellation of agents, non-renewal of policies and cessation of new business writing on certain products in problematic geographic areas. We expect that these actions will reduce the rate of premium growth for 2014 when compared with the patterns exhibited in prior years. However, we expect the reduced exposure to volatile weather to improve our loss experience during 2014.

Financial Advisory Segment

Income before income taxes in our financial advisory segment for the year ended December 31, 2013 and the month ended December 31, 2012 were $2.4 million and $0.9 million, respectively. Rising interest rates along with increased volatility in fixed income markets have resulted in reduced sales of fixed income securities to institutional customers, some trading losses on securities held to support those sales and reduction in financial advisory fee income.

The financial advisory segment had net interest income of $12.1 million and $1.2 million during the year ended December 31, 2013 and the month ended December 31, 2012, respectively, consisting of securities lending activity, customer margin loan balances and investment securities used to support sales, underwriting and other customer activities.

The majority of noninterest income for the year ended December 31, 2013 and the month ended December 31, 2012 of $102.7 million and $10.9 million, respectively, was generated from fees and commissions earned from investment advisory and securities brokerage activities of $93.1 million and $11.2 million, respectively. The financial advisory segment participates in programs in which it issues forward purchase commitments of mortgage-backed securities to certain clients and sells TBAs. Changes in the fair values of these derivative instruments during the year ended December 31, 2013 and the month ended December 31, 2012 produced net gains of $11.4 million and $0.2 million, respectively. Changes in the fair value of the financial advisory segment's trading portfolio, which is used to support sales, underwriting and other customer activities, produced losses of $1.8 million and $0.6 million during the year ended December 31, 2013 and the month ended December 31, 2012, respectively.

Noninterest expenses were $112.4 million and $11.1 million for the year ended December 31, 2013 and the month ended December 31, 2012, respectively. Employees' compensation and benefits and occupancy and equipment accounted for the majority of the costs incurred.

Corporate

Corporate includes certain activities not allocated to specific business segments. These activities include holding company financing and investing activities, and management and administrative services to support the overall operations of the Company including, but not limited to, certain executive management, corporate relations, legal, finance, and acquisition costs not allocated to business segments.

As a holding company, Hilltop's primary investment objectives are to preserve capital and have available cash resources to utilize in making acquisitions. Investment and interest income earned, primarily from available cash and available-for-sale securities, including our note receivable from SWS, were $6.6 million, $7.0 million and $4.3 million during 2013, 2012 and 2011, respectively.

Interest expense of $8.2 million, $7.0 million and $7.1 million during 2013, 2012 and 2011 was entirely due to interest costs associated with the Notes. During 2013, interest expense included the recognition of a non-recurring charge of $2.1 million due to the write-off of remaining unamortized loan origination fees associated with the Notes being called for redemption during the fourth quarter of 2013.

Noninterest expenses of $10.4 million, $14.5 million and $8.9 million during 2013, 2012 and 2011, respectively, primarily include compensation and benefits, professional fees and transaction costs associated with acquisition efforts. During 2013, noninterest expenses included the recognition of a non-recurring loss of $3.7 million associated with the Notes held by our insurance segment being called for redemption during the fourth quarter of 2013. This loss was eliminated in consolidation. In addition, noninterest expenses included $0.1 million, $6.4 million and $2.6 million of transaction costs associated with acquisition efforts during 2013, 2012 and 2011, respectively.

Financial Condition

The following discussion contains a more detailed analysis of our financial condition at December 31, 2013 as compared to 2012 and 2011.

Securities Portfolio

At December 31, 2013, investment securities consisted of securities of the U.S. Treasury, U.S. government and its agencies, obligations of municipalities and other political subdivisions, primarily in the State of Texas, mortgage-backed, corporate debt, and equity securities, a note receivable and a warrant. We have the ability to categorize investments as trading, available for sale, and held to maturity.

Our securities portfolio consists of two major components: trading securities and securities available for sale. Trading securities are bought and held principally for the purpose of selling them in the near term and are carried at fair value, marked to market through operations and held at the Bank and First Southwest. Securities that may be sold in response to changes in market interest rates, changes in securities' prepayment risk, increases in loan demand, general liquidity needs and other similar factors are classified as available for sale and are carried at estimated fair value, with unrealized gains and losses recorded in accumulated other comprehensive income (loss).

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

	December 31,		
	2013	2012	2011
Trading securities, at fair value	$ 58,846	$ 90,113	$
Securities available for sale, at fair value			
U.S. Treasury securities	43,528	7,185	
U.S. government agencies:			
Bonds	662,732	526,237	29,165
Residential mortgage-backed securities	60,087	18,893	12,652
Collateralized mortgage obligations	120,461	97,924	
Corporate debt securities	76,608	87,177	100,681
States and political subdivisions	156,835	175,759	
Commercial mortgage-backed securities	760	1,073	2,303
Equity securities	22,079	20,428	19,022
Note receivable	47,909	44,160	38,588
Warrant	12,144	12,117	21,789
Total securities portfolio	$ 1,261,989	$ 1,081,066	$ 224,200

We had a net unrealized loss of $53.7 million and net unrealized gains of $12.5 million and $21.5 million related to the available for sale investment portfolio at December 31, 2013, 2012 and 2011, respectively. The significant increase in the net unrealized loss position of our available for sale investment portfolio during 2013 was due to effects of an increase in market interest rates since May 2013 that resulted in a decrease in the fair value of our debt securities.

Banking Segment

The banking segment's securities portfolio plays a role in the management of our interest rate sensitivity and generates additional interest income. In addition, the securities portfolio is used to meet collateral requirements for public and trust deposits, securities sold under agreements to repurchase and other purposes. The available for sale securities portfolio serves as a source of liquidity. Historically, the Bank's policy has been to invest primarily in securities of the U.S. government and its agencies, obligations of municipalities in the State of Texas and other high grade fixed income securities to minimize credit risk. At December 31, 2013, the banking segment's securities portfolio of $1.0 billion was comprised of trading securities of $21.0 million and available for sale securities of $1.0 billion. The banking segment's portfolio at December 31, 2013 included available for sale securities acquired in connection with the FNB Transaction with a book value of $60.4 million, down from a book value of $286.3 million at the Bank Closing Date. Subsequent to the Bank Closing Date, securities acquired in the FNB Transaction with a book value of $223.5 million were either sold, matured or called. These additions to the Bank's balance sheet represent additional support for its liquidity needs.

Insurance Segment

Our insurance segment's primary investment objective is to preserve capital and manage for a total rate of return. NLC's strategy is to purchase securities in sectors that represent the most attractive relative value. Our insurance segment invests the premiums it receives from policyholders until they are needed to pay policyholder claims or other expenses. At December 31, 2013, the insurance segment's securities portfolio was comprised of $131.6 million in available for sale securities and $5.3 million of other investments included in other assets within the consolidated balance sheet.

Financial Advisory Segment

Our financial advisory segment holds securities to support sales, underwriting and other customer activities. Because FSC is a broker-dealer, it is required to carry its securities at fair value and record changes in the fair value of the portfolio in operations. Accordingly, FSC classifies its securities portfolio of $37.9 million at December 31, 2013 as trading.

Corporate

Available for sale securities of Hilltop at December 31, 2013 include the note receivable from, and warrant to purchase shares of SWS of $60.1 million, and equity securities of $9.0 million representing those shares of SWS common stock held by Hilltop.

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The following table sets forth the estimated maturities of securities, excluding trading and available for sale equity securities. Contractual maturities may be different (dollars in thousands, yields are tax-equivalent).

	December 31, 2013				
	One Year Or Less	One Year to Five Years	Five Years to Ten Years	Greater Than Ten Years	Total
U.S. government agencies:					
U.S. Treasury securities:					
Amortized cost	$ 25,705	$ 13,041	$ 4,938	$	$ 43,684
Fair value	25,712	13,014	4,802		43,528
Weighted average yield	0.10%	0.91%	2.65%		0.63%
Bonds:					
Amortized cost	89,697	12,249	26,524	589,439	717,909
Fair value	89,706	12,654	26,338	534,034	662,732
Weighted average yield	0.36%	2.67%	2.71%	1.94%	1.78%
Residential mortgage-backed securities:					
Amortized cost		24,415	14,145	21,376	59,936
Fair value		24,595	14,205	21,287	60,087
Weighted average yield		2.63%	3.93%	4.00%	3.42%
Collateralized mortgage obligations:					
Amortized cost	7,344	76,382	26,852	13,924	124,502
Fair value	7,419	74,376	24,697	13,969	120,461
Weighted average yield	2.54%	1.65%	1.48%	4.45%	1.98%
Corporate debt securities:					
Amortized cost	4,248	40,201	27,011	916	72,376
Fair value	4,278	43,825	27,590	915	76,608
Weighted average yield	3.72%	4.74%	3.66%	6.22%	4.30%
States and political subdivisions:					
Amortized cost	700	5,303	13,309	143,643	162,955
Fair value	720	5,349	13,162	137,604	156,835
Weighted average yield	5.57%	2.86%	2.92%	3.76%	3.67%
Commercial mortgage-backed securities:					
Amortized cost				691	691
Fair value				760	760
Weighted average yield				6.08%	6.08%
Note receivable:					
Amortized cost		42,674			42,674
Fair value		47,909			47,909
Weighted average yield		10.25%			10.25%
Warrant:					
Amortized cost		12,068			12,068
Fair value		12,144			12,144
Weighted average yield		0.61%			0.61%
Total securities portfolio:					
Amortized cost	127,694	226,333	112,779	769,989	1,236,795
Fair value	127,835	233,866	110,794	708,569	1,181,064
Weighted average yield	0.58%	3.91%	2.82%	2.39%	2.52%

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Non-Covered Loan Portfolio

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

December 31, 2013	Loans, excluding PCI Loans	PCI Loans	Total Loans
Commercial and industrial	$ 1,600,450	$ 36,816	$ 1,637,266
Real estate	1,418,003	39,250	1,457,253
Construction and land development	344,734	19,817	364,551
Consumer	51,067	4,509	55,576
Non-covered loans, gross	3,414,254	100,392	3,514,646
Allowance for loan losses	(30,104)	(3,137)	(33,241)
Non-covered loans, net of allowance	$ 3,384,150	$ 97,255	$ 3,481,405

December 31, 2012	Loans, excluding PCI Loans	PCI Loans	Total Loans
Commercial and industrial	$ 1,588,907	$ 71,386	$ 1,660,293
Real estate	1,122,667	62,247	1,184,914
Construction and land development	247,413	33,070	280,483
Consumer	26,629	77	26,706
Non-covered loans, gross	2,985,616	166,780	3,152,396
Allowance for loan losses	(3,409)		(3,409)
Non-covered loans, net of allowance	$ 2,982,207	$ 166,780	$ 3,148,987

Banking Segment

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

The banking segment's total non-covered loans, net of the allowance for non-covered loan losses, were $4.3 billion and $4.1 billion at December 31, 2013 and 2012, respectively. The banking segment's non-covered loan portfolio includes a $1.3 billion warehouse line of credit extended to PrimeLending, of which $1.0 billion was drawn at December 31, 2013, as well as term loans to First Southwest that had an outstanding balance of $23.0 million at December 31, 2013. Amounts advanced against the warehouse line of credit and the First Southwest term loans are eliminated from net loans on our consolidated balance sheets. Prior to September 2013, the warehouse line of credit extended to PrimeLending had $1.6 billion of availability, of which $1.3 billion was drawn at December 31, 2012, while the outstanding balance on a term loan to First Southwest was $4.0 million at December 31, 2012.

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The banking segment does not generally participate in syndicated loan transactions and has no foreign loans in its portfolio. At December 31, 2013, the banking segment's only non-covered loan concentration (loans to borrowers engaged in similar activities) that exceeded 10% of its total non-covered loans was non-construction residential real estate loans within our non-covered real estate portfolio. At December 31, 2013, non-construction residential real estate loans were 41.27% of the banking segment's total non-covered loans. The banking segment's non-covered loan concentrations were within regulatory requirements at December 31, 2013.

Mortgage Origination Segment

The loan portfolio of the mortgage origination segment consists of loans held for sale, primarily single-family residential mortgages funded through PrimeLending, and pipeline loans, which are loans in various stages of the application process, but not yet closed and funded. Pipeline loans may not close if potential borrowers elect in their sole discretion not to proceed with the loan application. Total loans held for sale were $1.1 billion and $1.4 billion at December 31, 2013 and 2012, respectively.

The components of the mortgage origination segment's loans held for sale and pipeline loans are as follows (in thousands).

	December 31,	
	2013	**2012**
Loans held for sale:		
Unpaid principal balance	$ 1,066,850	$ 1,359,829
Fair value adjustment	21,555	40,908
	$ 1,088,405	$ 1,400,737
Pipeline loans:		
Unpaid principal balance	$ 602,467	$ 968,083
Fair value adjustment	12,151	15,150
	$ 614,618	$ 983,233

Financial Advisory Segment

The loan portfolio of the financial advisory segment consists primarily of margin loans to customers and correspondents. These loans are collateralized by the securities purchased or by other securities owned by the clients and, because of collateral coverage ratios, are believed to present minimal collectability exposure. Additionally, these loans are subject to a number of regulatory requirements as well as FSC's internal policies. The financial advisory segment's total non-covered loans, net of the allowance for non-covered loan losses, were $281.6 million and $277.0 million at December 31, 2013 and 2012, respectively. This increase was primarily attributable to increased borrowings in margin accounts held by FSC customers and correspondents.

Covered Loan Portfolio

Banking Segment

Loans acquired in the FNB Transaction that are subject to loss-share agreements with the FDIC are referred to as "covered loans" and reported separately in our consolidated balance sheets. Under the terms of the loss-share agreements, the FDIC has agreed to reimburse the Bank for: (i) 80% of losses on the first $240.4 million of losses incurred; (ii) 0% of losses in excess of $240.4 million up to and including $365.7 million of losses incurred; and (iii) 80% of losses in excess of $365.7 million of losses incurred. The loss-share agreements for commercial and single family residential loans are in effect for 5 years and 10 years, respectively, and the loss recovery provisions to the FDIC are in effect

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for 8 years and 10 years, respectively, from the Bank Closing Date. In accordance with the loss-share agreements, the Bank may be required to make a "true-up" payment to the FDIC approximately ten years following the Bank Closing Date if the FDIC's initial estimate of losses on covered assets is greater than the actual realized losses. The "true-up" payment is calculated using a defined formula set forth in the P&A Agreement.

In connection with the FNB Transaction, the Bank acquired loans both with and without evidence of credit quality deterioration since origination. Based on purchase date valuations, the banking segment's portfolio of acquired covered loans had a fair value of $1.1 billion as of the Bank Closing Date, with no carryover of any allowance for loan losses.

Covered loans held for investment at December 31, 2013 are detailed in the table below and classified by portfolio segment (in thousands).

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

At December 31, 2013, the banking segment had covered loan concentrations (loans to borrowers engaged in similar activities) that exceeded 10% of total covered loans in its real estate portfolio. The areas of concentration within our covered real estate portfolio were construction and land development loans, non-construction residential real estate loans, and non-construction commercial real estate loans. At December 31, 2013, construction and land development loans, non-construction residential real estate loans, and non-construction commercial real estate loans were 21.98%, 28.63% and 36.67%, respectively, of the banking segment's total covered loans. The banking segment's covered loan concentrations were within regulatory requirements at December 31, 2013.

Loan Portfolio Maturities

Banking Segment

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

	December 31, 2013			
	Due Within One Year	Due From One To Five Years	Due After Five Years	Total
Commercial and industrial	$ 1,928,236	$ 413,160	$ 98,996	$ 2,440,392
Real estate (including construction and land development)	437,650	903,358	1,421,425	2,762,433
Total	$ 2,365,886	$ 1,316,518	$ 1,520,421	$ 5,202,825
Fixed rate loans	$ 2,169,850	$ 1,243,462	$ 1,332,608	$ 4,745,920

Floating rate loans	196,036	73,056	187,813	456,905
Total	$ 2,365,886	$ 1,316,518	$ 1,520,421	$ 5,202,825

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

Allowance for Loan Losses

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

It is our management's responsibility at the end of each quarter, or more frequently as deemed necessary, to analyze the level of the allowance for loan losses to ensure that it is appropriate for the estimated credit losses in the portfolio consistent with the Interagency Policy Statement on the Allowance for Loan and Lease Losses and the Receivables and Contingencies Topics of the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC"). Estimated credit losses are the probable current amount of loans that we will be unable to collect given facts and circumstances as of the evaluation date. When management determines that a loan, or portion thereof, is uncollectible, the loan, or portion thereof, is charged-off against the allowance for loan losses, or for acquired loans accounted for in pools, charged against the pool discount. Recoveries on charge-offs that occurred prior to the PlainsCapital Merger represent contractual cash flows not expected to be collected and are recorded as accretion income. Recoveries on loans charged-off subsequent to the PlainsCapital Merger are credited to the allowance for loan loss, except for recoveries on loans accounted for in pools, which are credited to the pool discount.

We have developed a methodology that seeks to determine an allowance within the scope of the Receivables and Contingencies Topics of the ASC. Each of the loans that has been determined to be impaired is within the scope of the Receivables Topic. Impaired loans that are equal to or greater than $0.5 million are individually evaluated for impairment using one of three impairment measurement methods as of the evaluation date: (1) the present value of expected future discounted cash flows on the loan, (2) the loan's observable market price, or (3) the fair value of the collateral if the loan is collateral dependent. Specific reserves are provided in our estimate of the allowance based on the measurement of impairment under these three methods, except for collateral dependent loans, which require the fair value method. All non-impaired loans are within the scope of the Contingencies Topic. Estimates of loss for the Contingencies Topic are calculated based on historical loss experience by collateral type adjusted for changes in trends, conditions, and other relevant factors that affect repayment of loans as of the evaluation date. While historical loss experience provides a reasonable starting point for the analysis, historical losses, or recent trends in losses, are not the sole basis upon which to determine the appropriate level for the allowance for loan losses. Management considers recent qualitative or environmental factors that are likely to cause estimated credit losses associated with the existing portfolio to differ from historical loss experience, including but not limited to: changes in lending policies and procedures; changes in underwriting standards; changes in economic and business conditions and developments that affect the collectability of the portfolio; the condition of various market segments; changes in the nature and volume of the portfolio and in the terms of loans; changes in lending management and staff; changes in the volume and severity of past due loans, the volume of non-accrual loans, and the volume and severity of adversely classified or graded loans; changes in the loan review system; changes in the value of underlying collateral for collateral-dependent loans; and any concentrations of credit and changes in the level of such concentrations.

We design our loan review program to identify and monitor problem loans by maintaining a credit grading process, requiring that timely and appropriate changes are made to reviewed loans and coordinating the delivery of the information necessary to assess the appropriateness of the allowance

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for loan losses. Loans are evaluated for impaired status when: (i) payments on the loan are delayed, typically by 90 days or more (unless the loan is both well secured and in the process of collection), (ii) the loan becomes classified, (iii) the loan is being reviewed in the normal course of the loan review scope, or (iv) the loan is identified by the servicing officer as a problem. We review on an individual basis all loan relationships over $0.5 million that exhibit probable or observed credit weaknesses, the top 25 loan relationships by dollar amount in each market we serve, and additional relationships necessary to achieve adequate coverage of our various lending markets.

Homogeneous loans, such as consumer installment loans, residential mortgage loans and home equity loans, are not individually reviewed and are generally risk graded at the same levels. The risk grade and reserves are established for each homogeneous pool of loans based on the expected net charge-offs from current trends in delinquencies, losses or historical experience and general economic conditions. At December 31, 2013, we had no material delinquencies in these types of loans.

The allowance is subject to regulatory examination and determination as to adequacy, which may take into account such factors as the methodology used to calculate the allowance and the size of the allowance. While we believe we have an appropriate allowance for our existing non-covered and covered portfolios at December 31, 2013, additional provisions for losses on existing loans may be necessary in the future. Within our non-covered portfolio, we recorded net charge-offs in the amount of $6.3 million and $0.4 million for the year ended December 31, 2013 and the month ended December 31, 2012, respectively. Our allowance for non-covered loan losses totaled $33.2 million and $3.4 million at December 31, 2013 and 2012, respectively. The ratio of the allowance for non-covered loan losses to total non-covered loans held for investment at December 31, 2013 and 2012 was 0.95% and 0.11%, respectively.

In connection with the PlainsCapital Merger and the FNB Transaction, we acquired loans both with and without evidence of credit quality deterioration since origination. PCI loans acquired in the PlainsCapital Merger are accounted for on an individual loan basis, while PCI loans acquired in the FNB Transaction are accounted for in pools as well as on an individual loan basis. We have established under our PCI accounting policy a framework to aggregate certain acquired loans into various loan pools based on a minimum of two layers of common risk characteristics for the purpose of determining their respective fair values as of their acquisition dates, and for applying the subsequent recognition and measurement provisions for income accretion and impairment testing. The common risk characteristics used for the pooling of the FNB PCI loans are risk grade and loan collateral type. The acquired loans were initially recorded at fair value with no carryover of any allowance for loan losses. Our allowance for covered loan losses totaled $1.1 million at December 31, 2013.

Provisions for loan losses are charged to operations to record the total allowance for loan losses at a level deemed appropriate by the banking segment's management based on such factors as the volume and type of lending it conducted, the amount of non-performing loans and related collateral security, the present level of the allowance for loan losses, the results of recent regulatory examinations, generally accepted accounting principles, general economic conditions and other factors related to the ability to collect loans in its portfolio. The provision for loan losses, primarily in the banking segment, was $37.2 million and $3.8 million for the year ended December 31, 2013 and the month ended December 31, 2012, respectively.

The following tables present the activity in our allowance for loan losses within our non-covered and covered loan portfolios for the periods presented (in thousands). Substantially all of the activity

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shown below occurred within the banking segment, which was acquired as a part of the PlainsCapital Merger.

Non-Covered Portfolio	Year Ended December 31, 2013	Month Ended December 31, 2012
Balance, beginning of period	$ 3,409	$
Provisions charged to operating expenses	36,093	3,800
Recoveries of non-covered loans previously charged off:		
Commercial and industrial	3,439	
Real estate	282	
Construction and land development	265	
Consumer	61	
Total recoveries	4,047	
Non-covered loans charged off:		
Commercial and industrial	9,359	391
Real estate	209	
Construction and land development	524	
Consumer	216	
Total charge-offs	10,308	391
Net charge-offs	(6,261)	(391)
Balance, end of period	$ 33,241	$ 3,409

Covered Portfolio	Year Ended December 31, 2013
Balance, beginning of period	$
Provisions charged to operating expenses	1,065
Recoveries of covered loans previously charged off:	
Commercial and industrial	
Real estate	
Construction and land development	
Consumer	
Total recoveries	
Covered loans charged off:	
Commercial and industrial	4
Real estate	
Construction and land development	

Consumer		
Total charge-offs		4
Net charge-offs		(4)
Balance, end of period	$	1,061

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

	December 31,			
	2013		2012	
Non-Covered Portfolio	**Reserve**	**% of Gross Non-Covered Loans**	**Reserve**	**% of Gross Non-Covered Loans**
Commercial and industrial	$ 16,865	46.58%	$ 1,845	52.67%
Real estate (including construction and land development)	16,288	51.84%	1,559	46.48%
Consumer	88	1.58%	5	0.85%
Total	$ 33,241	100.00%	$ 3,409	100.00%

	December 31, 2013	
Covered Portfolio	**Reserve**	**% of Gross Covered Loans**
Commercial and industrial	$ 1,053	6.65%
Real estate (including construction and land development)	8	93.35%
Consumer		0.00%
Total	$ 1,061	100.00%

Potential Problem Loans

Potential problem loans consist of loans that are performing in accordance with contractual terms but for which management has concerns about the ability of an obligor to continue to comply with repayment terms because of the obligor's potential operating or financial difficulties. Management monitors these loans and reviews their performance on a regular basis. Potential problem loans contain potential weaknesses that could improve, persist or further deteriorate. If such potential weaknesses persist without improving, the loan is subject to downgrade, typically to substandard, in three to six months. Within our non-covered loan portfolio at December 31, 2013, we had ten credit relationships totaling $24.7 million of potential problem loans, which are assigned a grade of special mention within our risk grading matrix. At December 31, 2012, we had four credit relationships totaling $2.7 million of non-covered potential problem loans.

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Non-Performing Assets

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

	December 31, 2013	December 31, 2012
Non-covered loans accounted for on a non-accrual basis:		
Commercial and industrial	$ 16,730	$
Real estate	6,511	1,756
Construction and land development	112	
Consumer		
	$ 23,353	$ 1,756
Non-covered non-performing loans as a percentage of total non-covered loans	0.51%	0.04%
Non-covered other real estate owned	$ 4,805	$ 11,098
Other repossessed assets	$ 13	$ 557
Non-covered non-performing assets	$ 28,171	$ 13,411
Non-covered non-performing assets as a percentage of total assets	0.32%	0.18%
Non-covered loans past due 90 days or more and still accruing	$ 534	$ 2,000
Troubled debt restructurings included in accruing non-covered loans	$ 1,055	$

At December 31, 2013, total non-covered non-performing assets increased $14.8 million to $28.2 million, compared with $13.4 million at December 31, 2012, primarily due to an increase in non-covered non-accrual PCI loans of $15.8 million. Non-covered non-performing loans totaled $23.4 million at December 31, 2013 and $1.8 million at December 31, 2012. At December 31, 2013, non-covered non-accrual loans included five commercial and industrial relationships with loans totaling $14.0 million secured by accounts receivable, inventory, aircraft and life insurance, and a total of $1.0 million in lease financing receivables. Non-covered non-accrual loans at December 31, 2013 also included $6.5 million characterized as real estate loans, including three commercial real estate loan relationships totaling $2.5 million and loans secured by residential real estate totaling $3.5 million, substantially all of which were classified as loans held for sale, as well as construction and land development loans of $0.1 million. At December 31, 2012, non-covered non-accrual loans of $1.8 million included real estate loans secured by residential real estate and classified as loans held for sale.

Non-covered OREO decreased $6.3 million to $4.8 million at December 31, 2013, compared with $11.1 million at December 31, 2012. The decrease was primarily due to the disposal of two properties totaling $5.7 million. At December 31, 2013, non-covered OREO included commercial properties of $4.2 million, commercial real estate property consisting of parcels of unimproved land of $0.5 million and residential lots under development of $0.1 million. At December 31, 2012, non-covered OREO included commercial properties of $6.8 million, commercial real estate property consisting of parcels of unimproved land of $3.1 million and residential lots under development of $1.2 million.

At December 31, 2013, troubled debt restructurings ("TDRs") granted on non-covered loans totaled $11.4 million. These TDRs were comprised of $1.1 million of non-covered PCI loans that are considered to be performing due to the application of the accretion method and non-covered non-performing loans of $10.3 million for which discount accretion has been suspended. There were no troubled debt restructurings granted on non-covered loans at December 31, 2012.

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Non-covered loans past due 90 days or more and still accruing totaled $0.5 million and $2.0 million at December 31, 2013 and 2012, respectively, and included secured commercial and industrial loans, and a real estate loan.

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

Covered Portfolio		
Covered loans accounted for on a non-accrual basis:		
Commercial and industrial	$	973
Real estate		249
Construction and land development		575
Consumer		
	$	1,797
Covered non-performing loans as a percentage of total covered loans		0.18%
Covered other real estate owned	$	142,833
Other repossessed assets	$	
Covered non-performing assets	$	144,630
Covered non-performing assets as a percentage of total assets		1.62%
Covered loans past due 90 days or more and still accruing	$	
Troubled debt restructurings included in accruing covered loans	$	

At December 31, 2013, covered non-performing assets totaled $144.6 million. Covered non-performing loans of $1.8 million at December 31, 2013 included one commercial and industrial relationship with loans totaling $1.0 million secured by accounts receivable, inventory and equipment. Covered non-accrual loans at December 31, 2013 also included one commercial real estate loan relationship totaling $0.2 million, as well as construction and land development loans of $0.6 million.

OREO acquired in the FNB Transaction that is subject to the FDIC loss-share agreements is referred to as "covered OREO" and reported separately in our consolidated balance sheets. At December 31, 2013, covered OREO was $142.8 million and included commercial properties of $90.5 million, commercial real estate property consisting of parcels of unimproved land of $21.4 million and residential lots under development of $30.9 million.

Insurance Losses and Loss Adjustment Expenses

At December 31, 2013 and 2012, our reserves for unpaid losses and LAE were $27.5 million and $34.0 million, respectively. The liability for insurance losses and LAE represents estimates of the ultimate unpaid cost of all losses incurred, including losses for claims that have not yet been reported. Separately for each of NLIC and ASIC and each line of business, our actuaries estimate the liability for unpaid losses and LAE by first estimating ultimate losses and LAE amounts for each year, prior to recognizing the impact of reinsurance.

Insured losses for a given accident year change in value over time as additional information on claims is received, as claim conditions change and as new claims are reported. This process is commonly referred to as loss development. To project ultimate losses and LAE, our actuaries examine the paid and reported losses and LAE for each accident year and multiply these values by a loss development factor. The selected loss development factors are based upon a review of the loss development patterns indicated in the companies' historical loss triangles and applicable insurance industry loss development factors.

The reserve analysis performed by our actuaries provides preliminary central estimates of the unpaid losses and LAE. At each quarter-end, the results of the reserve analysis are summarized and discussed with our senior management. The senior management group considers many factors in determining the amount of reserves to record for financial statement purposes. These factors include the extent and timing of any recent catastrophic events, historical pattern and volatility of the actuarial indications, the sensitivity of the actuarial indications to changes in paid and reported loss patterns, the consistency of claims handling processes, the consistency of case reserving practices, changes in our pricing and underwriting, and overall pricing and underwriting trends in the insurance market.

Deposits

The banking segment's major source of funds and liquidity is its deposit base. Deposits provide funding for its investment in loans and securities. Interest paid for deposits must be managed carefully to control the level of interest expense and overall net interest margin. The composition of the deposit base (time deposits versus interest-bearing demand deposits and savings) is constantly changing due to the banking segment's needs and market conditions. Overall, average deposits totaled $5.3 billion for the year ended December 31, 2013, an increase from average deposits of $4.6 billion for the month ended December 31, 2012. The table below presents the average balance of deposits and the average rate paid on those deposits (dollars in thousands).

	Year Ended December 31, 2013		Month Ended December 31, 2012	
	Average Balance	Average Rate Paid	Average Balance	Average Rate Paid
Noninterest-bearing demand deposits	$ 1,370,029	0.00%	$ 1,321,011	0.00%
Interest-bearing demand deposits	1,930,622	0.24%	1,700,265	0.25%
Savings deposits	247,789	0.32%	177,803	0.32%
Certificates of deposit	1,745,483	0.54%	1,355,435	0.53%
	$ 5,293,923	0.28%	$ 4,554,514	0.26%

The maturity of interest-bearing time deposits of $100,000 or more at December 31, 2013 is set forth in the table below (in thousands).

Months to maturity:	
3 months or less	$ 453,642
3 months to 6 months	272,461
6 months to 12 months	492,140
Over 12 months	456,146
	$ 1,674,389

The banking segment experienced growth of $693.1 million in interest-bearing time deposits of $100,000 or more at December 31, 2013 compared with December 31, 2012, primarily due to those deposits assumed as a part of the FNB Transaction. At December 31, 2013, there were $1.7 billion in interest-bearing time deposits scheduled to mature within one year.

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Borrowings

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

	December 31,			
	2013		2012	
	Balance	Average Rate Paid	Balance	Average Rate Paid
Short-term borrowings	$ 342,087	0.36%	$ 728,250	0.33%
Notes payable	56,327	6.33%	141,539	5.89%
Junior subordinated debentures	67,012	3.59%	67,012	3.53%
	$ 465,426	2.10%	$ 936,801	1.40%

Short-term borrowings consist of federal funds purchased, securities sold under agreements to repurchase, borrowings at the Federal Home Loan Bank ("FHLB") and short-term bank loans. The $386.2 million decrease in short-term borrowings at December 31, 2013 compared with December 31, 2012 included decreases of $250.0 million in borrowings at the FHLB and $132.4 million in federal funds purchased. These decreases were primarily the result of lower funding requirements due to a reduction in our mortgage origination segment's balance on its warehouse line of credit with the Bank. Notes payable at December 31, 2013 of $56.3 million is comprised of insurance segment term notes and nonrecourse notes owed by First Southwest. The $85.2 million decrease in notes payable at December 31, 2013 compared to December 31, 2012 was primarily due to the Notes at OP, a wholly owned subsidiary of Hilltop, being called for redemption on October 15, 2013.

Liquidity and Capital Resources

Hilltop is a financial holding company whose assets primarily consist of the stock of its subsidiaries and invested assets. Hilltop's primary investment objectives, as a holding company, are to preserve capital and have available cash resources to utilize in making acquisitions. At June 30, 2014, Hilltop had approximately $158 million in freely available cash and cash equivalents. If necessary or appropriate, we may also finance acquisitions with the proceeds from equity or debt issuances. The current short-term liquidity needs of Hilltop include operating expenses, dividends on preferred stock and the cash consideration associated with the SWS Merger.

Recent Events

On March 31, 2014, we entered into a definitive merger agreement with SWS providing for the merger of SWS with and into a subsidiary of Hilltop formed for the purpose of facilitating this transaction (see "The Merger Agreement" included elsewhere in this proxy statement/prospectus). Under the terms of the merger agreement, SWS stockholders will receive per share consideration of 0.2496 shares of Hilltop common stock and $1.94 of cash, equating to $7.25 per share based on Hilltop's closing price on June 30, 2014. The value of the merger consideration will fluctuate with the market price of Hilltop's common stock. We intend to fund the cash portion of the consideration, currently estimated at approximately $78 million in the aggregate, through available cash. The merger is subject to customary closing conditions, including regulatory approvals and approval of the stockholders of SWS, and is expected to be completed prior to the end of 2014.

On October 15, 2013, OP called for redemption all of its outstanding Notes on November 14, 2013 (the "Redemption Date"). At October 15, 2013, OP had $90.9 million in aggregate principal amount of Notes outstanding, including $6.9 million aggregate principal amount held by our insurance company subsidiaries. The Notes were redeemed at a redemption price equal to the principal amount of the Notes, plus accrued and unpaid interest up to, but excluding, the Redemption Date. At any time prior to the Redemption Date, holders of the Notes could exchange the Notes for shares of Hilltop common stock at the rate of 73.94998 shares per $1,000 principal amount of the Notes (or approximately $13.52 per share). In lieu of delivery of Hilltop common stock upon the exercise of a holder of its exchange right, OP could elect to pay such holder of the Notes an amount in cash (or a combination of Hilltop common stock and cash) in respect of all or a portion of such holder's Notes equal to the closing price of Hilltop's common stock for the five consecutive trading days commencing on and including the third business day following the exercise of such exchange right. As of the closing of the redemption, the Notes held by third party investors were exchanged for 6,208,005 shares of Hilltop common stock and an aggregate cash payment of $11.1 million was made in exchange for the Notes held by our insurance company subsidiaries.

During September 2013, Hilltop and PlainsCapital contributed capital of $35.0 million and $25.0 million, respectively, to the Bank to provide additional capital in connection with the FNB Transaction.

Series B Preferred Stock

As a result of the PlainsCapital Merger, the outstanding shares of PlainsCapital Corporation's Non-Cumulative Perpetual Preferred Stock, Series C, all of which were held by the U.S. Treasury, were converted on a one-for-one basis into shares of Hilltop Series B Preferred Stock. The terms of our Series B Preferred Stock provide for the payment of non-cumulative dividends on a quarterly basis. The dividend rate, as a percentage of the liquidation amount, fluctuated until December 31, 2013 based upon changes in the level of "qualified small business lending" ("QSBL") by the Bank. The shares of Hilltop Series B Preferred Stock are senior to shares of our common stock with respect to dividends and liquidation preference, and qualify as Tier 1 Capital for regulatory purposes. At each of March 31, 2014, December 31, 2013 and December 31, 2012, $114.1 million of Hilltop's Series B Preferred Stock was outstanding. During the three months ended March 31, 2014, we accrued dividends of $1.4 million on the Hilltop Series B Preferred Stock.

The dividend rate on the Hilltop Series B Preferred Stock was 4.706% for the three months ended December 31, 2013. From January 1, 2014 until March 26, 2016, the dividend rate is fixed at 5.0% based upon Hilltop's level of QSBL at September 30, 2013. Beginning March 27, 2016, the dividend rate on any outstanding shares of Hilltop Series B Preferred Stock will be fixed at nine percent (9%) per annum.

Loss-Share Agreements

In connection with the FNB Transaction, the Bank entered into two loss-share agreements with the FDIC that collectively cover $1.2 billion of loans and OREO acquired in the FNB Transaction, which we refer to as "covered assets". Pursuant to the loss-share agreements, the FDIC has agreed to reimburse the Bank the following amounts with respect to the covered assets: (i) 80% of losses on the first $240.4 million of losses incurred; (ii) 0% of losses in excess of $240.4 million up to and including $365.7 million of losses incurred; and (iii) 80% of losses in excess of $365.7 million of losses incurred. The Bank has also agreed to reimburse the FDIC for any subsequent recoveries. The loss-share agreements for commercial and single family residential loans are in effect for 5 years and 10 years, respectively, from the Bank Closing Date and the loss recovery provisions to the FDIC are in effect for 8 years and 10 years, respectively, from the Bank Closing Date. In accordance with the loss-share agreements, the Bank may be required to make a "true-up" payment to the FDIC, approximately ten years following the Bank Closing Date, if the FDIC's initial estimate of losses on covered assets is greater than the actual realized losses. The "true-up" payment is calculated using a defined formula set forth in the P&A Agreement.

Regulatory Capital

We are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements may prompt certain actions by regulators that, if undertaken, could have a direct material adverse effect on our financial condition and results of operations. Under capital adequacy and regulatory requirements, we must meet specific capital guidelines that involve quantitative measures of our assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. Our capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

At June 30, 2014, Hilltop exceeded all regulatory capital requirements with a total capital to risk weighted assets ratio of 18.79%, Tier 1 capital to risk weighted assets ratio of 18.11% and a Tier 1 capital to average assets, or leverage, ratio of 13.51%. At June 30, 2014, the Bank was also considered to be "well-capitalized" under regulatory requirements without giving effect to the final Basel III capital rules adopted by the Federal Reserve Board on July 2, 2013. We discuss regulatory capital requirements in more detail in Note 14 to our unaudited consolidated financial statements also included in this proxy statement/prospectus.

Cash Flow Activities

Cash and cash equivalents (consisting of cash and due from banks and federal funds sold), totaled $688.8 million at June 30, 2014, a decrease of $57.2 million from $746.0 million at December 31, 2013. Cash and cash equivalents totaled $746.0 million at December 31, 2013, an increase of $19.6 million from $726.5 million at December 31, 2012. Deposit flows, calls of investment securities and borrowed funds, and prepayments of loans and mortgage-backed securities are strongly influenced by interest rates, general and local economic conditions and competition in the marketplace. These factors reduce the predictability of the timing of these sources of funds.

Cash used in operations during the six months ended June 30, 2014 was $291.7 million, a decrease in cash flow of $306.4 million compared with the same period in 2013, and was primarily due to reductions in cash provided by our mortgage loan origination activities. Cash provided by operations during 2013 of $396.7 million increased by $281.5 million compared with 2012 primarily due to the PlainsCapital Merger on November 30, 2012 and inclusion of operating activities of the banking, mortgage origination and financial advisory segments for the year ended December 31, 2013 compared with the month ended December 31, 2012.

Cash provided by our investment activities during the six months ended June 30, 2014 was $40.6 million, including $68.6 million from net changes in loans and $38.3 million from sales of premises and equipment and other real estate owned, partially offset by net cash paid for FHLB and FRB stock of $31.4 million, net purchases of premises and equipment and other assets of $19.8 million and net purchases of securities in our investment portfolio of $15.0 million. Cash used in our investment activities during the six months ended June 30, 2013 of $206.3 million primarily included net purchases of securities for investment of $127.5 million, $51.0 million for the origination of loans held for investment and net cash paid for FHLB and FRB stock of $21.2 million. The increase in cash provided by investing activities during the six months ended June 30, 2014, compared to the same period in 2013, was primarily due to reduced net purchases of securities driven by market conditions.

Cash provided by Hilltop's investment activities during 2013 was $223.9 million, including $362.7 million in net cash from the FNB Transaction and net proceeds from securities in Hilltop's investment portfolio of $8.9 million, partially offset by $140.4 million for the origination of loans held for investment and net purchases of premises and equipment and other assets of $11.9 million. During 2012, cash provided by Hilltop's investment activities was $12.9 million and primarily included $165.7 million in net cash from the PlainsCapital Merger, offset by $147.4 million in net purchases of securities for investment.

Cash provided by financing activities during the six months ended June 30, 2014 was $193.9 million, an increase in cash provided of $102.7 million compared with the same period in 2013. The increase in cash provided by financing activities was due primarily to a greater increase in short-term borrowings during the six months ended June 30, 2014, offset by a greater decrease in deposits during the six months ended June 30, 2014, compared with the same period in 2013. Cash used in financing activities during 2013 was $601.1 million, an increase in cash used of $620.9 million compared with 2012. The increase in cash during 2013 used was due primarily to the PlainsCapital Merger on November 30, 2012 and the inclusion of financing activities of the banking segment for the year ended December 31, 2013 compared with the month ended December 31, 2012.

Banking Segment

Within our banking segment, liquidity refers to the measure of our ability to meet our customers' short-term and long-term deposit withdrawals and anticipated and unanticipated increases in loan demand without penalizing earnings. Interest rate sensitivity involves the relationships between rate-sensitive assets and liabilities and is an indication of the probable effects of interest rate fluctuations on our net interest income.

Our asset and liability group is responsible for continuously monitoring our liquidity position to ensure that assets and liabilities are managed in a manner that will meet our short-term and long-term cash requirements. Funds invested in short-term marketable instruments, the continuous maturing of other interest-earning assets, cash flows from self-liquidating investments such as mortgage-backed securities and collateralized mortgage obligations, the possible sale of available for sale securities, and the ability to securitize certain types of loans provide sources of liquidity from an asset perspective. The liability base provides sources of liquidity through deposits and the maturity structure of short-term borrowed funds. For short-term liquidity needs, we utilize federal fund lines of credit with correspondent banks, securities sold under agreements to repurchase, borrowings from the Federal Reserve and borrowings under lines of credit with other financial institutions. For intermediate liquidity needs, we utilize advances from the FHLB. To supply liquidity over the longer term, we have access to brokered certificates of deposit, term loans at the FHLB and borrowings under lines of credit with other financial institutions.

We had deposits of $6.2 billion at June 30, 2014, a decrease of $567.6 million from $6.7 billion at December 31, 2013. This decrease is primarily due to seasonal factors related to our customers' requirements to satisfy year-end tax obligations and our strategic decision to offer lower renewal rates on certain time deposits acquired in the FNB Transaction that conform to the legacy PlainsCapital Bank interest rate structure. Deposits at December 31, 2013 increased by $2.0 billion from $4.7 billion at December 31, 2012, primarily due to the inclusion of $2.2 billion of deposits assumed as a part of the FNB Transaction. Deposit flows are affected by the level of market interest rates, the interest rates and products offered by competitors, the volatility of equity markets and other factors.

At June 30, 2014, money market deposits, including brokered deposits, were $959.4 million; time deposits, including brokered deposits, were $1.9 billion; and noninterest bearing demand deposits were $1.8 billion. Money market deposits, including brokered deposits, decreased by $195.9 million from $1.2 billion and time deposits, including brokered deposits, decreased $419.9 million from $2.3 billion at December 31, 2013.

At December 31, 2013, money market deposits, including brokered deposits, were $1.2 billion; time deposits, including brokered deposits, were $2.3 billion, and noninterest bearing demand deposits were $1.8 billion. Money market deposits, including brokered deposits, increased by $264.3 million from $891.0 million and time deposits, including brokered deposits, increased $910.7 million from $1.4 billion at December 31, 2012.

The Bank's 15 largest depositors, excluding Hilltop and First Southwest, accounted for 13.26% of the Bank's total deposits, and the Bank's five largest depositors, excluding First Southwest, accounted for 8.63% of the Bank's total deposits at June 30, 2014. The loss of one or more of our largest Bank customers, or a significant decline in our deposit balances due to ordinary course fluctuations related to these customers' businesses, could adversely affect our liquidity and might require us to raise deposit rates to attract new deposits, purchase federal funds or borrow funds on a short-term basis to replace such deposits. We have not experienced any liquidity issues to date with respect to brokered deposits or our other large balance deposits, and we believe alternative sources of funding are available to more than compensate for the loss of one or more of these customers.

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Mortgage Origination Segment

PrimeLending funds the mortgage loans it originates through a warehouse line of credit of up to $1.5 billion maintained with the Bank. At June 30, 2014 and December 31, 2013, PrimeLending had outstanding borrowings of $1.3 billion and $1.0 billion, respectively, against the warehouse line of credit. PrimeLending sells substantially all mortgage loans it originates to various investors in the secondary market, the majority with servicing released. As these mortgage loans are sold in the secondary market, PrimeLending pays down its warehouse line of credit with the Bank. In addition, PrimeLending has an available line of credit with JPMorgan Chase Bank, NA ("JPMorgan Chase") of up to $1.0 million. At both June 30, 2014 and December 31, 2013, PrimeLending had no borrowings under the JPMorgan Chase line of credit.

Insurance Segment

Our insurance operating subsidiary's primary investment objectives is to preserve capital and manage for a total rate of return. NLC's strategy is to purchase securities in sectors that represent the most attractive relative value. Bonds, cash and short-term investments of $210.4 million, or 91.6%, equity investments of $13.9 million and other investments of $5.5 million comprised NLC's $229.8 million in total cash and investments at June 30, 2014. At December 31, 2013, bonds, cash and short-term investments of $196.6 million, or 91.5%, equity investments of $13.1 million and other investments of $5.3 million comprised NLC's $215.0 million in total cash and investments. NLC does not currently have any significant concentration in both direct and indirect guarantor exposure or any investments in subprime mortgages. NLC has custodial agreements with Wells Fargo and an investment management agreement with DTF Holdings, LLC.

Financial Advisory Segment

FSC relies on its equity capital, short-term bank borrowings, interest-bearing and non-interest-bearing client credit balances, correspondent deposits, securities lending arrangements, repurchase agreement financings and other payables to finance its assets and operations. FSC has credit arrangements with four unaffiliated banks of up to $305.0 million, which are used to finance securities owned, securities held for correspondent accounts, receivables in customer margin accounts and underwriting activities. These credit arrangements are provided on an "as offered" basis and are not committed lines of credit. At June 30, 2014 and December 31, 2013, FSC had borrowed $102.0 million and $97.4 million, respectively, under these credit arrangements.

Contractual Obligations

The following table presents information regarding our contractual obligations at December 31, 2013 (in thousands). Our reserve for losses and loss adjustment expenses does not have a contractual maturity date. However, based on historical payment patterns, the amounts presented are management's estimate of the expected timing of these payments. The timing of payments is subject to significant uncertainty. NLC maintains a portfolio of investments with varying maturities to provide adequate cash flows for such payments. Payments related to leases are based on actual payments specified in the underlying contracts. Payments related to short-term borrowings and long-term debt obligations include the estimated contractual interest payments under the respective agreements.

	Payments Due by Period				
	1 year or Less	More than 1 Year but Less than 3 Years	3 Years or More but Less than 5 Years	5 Years or More	Total
Reserve for losses and loss adjustment expenses	$ 15,904	$ 9,120	$ 2,308	$ 136	$ 27,468
Short-term borrowings	343,604				343,604
Long-term debt obligations	6,965	9,395	10,053	259,560	285,973
Capital lease obligations	1,080	2,193	2,296	9,514	15,083
Operating lease obligations	25,541	39,311	23,241	30,041	118,134
Total	$ 393,094	$ 60,019	$ 37,898	$ 299,251	$ 790,262

Impact of Inflation and Changing Prices

Our consolidated financial statements included herein have been prepared in accordance with GAAP, which presently require us to measure financial position and operating results primarily in terms of historic dollars. Changes in the relative value of money due to inflation or recession are generally not considered. The primary effect of inflation on our operations is reflected in increased operating costs. In management's opinion, changes in interest rates affect the financial condition of a financial institution to a far greater degree than changes in the inflation rate. While interest rates are greatly influenced by changes in the inflation rate, they do not necessarily change at the same rate or in the same magnitude as the inflation rate. Interest rates are highly sensitive to many factors that are beyond our control, including changes in the expected rate of inflation, the influence of general and local economic conditions and the monetary and fiscal policies of the U.S. government, its agencies and various other governmental regulatory authorities.

Off-Balance Sheet Arrangements; Commitments; Guarantees

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

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

Standby letters of credit are written conditional commitments issued by us to guarantee the performance of a customer to a third party. In the event the customer does not perform in accordance with the terms of the agreement with the third party, we would be required to fund the commitment. The maximum potential amount of future payments we could be required to make is represented by the contractual amount of the commitment. If the commitment is funded, we would be entitled to seek recovery from the customer. Our policies generally require that standby letter of credit arrangements contain security and debt covenants similar to those contained in loan agreements.

In the aggregate, the Bank had outstanding unused commitments to extend credit of $1.2 billion and $1.1 billion at June 30, 2014 and December 31, 2013, respectively, and outstanding financial and performance standby letters of credit of $40.6 million and $42.2 million at June 30, 2014 and December 31, 2013, respectively.

In the normal course of business, FSC executes, settles and finances various securities transactions that may expose FSC to off-balance sheet risk in the event that a customer or counterparty does not fulfill its contractual obligations. Examples of such transactions include the sale of securities not yet purchased by customers or for the account of FSC, clearing agreements between FSC and various clearinghouses and broker-dealers, secured financing arrangements that involve pledged securities, and when-issued underwriting and purchase commitments.

Critical Accounting Policies and Estimates

Our accounting policies are fundamental to understanding our management's discussion and analysis of our results of operations and financial condition. Our significant accounting policies are presented in Note 1 to our audited consolidated financial statements, which are included in this proxy statement/prospectus. We have identified certain significant accounting policies which involve a higher degree of judgment and complexity in making certain estimates and assumptions that affect amounts reported in our consolidated financial statements. The significant accounting policies which we believe to be the most critical in preparing our consolidated financial statements relate to Allowance for Loan Losses, FDIC Indemnification Asset, Reserve for Losses and Loss Adjustment Expenses, Goodwill and Identifiable Intangible Assets, Loan Indemnification Liability, Mortgage Servicing Rights and Acquisition Accounting.

Allowance for Loan Losses

The allowance for loan losses is a valuation allowance for probable losses inherent in the loan portfolio. Loans are charged to the allowance when the loss is confirmed or when a determination is made that a probable loss has occurred on a specific loan. Recoveries are credited to the allowance at the time of recovery. Throughout the year, management estimates the probable level of losses to determine whether the allowance for credit losses is appropriate to absorb losses in the existing portfolio. Based on these estimates, an amount is charged to the provision for loan losses and credited to the allowance for loan losses in order to adjust the allowance to a level determined to be appropriate to absorb losses. Management's judgment regarding the appropriateness of the allowance for loan losses involves the consideration of current economic conditions and their estimated effects on specific borrowers; an evaluation of the existing relationships among loans, potential loan losses and the present level of the allowance; results of examinations of the loan portfolio by regulatory agencies; and management's internal review of the loan portfolio. In determining the ability to collect certain loans, management also considers the fair value of any underlying collateral. The amount ultimately realized may differ from the carrying value of these assets because of economic, operating or other conditions beyond our control. For additional discussion of allowance for loan losses and provisions for loan losses, see the section entitled "Allowance for Loan Losses" earlier in this Management's Discussion and Analysis of Financial Condition and Results of Operations.

FDIC Indemnification Asset

We have elected to account for the FDIC Indemnification Asset in accordance with FASB ASC 805. The FDIC Indemnification Asset is initially recorded at fair value, based on the discounted value of expected future cash flows under the loss-share agreements. The difference between the present value and the undiscounted cash flows we expect to collect from the FDIC will be accreted into noninterest income within the consolidated statements of operations over the life of the FDIC Indemnification Asset. The FDIC Indemnification Asset is reviewed quarterly and adjusted for any changes in expected cash flows based on recent performance and expectations for future performance of the covered portfolio. These adjustments are measured on the same basis as the related covered loans and covered OREO. Any increases in cash flow of the covered assets over those expected will reduce the FDIC Indemnification Asset, and any decreases in cash flow of the covered assets under those expected will increase the FDIC Indemnification Asset. Any amortization of changes in value is limited to the contractual terms of the loss-share agreements. Increases and decreases to the FDIC Indemnification Asset are recorded as adjustments to noninterest income within the consolidated statements of operations over the life of the loss-share agreements.

Reserve for Losses and Loss Adjustment Expenses

The reserve for losses and loss adjustment expenses represents our best estimate of our ultimate liability for losses and loss adjustment expenses relating to events that occurred prior to the end of any given accounting period but have not been paid. Months and potentially years may elapse between the occurrence of a loss covered by one of our insurance policies, the reporting of the loss and the

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payment of the claim. We record a liability for estimates of losses that will be paid for claims that have been reported, which is referred to as case reserves. As claims are not always reported when they occur, we estimate liabilities for claims that have occurred but have not been reported, or IBNR.

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

Goodwill and Identifiable Intangible Assets

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

The goodwill impairment test is a two-step process that requires us to make judgments in determining what assumptions to use in the calculation. The first step of the process consists of estimating the fair value of each reporting unit based on valuation techniques, including a discounted cash flow model using revenue and profit forecasts and recent industry transaction and trading multiples of our peers, and comparing those estimated fair values with the carrying values of the assets and liabilities of the reporting unit, which includes the allocated goodwill. If the estimated fair value is less than the carrying value, a second step is performed to compute the amount of the impairment, if any, by determining an "implied fair value" of goodwill. The determination of the "implied fair value" of goodwill of a reporting unit requires us to allocate the estimated fair value of the reporting unit to the assets and liabilities of the reporting unit. Any unallocated fair value represents the "implied fair value" of goodwill, which is compared to its corresponding carrying value.

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

Loan Indemnification Liability

The mortgage origination segment may be responsible for errors or omissions relating to its representations and warranties that the loans sold meet certain requirements, including representations as to underwriting standards and the validity of certain borrower representations in connection with the loan. If determined to be at fault, the mortgage origination segment either repurchases the loans from the investors or reimburses the investors' losses (a "make-whole" payment). The mortgage origination segment has established an indemnification liability for such probable losses based upon, among other things, the level of current unresolved repurchase requests, the volume of estimated probable future repurchase requests, our ability to cure the defects identified in the repurchase requests, and the severity of the estimated loss upon repurchase. Although we consider this reserve to be appropriate, there can be no assurance that the reserve will prove to be appropriate overtime to cover ultimate losses, due to unanticipated adverse changes in the economy and historical loss patterns, discrete events adversely affecting specific borrowers or industries, and/or actions taken by institutions or investors. The impact of such matters will be considered in the reserving process when known.

Mortgage Servicing Rights

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

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

Acquisition Accounting

We account for business combinations using the acquisition method, which requires an allocation of the purchase price of an acquired entity to the assets acquired, including identifiable intangibles, and liabilities assumed based on their estimated fair values at the date of acquisition. Management applies various valuation methodologies to these acquired assets and assumed liabilities which often involve a significant degree of judgment, particularly when liquid markets do not exist for the particular item being valued. Examples of such items include loans, deposits, identifiable intangible assets and certain other assets and liabilities acquired or assumed in business combinations. Management uses significant estimates and assumptions to value such items, including, among others, projected cash flows, prepayment and default assumptions, discount rates, and realizable collateral values. The purchase date valuations, which are considered preliminary and are subject to change for up to one year after the acquisition date, determine the amount of goodwill or bargain purchase gain recognized in connection with the business combination. While we are in the process of finalizing our purchase price allocation, significant changes are not anticipated. Certain assumptions and estimates must be updated regularly in connection with the ongoing accounting for purchased loans. Valuation assumptions and estimates may also have to be revisited in connection with periodic assessments of possible value impairment, including impairment of goodwill, intangible assets and certain other long-lived assets. The use of different assumptions could produce significantly different valuation results, which could have material positive or negative effects on the Company's results of operations.

Quantitative and Qualitative Disclosures About Market Risk.

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

At June 30, 2014 and December 31, 2013, total notes payable outstanding on our consolidated balance sheets was $55.6 million and $56.3 million, respectively, and was comprised entirely of indebtedness subject to variable interest rates. If LIBOR and the prime rate were to increase by one eighth of one percent (0.125%), the increase in interest expense on the variable rate debt would not have a significant impact on our future consolidated earnings or cash flows.

Banking Segment

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

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

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

An interest rate sensitive asset or liability is one that, within a defined time period, either matures or experiences an interest rate change in line with general market interest rates. The management of interest rate risk is performed by analyzing the maturity and repricing relationships between interest-earning assets and interest-bearing liabilities at specific points in time ("GAP") and by analyzing the effects of interest rate changes on net interest income over specific periods of time by projecting the performance of the mix of assets and liabilities in varied interest rate environments. Interest rate sensitivity reflects the potential effect on net interest income resulting from a movement in interest rates. A company is considered to be asset sensitive, or have a positive GAP, when the amount of its interest-earning assets maturing or repricing within a given period exceeds the amount of its interest-bearing liabilities also maturing or repricing within that time period. Conversely, a company is considered to be liability sensitive, or have a negative GAP, when the amount of its interest-bearing liabilities maturing or repricing within a given period exceeds the amount of its interest-earning assets also maturing or repricing within that time period. During a period of rising interest rates, a negative GAP would tend to affect net interest income adversely, while a positive GAP would tend to result in an increase in net interest income. During a period of falling interest rates, a negative GAP would tend to result in an increase in net interest income, while a positive GAP would tend to affect net interest income adversely. However, it is our intent to remain relatively balanced so that changes in rates do not have a significant impact on earnings.

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

	June 30, 2014					
	3 Months or Less	> 3 Months to 1 Year	> 1 Year to 3 Years	> 3 Years to 5 Years	> 5 Years	Total
Interest sensitive assets:						
Loans	$ 3,197,277	$ 624,873	$ 721,139	$ 284,195	$ 671,708	$ 5,499,192
Securities	563,121	155,138	111,599	39,106	191,563	1,060,527
Federal funds sold and securities purchased under agreements to resell	14,813					14,813
Other interest sensitive assets	341,181					341,181
Total interest sensitive assets	4,116,392	780,011	832,738	323,301	863,271	6,915,713
Interest sensitive liabilities:						
Interest bearing checking	$ 2,203,098	$	$	$	$	$ 2,203,098
Savings	259,540					259,540
Time deposits	588,856	875,132	276,967	130,068	14,353	1,885,376
Notes payable & other borrowings	1,004,440	75,488	1,389	745	5,290	1,087,352
Total interest sensitive liabilities	4,055,934	950,620	278,356	130,813	19,643	5,435,366
Interest sensitivity gap	$ 60,458	$ (170,609)	$ 554,382	$ 192,488	$ 843,628	$ 1,480,347
Cumulative interest sensitivity gap	$ 60,458	$ (110,151)	$ 444,231	$ 636,719	$ 1,480,347	
Percentage of cumulative gap to total interest sensitive assets	0.87%	-1.59%	6.42%	9.21%	21.41%	

The positive GAP in the interest rate analysis indicates that banking segment net interest income would generally rise if rates increase. Because of inherent limitations in interest rate GAP analysis, the banking segment uses multiple interest rate risk measurement techniques. Simulation analysis is used to subject the current repricing conditions to rising and falling interest rates in increments and decrements of 1%, 2% and 3% to determine the effect on net interest income changes for the next twelve months. The banking segment also measures the effects of changes in interest rates on market value of equity by discounting projected cash flows of deposits and loans. Market value changes in the investment portfolio are estimated by discounting future cash flows and using duration analysis. Investment security prepayments are estimated using current market information. We believe the simulation analysis

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presents a more accurate picture than the GAP analysis. Simulation analysis recognizes that deposit products may not react to changes in interest rates as quickly or with the same magnitude as earning assets contractually tied to a market rate index. The sensitivity to changes in market rates varies across deposit products. Also, unlike GAP analysis, simulation analysis takes into account the effect of embedded options in the securities and loan portfolios as well as any off-balance-sheet derivatives.

The table below shows the estimated impact of increases of 1%, 2% and 3% and a decrease of 0.5% in interest rates on net interest income and on economic value of equity for the banking segment at June 30, 2014 (dollars in thousands).

Change in Interest Rates (basis points)	Changes in Net Interest Income		Changes in Economic Value of Equity	
	Amount	Percent	Amount	Percent
+300	$ (3,821)	-1.51%	$ (73,215)	-5.95%
+200	$ (12,028)	-4.75%	$ (61,258)	-4.98%
+100	$ (14,390)	-5.68%	$ (24,987)	-2.03%
-50	$ 1,026	0.40%	$ 15,910	1.29%

The projected changes in net interest income and market value of equity to changes in interest rates at June 30, 2014 were in compliance with established internal policy guidelines. These projected changes are based on numerous assumptions of growth and changes in the mix of assets or liabilities.

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

Mortgage Origination Segment

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

IRLCs represent an agreement to extend credit to a mortgage loan applicant, whereby the interest rate on the loan is set prior to funding. Our mortgage loans held for sale, which we hold in inventory while awaiting sale into the secondary market, and our IRLCs are subject to the effects of changes in mortgage interest rates from the date of the commitment through the sale of the loan into the secondary market. As a result, we are exposed to interest rate risk and related price risk during the period from the date of the lock commitment until (i) the lock commitment cancellation or expiration date or (ii) the date of sale into the secondary mortgage market. Loan commitments generally range from 20 to 60 days, and our average holding period of the mortgage loan from funding to sale is approximately 30 days. An integral component of our interest rate risk management strategy is our execution of forward commitments to sell mortgage-backed securities to minimize the impact on earnings resulting from significant fluctuations in the fair value of mortgage loans held for sale and IRLCs caused by changes in interest rates.

We have recently expanded, and may continue to expand, our residential mortgage servicing operations within our mortgage origination segment. As a result of our mortgage servicing business, we have a portfolio of MSRs. One of the principal risks associated with MSRs is that in a declining interest rate environment, they will likely lose a substantial portion of their value as a result of higher than anticipated prepayments. Moreover, if prepayments are greater than expected, the cash we receive over the life of the mortgage loans would be reduced. In the future, we may use various derivative financial instruments to provide a level of protection against such interest rate risk. However, no hedging strategy can protect us completely, and hedging strategies may fail because they are improperly designed, improperly executed and documented or based on inaccurate assumptions and, as a result, could actually increase our risks and losses. The increasing size of our MSR portfolio may increase our interest rate risk and correspondingly, the volatility of our earnings, especially if we cannot adequately hedge the interest rate risk relating to our MSRs.

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

Insurance Segment

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

Financial Advisory Segment

Our financial advisory segment is exposed to market risk primarily due to its role as a financial intermediary in customer transactions, which may include purchases and sales of securities, use of derivatives and securities lending activities.

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

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

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

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

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

Financial Statements and Supplementary Data.

Hilltop's financial statements and the financial statements of FNB are submitted as a separate section of this proxy statement/prospectus. See "Financial Statements," commencing on page F-1 hereof.

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

None.

Directors, Executive Officers and Corporate Governance.

Directors

Set forth below is a brief biography of each of the current members of Hilltop's board of directors.

Charlotte Jones Anderson Age 48	Ms. Anderson has served as a director of Hilltop since our acquisition of PlainsCapital in November 2012. She previously served as a director of PlainsCapital from September 2009 to November 2012. She currently serves as Executive Vice President, Brand Management and President of Charities for the Dallas Cowboys Football Club, Ltd., a National Football League team. She has worked in various capacities for the Dallas Cowboys organization since 1990. A native of Little Rock, Arkansas, Ms. Anderson is a graduate of Stanford University where she earned a Bachelor of Science degree in Human Biology. Ms. Anderson is actively involved with a number of charitable and philanthropic organizations, including The Boys and Girls Clubs of America (regional trustee), the Salvation Army (chairman of board of directors), The Rise School (board of directors), the Southwest Medical Foundation (board of directors), the Dallas Symphony (board of directors), and the President's Advisory Counsel for The Dallas Center for Performing Arts Foundation.
Rhodes R. Bobbitt Age 69	Mr. Bobbitt has served as a director of Hilltop since November 2005. Mr. Bobbitt is retired. From 1987 until June 2004, he served as a Managing Director and the Regional Office Manager of the Private Client Service Group of Credit Suisse First Boston/Donaldson, Lufkin & Jenrette. Mr. Bobbitt was formerly Vice President of Security Sales in the Dallas office of Goldman, Sachs & Company from 1969 until 1987. He also serves on the Board of Directors of First Acceptance Corporation, including the Nominating and Corporate Governance, Investment, and Audit Committees of that company.

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Tracy A. Bolt Age 50	Mr. Bolt has served as a director of Hilltop since our acquisition of PlainsCapital in November 2012. He previously served as a director of PlainsCapital from September 2009 to November 2012. In 1994, Mr. Bolt co-founded Hartman Leito & Bolt, LLP, an accounting and consulting firm based in Fort Worth, Texas, where he serves as a partner and is a member of the firm's leadership committees. Mr. Bolt holds a Bachelor of Science and Master of Science from the University of North Texas, and he is a certified public accountant. He currently serves as a business advisor to numerous management teams, public and private company boards, not for profit organizations and trusts.
W. Joris Brinkerhoff Age 62	Mr. Brinkerhoff has served as a director of Hilltop since June 2005. Mr. Brinkerhoff founded a Native American-owned joint venture, Doyon Drilling Inc. J.V., in 1981 and served as its operations Chief Executive Officer and Chief Financial Officer until selling his venture interests in 1992. Doyon Drilling Inc. J.V. designed, built, leased and operated state of the art mobile drilling rigs for ARCO and British Petroleum in conjunction with their development of the North Slope Alaska petroleum fields. Mr. Brinkerhoff currently manages, on a full-time basis, family interests, including oil and gas production, a securities portfolio and various other business interests. He actively participates in numerous philanthropic organizations.
Charles R. Cummings Age 78	Mr. Cummings has served as a director of Hilltop since October 2005. Mr. Cummings currently serves as the Co-Manager of Acoustical Control LLC, a provider of noise abatement primarily for the oil and gas industry; DQB Solutions, LLC, a service provider to the waste industry; and Argyle Equipment, LLC, a lessor of equipment to the waste industry. In addition, Mr. Cummings is the President and Chief Executive Officer of CB Resources LLC, an investor in the oil and natural gas industry, and Container Investments, LLC, a lessor of equipment to the waste industry, each of which positions he has held since 1999 and 1991, respectively. Until its sale in January 2014, he served as the Chairman of Aaren Scientific, Inc., a manufacturer of intraocular lenses used in cataract surgery. From 1998 through 2008, he was the Chairman and Chief Executive Officer of Aaren Scientific, Inc. and its predecessors. In 1994, Mr. Cummings co-founded I.E.S.I. Corporation, a regional, non-hazardous waste management company, and serving as a director until its sale in 2005. Prior to that, he served as a Managing Director of AEA Investors, Inc., a private investment firm. Prior to 1979, he was a partner with Arthur Young & Company.

Hill A. Feinberg Age 67	Mr. Feinberg has served as Chairman and Chief Executive Officer of First Southwest since 1991. He has also served as a director of Hilltop since our acquisition of PlainsCapital in November 2012. He previously served as a director of PlainsCapital from December 31, 2008 (in conjunction with PlainsCapital's acquisition of First Southwest) to November 2012. Prior to joining First Southwest, Mr. Feinberg was a senior managing director at Bear Stearns & Co. Mr. Feinberg is a past chairman of the Municipal Securities Rulemaking Board, the self-regulatory organization with responsibility for authoring the rules that govern the municipal securities activities of registered brokers. Mr. Feinberg also is a member of the board of directors of Energy XXI (Bermuda) Limited, a public company. Mr. Feinberg also formerly served as a member of the board of directors of Compass Bancshares, Inc. and Texas Regional Bancshares, Inc., as an advisory director of Hall Phoenix Energy, LLC and as the non-executive chairman of the board of directors of General Cryogenics, Inc.
Gerald J. Ford Age 70	Mr. Ford has served as Chairman of the Board of Hilltop since August 2007, and has served as a director of Hilltop since June 2005. Mr. Ford served as interim Chief Executive Officer of Hilltop from January 1, 2010 until March 11, 2010. Mr. Ford is a banking and financial institutions entrepreneur who has been involved in numerous mergers and acquisitions of private and public sector financial institutions, primarily in the Southwestern United States, over the past 35 years. In that capacity, he acquired and consolidated 30 commercial banks from 1975 to 1993, forming First United Bank Group, Inc., a multi-bank holding company for which he functioned as Chairman of the Board and Chief Executive Officer until its sale in 1994. During this period, he also led investment consortiums that acquired numerous financial institutions, forming in succession, First Gibraltar Bank, FSB, First Madison Bank, FSB and First Nationwide Bank. Mr. Ford also served as Chairman of the Board of Directors and Chief Executive Officer of Golden State Bancorp Inc. and its subsidiary, California Federal Bank, FSB, from 1998 to 2002. He currently serves on the boards of directors of Freeport McMoRan Copper and Gold Inc., SWS and Scientific Games Corporation. Mr. Ford previously served as Chairman of Pacific Capital Bancorp and a director of First Acceptance Corporation, McMoRan Exploration Co. and Triad Financial Corporation. Mr. Ford also currently serves on the Board of Trustees of Southern Methodist University, is the Co-Managing Partner of Ford Financial Fund II, L.P., a private equity fund. Hilltop's President and Chief Executive Officer, Jeremy B. Ford, is the son of Mr. Ford, and Hilltop's Executive Vice President, General Counsel and Secretary, Corey G. Prestidge, is the son-in-law of Mr. Ford.

Jeremy B. Ford Age 40	Mr. Jeremy B. Ford has served as President, Chief Executive Officer and a director of Hilltop since March 2010. Mr. Jeremy B. Ford worked in the financial services industry for over thirteen years, primarily focused on investments in, and acquisitions of, depository institutions and insurance and finance companies. He also is one of the individuals who provided services to Hilltop under the prior Management Services Agreement with Diamond A Administration Company, LLC. Accordingly, he was actively involved in numerous potential acquisitions for Hilltop prior to 2010, and the divestiture of the mobile home communities business in 2007. Mr. Jeremy B. Ford also is currently Chairman of the Board of First Acceptance Corporation. Prior to becoming President and Chief Executive Officer of Hilltop, he was a principal of Ford Financial Fund, L.P., a private equity fund. From 2004 to 2008, he worked for Diamond A-Ford Corporation, where he was involved in various investments made by a family limited partnership. Prior to that, he worked at Liberté Investors Inc. (now First Acceptance Corporation), California Federal Bank, FSB (now Citigroup Inc.), and Salomon Smith Barney (now Citigroup Inc.). Jeremy Ford is the son of Gerald J. Ford, Hilltop's Chairman of the Board, and the brother-in-law of Corey G. Prestidge, Hilltop's Executive Vice President, General Counsel and Secretary.
J. Markham Green Age 71	Mr. Green has served as a director of Hilltop since February 2004. Mr. Green is a private investor. From 2001 to 2003, he served as Vice Chairman of the Financial Institutions and Governments Group in investment banking at JP Morgan Chase. From 1993 until joining JP Morgan Chase, Mr. Green was involved in the start-up, and served on the boards, of eight companies, including Affordable Residential Communities Inc., the predecessor company to Hilltop Holdings Inc. From 1973 to 1992, Mr. Green served in various capacities at Goldman, Sachs & Co. in investment banking. He was a general partner of Goldman, Sachs & Co. and co-head of its Financial Services Industry Group. Mr. Green is a member of the board of directors of MENTOR/The National Mentoring Partnership. Mr. Green previously served as Chairman of the Board of PowerOne Media LLC.
Jess T. Hay Age 83	Mr. Hay has served as a director of Hilltop since March 2009. Mr. Hay is the retired Chairman and Chief Executive Officer of Lomas Financial Corporation, formerly a diversified financial services company engaged principally in mortgage banking, retail banking, commercial leasing and real estate lending, and of Lomas Mortgage USA, a mortgage banking institution, from which he retired in December 1994. As Chairman and Chief Executive Officer of Lomas Financial Corporation, which included during his tenure, a total of five different corporations listed on the New York Stock Exchange, Mr. Hay has had extensive experience with all of the major functions within the operations of a public company. He was a director of Viad Corp. from 1981 until 2013, and presently is a Director Emeritus. He previously served as a director of Trinity Industries, Inc. from 1965 to 2011, Exxon Mobil from 1982 to 2001, SBC Communications (now AT&T) from 1985 to 2004 and MoneyGram International, Inc. from 2004 to 2010.

William T. Hill, Jr. Age 72	Mr. Hill has served as a director of Hilltop since April 2008. He currently has his own law firm. Prior to 2012, Mr. Hill was of counsel at Fitzpatrick Hagood Smith & Uhl, a criminal defense firm. Prior to that, Mr. Hill served as the Dallas District Attorney and the Chief Prosecuting Attorney of the Dallas District Attorney's office. During his tenure at the District Attorney's office, Mr. Hill restructured the office of 250 lawyers and 150 support personnel, including the computerization of the office in 1999. For more than four decades, Mr. Hill has been a strong community leader serving on a number of charitable boards and receiving numerous civic awards, including President of the SMU Mustang Board of Directors and Chairman of the Doak Walker Running Back Award for its first year. Mr. Hill currently serves on the board of directors of Oncor Electric Delivery Company LLC, Oncor Electric Delivery Holdings Company LLC and Baylor Hospital Foundation, and is actively involved in the Mercy Street Mission. Mercy Street is a Christian-based organization serving West Dallas children by placing mentors with the children.
James R. Huffines Age 63	Mr. Huffines is the President and Chief Operating Officer of PlainsCapital, a position he has held since November 2010. He has served as a director of Hilltop since our acquisition of PlainsCapital in November 2012. He previously served as a director of PlainsCapital from May 2011 to November 2012. Prior to that, Mr. Huffines served as the Chairman of the Central and South Texas region and a director of PlainsCapital Bank, a position he held since joining PlainsCapital in 2001. Mr. Huffines holds a Bachelor of Business Administration in Finance from the University of Texas. He served on the board of Energy Future Holdings (formerly TXU Corp.), from 2007 until 2012. In addition, Mr. Huffines previously served as Chairman of the University of Texas System Board of Regents for over four and a half years. Mr. Huffines also participates in many community and business organizations, including serving as a board member of the Dallas Citizens Council, Board of Advisors of Dallas Chamber, the Board of Trustees of the Bob Bullock Texas State History Museum Foundation, Vice Chair of the Texas Business Leadership Council, the Executive Committee of the Chancellor's Council at the University of Texas System; and a member of the Texas Philosophical Society.
Lee Lewis Age 62	Mr. Lewis has served as a director of Hilltop since our acquisition of PlainsCapital in November 2012. He previously served as a director of PlainsCapital from 1989 to November 2012. He founded in 1976, and currently serves as the chief executive officer of, Lee Lewis Construction, Inc., a construction firm based in Lubbock, Texas. Mr. Lewis graduated from Texas Tech University and is a member of the American General Contractors Association, West Texas Chapter, the Chancellors Council for the Texas Tech University System, and the Red Raider Club.

Andrew J. Littlefair Age 53	Mr. Littlefair has served as a director of Hilltop since our acquisition of PlainsCapital in November 2012. He previously served as a director of PlainsCapital from September 2009 to November 2012. He is a co-founder of Clean Energy Fuels Corp., a provider of compressed and liquefied natural gas in the United States and Canada that is publicly traded on the NASDAQ Global Select Market, and has served as that company's President, Chief Executive Officer and a director since 2001. From 1996 to 2001, Mr. Littlefair served as President of Pickens Fuel Corp., and from 1987 to 1996, he served in various management positions at Mesa, Inc., an energy company. From 1983 to 1987, Mr. Littlefair served in the Reagan Administration as a Staff Assistant to the President. He served as the Chairman of NGV America, the leading U.S. advocacy group for natural gas vehicles, from March 1993 to March 2011. Mr. Littlefair served on the board of directors of Westport Innovations Inc., a Canadian company publicly traded on the NASDAQ Global Market from 2007 to June 2010.
W. Robert Nichols, III Age 70	Mr. Nichols has served as a director of Hilltop since April 2008. Mr. Nichols has been a leader in the construction machinery business since 1966. He was the president of Conley Lott Nichols, a dealer for several manufacturers of construction machinery, until its sale in 2012. In 2013, he purchased an oilfield services company in Midland, Texas, for which he serves as Chairman and President. He has served on numerous bank and bank holding company boards, including United Mexico Bancorp and Ford Bank Group. Mr. Nichols is active in civic and charitable activities, serving as an active director at M.D. Anderson Hospital, The Nature Conservancy of Texas and Mercy Street.

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C. Clifton Robinson
Age 76

Mr. Robinson has served as a director of Hilltop since March 2007. From 2000 until its acquisition by a subsidiary of Hilltop in January 2007, Mr. Robinson was Chairman of the Board and Chief Executive Officer of NLASCO, Inc., an insurance holding company domiciled in Texas. Until December 2012, Mr. Robinson served as Chairman of the Board of NLASCO, Inc. In 2000, Mr. Robinson formed NLASCO, Inc. in conjunction with the acquisition of American Summit Insurance Company and the reacquisition of National Lloyds Insurance Company, which he had initially acquired in 1964 and later sold. In 1979, he organized National Group Corporation for the purpose of purchasing insurance companies and related businesses. In 1964, he became the President and Chief Executive Officer of National Lloyds Insurance Company in Waco, Texas, one of the two current insurance subsidiaries of NLC (formerly known as NLASCO, Inc.). From 1964 to the present, Mr. Robinson has participated in the formation, acquisition and management of numerous insurance business enterprises. Mr. Robinson established the Robinson-Lanham Insurance Agency in 1961. He previously has held positions with various insurance industry associations, including Vice-Chairman of the Board of Texas Life and Health Guaranty Association, President of the Independent Insurance Agents of Waco-McLennan County and member of the board of directors of the Texas Life Insurance Association and the Texas Medical Liability Insurance Underwriting Association. Mr. Robinson currently serves on the Board of Trustees of the Scottish Rite Hospital for Children in Dallas, Texas and the Baylor University Board of Regents.

Kenneth D. Russell
Age 65

Mr. Russell has served as a director of Hilltop since August 2010. Mr. Russell is a former member of the managing board of directors for KPMG Deutsche Treuhand-Gesellschaft Aktiengesellschaft (KPMG DTG). While a member of KPMG DTG, Mr. Russell served in leadership of Audit Financial Services. Subsequent to his service as a member of the German firm leadership, he functioned as a freelance strategic advisory to KPMG DTG's managing board of directors, working directly with members of its executive committee. He also participated in the integration of the UK and German KPMG firms in the formation of KPMG Europe and headed a partner development program, which focuses on assisting partners in becoming better businessmen, as well as technicians. Prior to joining KPMG DTG, Mr. Russell was the lead financial services partner in the US KPMG LLP's Department of Professional Practice in New York. His responsibilities in the Department of Profession Practice included leading the financial instruments, structured financing and securitization topic teams, and he was one of KPMG's leading consultants on financial instruments, hedging and securitization accounting issues. Prior to joining the Department of Professional Practice at KPMG in 1993, Mr. Russell spent 20 years in KPMG's Dallas office and had engagement responsibilities for several significant regional banking, thrift and other financial services clients. He currently serves as a Financial Advisor with Diamond A Administration Company, LLC, an affiliate of Gerald J. Ford.

A. Haag Sherman Age 48	Mr. Sherman has served as a director of Hilltop since our acquisition of PlainsCapital in November 2012. He previously served as a director of PlainsCapital from September 2009 to November 2012. Mr. Sherman co-founded and served in various capacities, including Chief Executive Officer and Chief Investment Officer, at Salient Partners, L.P., an investment firm based in Houston, Texas, from 2002 to 2011. Mr. Sherman serves on the board of directors of The Endowment Fund complex, Salient Absolute Return Fund complex, Salient MLP & Energy Infrastructure Fund (NYSE: SMF) and Blue Dolphin Energy Company (Nasdaq: BDCO). Mr. Sherman is an honors graduate of the University of Texas School of Law and a cum laude graduate of Baylor University. He is a certified public accountant and a member of the State Bar of Texas.
Robert C. Taylor, Jr. Age 67	Mr. Taylor has served as a director of Hilltop since our acquisition of PlainsCapital in November 2012. He previously served as a director of PlainsCapital from 1997 to November 2012. He has been engaged in the wholesale distribution business in Lubbock, Texas since 1971. In February 2009, Mr. Taylor was appointed to serve as Chief Executive Officer for United Supermarkets, LLC, a retail grocery business in Texas since 1915. He also serves on the board of directors of United Supermarkets, LLC. Prior to that appointment, Mr. Taylor served as the Vice President of Manufacturing and Supply Chain for United Supermarkets since 2007. From 2002 to 2007, Mr. Taylor was the President of R.C. Taylor Distributing, Inc., a business engaged in the business of general merchandise, candy and tobacco to retail outlets in West Texas and Eastern New Mexico. Mr. Taylor is a 1971 graduate of Texas Tech University. He is chairman of the Lubbock Downtown Tax Increment Finance Redevelopment Committee and serves on the Texas Tech Chancellors Advisory Board.

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Carl B. Webb Age 64	Mr. Webb has served as a director of Hilltop since June 2005. From August 2010 until December 2012, Mr. Webb served as the Chief Executive Officer of Pacific Capital Bancorp and as Chairman of the Board and Chief Executive Officer of Santa Barbara Bank & Trust, N.A. He was a Senior Principal of Ford Financial Fund, L.P., a private equity fund that was the parent company of SB Acquisition Company LLC, the majority stockholder of Pacific Capital Bancorp prior to its sale to UnionBanCal Corporation. Mr. Webb also is the Co-Managing Partner of Ford Financial Fund II, L.P., a private equity fund. In addition, Mr. Webb has served as a consultant to Hunter's Glen/Ford, Ltd., a private investment partnership, since November 2002. He served as the Co-Chairman of Triad Financial Corporation, a privately held financial services company, from July 2007 to October 2009, as was the interim President and Chief Executive Officer from August 2005 to June 2007. Previously, Mr. Webb was the President and Chief Operating Officer and a Director of Golden State Bancorp Inc. and its subsidiary, California Federal Bank, FSB, from September 1994 to November 2002. Prior to his affiliation with California Federal Bank, FSB, Mr. Webb was the President and Chief Executive Officer of First Madison Bank, FSB (1993 to 1994) and First Gibraltar Bank, FSB (1988 to 1993), as well as President and a Director of First National Bank at Lubbock (1983 to 1988). Mr. Webb also is a director of Prologis, Inc. He is a former director of Pacific Capital Bancorp, M&F Worldwide Corp., Plum Creek Timber Company and Triad Financial Corporation.
Alan B. White Age 65	Mr. White is one of PlainsCapital's founders. He has served as Chairman and Chief Executive Officer of PlainsCapital since 1987. He has served as a director of Hilltop since our acquisition of PlainsCapital in November 2012 and is the Vice-Chairman of the Board of Directors and the Chairman of Hilltop's Executive Committee. Mr. White received his Bachelors of Business Administration in Finance at Texas Tech University. Mr. White's current charitable and civic service includes serving as a member of the Cotton Bowl Athletic Association Board of Directors, the MD Anderson Cancer Center Living Legend Committee and the Dallas Citizens Council. He was also the founding chairman of the Texas Tech School of Business Chief Executive's Roundtable; the former Chairman of the Texas Tech Board of Regents, the Covenant Health System Board of Trustees, and the Methodist Hospital System Board of Trustees; and a member of the Texas Tech University President's Council and the Texas Hospital Association Board.

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Director Compensation

General

Members of our Board of Directors who also are full-time employees do not receive any compensation for their service on the Board of Directors or any committee of the Board of Directors. All other directors receive the following compensation for their service on the Board of Directors:

- $40,000 annual retainer; and
- $2,000 fee for participation in each meeting of the Board of Directors at which attendance in person is requested (one-half of that fee is paid for participation in any meeting at which attendance is requested by telephone).

In addition, members of board committees receive the following additional compensation:

- Audit Committee $65,000 annual fee for the chairperson of the committee;
- Nominating and Corporate Governance Committee $10,000 annual fee for the chairperson of the committee;
- Compensation Committee $10,000 annual fee for the chairperson of the committee;
- Investment Committee $25,000 annual fee for the chairperson of the committee;
- Merger and Acquisition Committee $10,000 annual fee for the chairperson of the committee; and
- $1,000 fee for participation in each meeting of a board committee.

Members of our Board of Directors may elect to receive their aggregate Board of Directors and board committee compensation:

- entirely in the form of cash;
- entirely in the form of common stock; or
- one-half in cash and one-half in common stock.

Any elections, or changes in elections, by directors regarding the form of compensation to be received may only occur during a "trading window" and only become effective at the "trading window" immediately following such election or change in election. Cash and shares of common stock are paid and issued, respectively, in arrears on a calendar quarterly basis, with no vesting requirements. Customarily, these payments and issuances occur by the 15th day of the month following the applicable calendar quarter-end. The value of the common stock awarded is based upon the average closing price per share of our common stock for the last ten consecutive trading days of the applicable calendar quarter. In lieu of fractional shares of common stock that would otherwise be issuable to directors, we pay cash to the director based upon the value of those fractional shares at the value the shares are awarded to the director. If a director does not serve for the entire calendar quarter, that director is compensated based upon the time of service during the applicable calendar quarter.

Each member of our Board of Directors is reimbursed for out-of-pocket expenses associated with his service on, and attendance at, Board of Directors or board committee meetings. Other than as described above, members of our Board of Directors receive no additional compensation for their service on the Board of Directors or board committees.

Political Action Committee Matching Program

The NLASCO Political Action Committee, or the PAC, is a separate segregated fund that was formed to make political contributions. To encourage participation in the PAC by eligible participants, for each contribution made to the PAC by an eligible individual contributor, NLC makes a matching contribution to any Section 501(c)(3) organization of the contributor's choice, dollar for dollar, up to the maximum amount an eligible individual can contribute to the PAC in a given calendar year. Under this program, no contributor to the PAC receives any financial, tax or other tangible benefit or premium from either the recipient charities or us. This program is completely voluntary.

2013 Director Compensation

Director Compensation Table for 2013(1)

Name	Fees earned or paid in cash ($)	Stock awards ($)	Total ($)
Charlotte Jones Anderson	28,031	27,970	56,000
Rhodes Bobbit	89,000		89,000
Tracy A. Bolt	24	65,976	66,000
W. Joris Brinkerhoff	56,000		56,000
Charles R. Cummings	131,000		131,000
Hill A. Feinberg			
Gerald J. Ford	50,000		50,000
Jeremy B. Ford			
J. Markham Green	68,000		68,000
Jess T. Hay	63,000		63,000
William T. Hill, Jr.	62,000		62,000
James Huffines			
Lee Lewis	54,000		54,000
Andrew J. Littlefair	28,541	28,459	57,000
W. Robert Nichols, III	66,000		66,000
C. Clifton Robinson	50,000		50,000
Kenneth D. Russell	50,000		50,000
A. Haag Sherman	73,000		73,000
Robert C. Taylor, Jr.	28,031	27,970	56,000
Carl B. Webb	36	49,964	50,000
Alan B. White			

(1) Fees earned for services performed in 2013 include annual retainers, meeting fees and chairperson remuneration. Aggregate fees paid to non-employee directors for annual retainers and committee chairmanships were paid quarterly in arrears. Cash was paid in lieu of the issuance of fractional shares. Service for any partial quarter is calculated and paid on the basis of time served during the applicable calendar quarter. Non-employee directors are solely responsible for the payment of taxes payable on remuneration paid by the Company. The number of shares awarded was determined based upon the average closing price per share of our common stock for the last ten consecutive trading days of the calendar quarter during which the stock was earned; however, the dollar value reported in the table for each stock award was determined in accordance with FASB ASC Topic 718.

As described above, the 2013 stock awards were issued to each non-employee director who elected to receive all or part of his or her director compensation in the form of our common stock, generally within 15 days following each applicable calendar quarter-end. All of our personnel, as well as non-employee directors, are subject to trading restrictions with regard to our common stock, and trading may only occur during a "trading window." Provided that any such party does not possess

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material, non-public information about us, this trading period commences on the next trading day following two trading days after the public release of quarterly or annual financial information and continues until the close of business on last day of the month preceding the last month of the next fiscal quarter.

The following numbers of shares of our common stock were issued to our directors for services performed during 2013:

Name of Director	Number of Shares
Charlotte Jones Anderson	1,623
Tracy A. Bolt	3,826
Andrew J. Littlefair	1,666
Robert C. Taylor, Jr.	1,623
Carl B. Webb	2,908

Each of the following directors had outstanding the following aggregate numbers of shares of our common stock awarded for services performed on behalf of us from election or appointment through the end of fiscal 2013: For further information about the stockholdings of these directors and our management, see "Information About the Companies Hilltop Security Ownership of Hilltop Management" elsewhere in this proxy statement/prospectus.

Name of Director	Number of Shares
Charlotte Jones Anderson	1,623
Tracy A. Bolt	3,826
Rhodes Bobbitt	1,562
W. Joris Brinkerhoff	9,943
Charles R. Cummings	5,379
Gerald J. Ford	2,893
J. Markham Green	3,872
Andrew J. Littlefair	1,666
Robert C. Taylor, Jr.	1,623
Carl B. Webb	35,080

Board Committees

General

Our Board of Directors appoints committees to assist it in carrying out its duties. In particular, committees work on key issues in greater detail than would be practical at a meeting of all the members of the Board of Directors. Each committee reviews the results of its deliberations with the full Board of Directors.

The standing committees of the Board of Directors currently consist of the Audit Committee, the Compensation Committee, the Executive Committee, the Investment Committee, the Merger and Acquisition Committee, and the Nominating and Corporate Governance Committee. Current copies of the charters for the Audit Committee, the Compensation Committee, and the Nominating and Corporate Governance Committee, as well as our Corporate Governance Guidelines, Code of Ethics and Business Conduct, or the General Code of Ethics and Business Conduct, and Code of Ethics for Chief Executive and Senior Financial Officers, or the Senior Officer Code of Ethics, may be found on our website at ir.hilltop-holdings.com, under the heading "Corporate Information Governance Documents." Printed versions also are available to any stockholder who requests them by writing to our corporate Secretary at the following address: Hilltop Holdings Inc., 200 Crescent Court, Suite 1330,

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Dallas, Texas 75201. A more detailed description of these committees is set forth below. Our Board of Directors may, from time to time, establish certain other committees to facilitate our management.

Committee Membership

The following table shows the current membership of, and the 2013 fiscal meeting information for, each of the committees of the Board of Directors.

Name	Audit Committee	Compensation Committee	Nominating and Corporate Governance Committee	Investment Committee	Merger and Acquisition Committee	Executive Committee
Charlotte Jones Anderson						
Rhodes Bobbit				Chairman		
Tracy A. Bolt						
W. Joris Brinkerhoff						
Charles R. Cummings	Chairman					
Hill A. Feinberg						
Gerald J. Ford						
Jeremy B. Ford						
J. Markham Green						
Jess T. Hay					Chairman	
William T. Hill, Jr.						
James Huffines						
Lee Lewis						
Andrew J. Littlefair						
W. Robert Nichols, III			Chairman			
C. Clifton Robinson						
Kenneth D. Russell						
A. Haag Sherman		Chairman				
Robert C. Taylor, Jr.						
Carl B. Webb						
Alan B. White						Chairman
	14	7	3	6	3	5

Meetings in Fiscal
2013

Audit Committee

We have a standing Audit Committee established within the meaning of Section 3(a)(58)(A) of the Securities Exchange Act of 1934, as amended, or the Exchange Act. The Audit Committee helps our Board of Directors ensure the integrity of our financial statements, the qualifications and independence of our independent registered public accounting firm and the performance of our internal audit function and independent registered public accounting firm. In furtherance of those matters, the Audit Committee assists in the establishment and maintenance of our internal audit controls, selects, meets with and assists the independent registered public accounting firm, oversees each annual audit and quarterly review and prepares the report that federal securities laws require be included in our annual proxy statement. Mr. Cummings has been designated as Chairman, and Messrs. Green and Bolt are members, of the Audit Committee. Until January 9, 2013, Mr. Bobbitt also served as a member of the Audit Committee. Our Board of Directors has reviewed the education, experience and other qualifications of each member of the Audit Committee. Based upon that review, our Board of Directors has determined that each of Mr. Cummings and Mr. Bolt qualifies as an "audit committee financial expert," as defined by the rules of the SEC, and each member of the Audit Committee is independent in accordance with the listing standards of the NYSE. Currently, none of our Audit Committee members serve on the audit committees of three or more public companies.

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Compensation Committee

The Compensation Committee reviews and approves the compensation and benefits of our executive officers, administers the Hilltop Holdings Inc. 2012 Annual Incentive Plan, or the Annual Incentive Plan, the Hilltop Holdings Inc. 2003 Equity Incentive Plan, or the 2003 Equity Incentive Plan, and the Hilltop Holdings Inc. 2012 Equity Incentive Plan, or the 2012 Equity Incentive Plan, and produces the annual report on executive compensation for inclusion in our annual proxy statement, which is also included in this proxy statement/prospectus and appears below on page 201. Each member is independent in accordance with the listing standards of the NYSE.

Nominating and Corporate Governance Committee

The Nominating and Corporate Governance Committee's purpose is as follows:

- Identify, screen and recommend to our Board of Directors individuals qualified to serve as members, and on committees, of the Board of Directors;
- Advise our Board of Directors with respect to the composition, procedures and committees of the Board of Directors;
- Advise our Board of Directors with respect to the corporate governance principles applicable to the Company; and
- Oversee the evaluation of the Board of Directors and our management.

Each member of the Nominating and Corporate Governance Committee is independent in accordance with the listing standards of the NYSE.

Investment Committee

The Investment Committee is responsible for, among other things, reviewing investment policies, strategies and programs; reviewing the procedures that we utilize in determining that funds are invested in accordance with policies and limits approved by the Investment Committee; and reviewing the quality and performance of our investment portfolios and the alignment of asset duration to liabilities.

Merger and Acquisition Committee

The purpose of the Merger and Acquisition Committee is to review potential mergers, acquisitions or dispositions of material assets or a material portion of any business proposed by management and to report its findings and conclusions to the Board of Directors. Each member is independent in accordance with the listing standards of the NYSE.

Executive Committee

The Executive Committee, with certain exceptions, has the power and authority of the Board of Directors to manage the affairs of the Company between meetings of the Board of Directors.

Corporate Governance

General

We are committed to good corporate governance practices and, as such, we have adopted formal corporate governance guidelines to maintain our effectiveness. The guidelines govern, among other things, board member qualifications, responsibilities, education, management succession and executive sessions. A copy of the corporate governance guidelines may be found at our corporate website at ir.hilltop-holdings.com under the heading "Corporate Information Governance Documents." A

copy also may be obtained upon request from our corporate Secretary at the following address: Hilltop Holdings Inc., 200 Crescent Court, Suite 1330, Dallas, Texas 75201.

Board Leadership Structure

We have separated the offices of Chief Executive Officer and Chairman of the Board as a means of separating management of the Company from our Board of Director's oversight of management. Separating these roles also enables an orderly leadership transition when necessary. We believe, at this time, that this structure provides desirable oversight of our management and affairs. We have in the past appointed, and will continue to appoint, lead independent directors as circumstances require.

Risk Oversight

Our Board of Directors oversees an enterprise-wide approach to risk management, intended to support the achievement of organizational objectives, including strategic objectives, to improve long-term organizational performance and enhance stockholder value. Our Board of Directors is actively involved in establishing and refining our business strategy, including assessing management's appetite for risk and determining the appropriate level of overall risk for the Company. We may conduct assessments in the future as circumstances warrant.

While the Board of Directors has the ultimate oversight responsibility for the risk management process, various committees of the Board of Directors also have responsibility for risk management. In particular, the Audit Committee focuses on financial risk, including internal controls, and, from time to time, discusses and evaluates matters of risk, risk assessment and risk management with our management team. The Compensation Committee is responsible for overseeing the management of risk associated with our compensation policies and arrangements. The Nominating and Corporate Governance Committee ensures that the internal rule processes by which we are governed are consistent with prevailing governance practices and applicable laws and regulations. Finally, the Investment Committee ensures that our funds are invested in accordance with policies and limits approved by it. Our Senior Officer Code of Ethics, General Code of Ethics and Business Conduct, committee charters and other governance documents are reviewed by the appropriate committees annually to confirm continued compliance, ensure that the totality of our risk management processes and procedures is appropriately comprehensive and effective and that those processes and procedures reflect established best practices.

Board Performance

Our Board of Directors conducts an annual survey of its members regarding its performance and reviews the results of the survey with a view to improving efficacy and effectiveness of the Board of Directors. In addition, the full Board of Directors reviews annually the qualifications and effectiveness of the Audit Committee and its members.

Director Qualifications for Service

As described below, the Nominating and Corporate Governance Committee considers a variety of factors when evaluating a potential candidate to fill a vacancy on the Board of Directors or when nomination of an incumbent director for re-election is under consideration. The Nominating and Corporate Governance Committee and our Board of Directors strive to balance a diverse mix of experience, perspective, skill and background with the practical requirement that the Board of Directors will operate collegially, with the common purpose of overseeing our business on behalf of our stockholders. All of our directors possess relevant experience, and each of them approaches the business of the Board of Directors and their responsibilities with great seriousness of purpose. The following describes, with respect to each director, his or her particular experience, qualifications, attributes and skills that qualify him or her to serve as a director:

Charlotte Jones Anderson	Ms. Anderson has significant managerial and executive officer experience with large entrepreneurial businesses and provides the Board of Directors the perspective of one of PlainsCapital's significant customers.
Rhodes Bobbitt	Mr. Bobbitt has an extensive investment background. This is particularly important given our available cash on hand and the investment portfolios at our subsidiaries.
Tracy A. Bolt	Mr. Bolt has significant experience concerning accounting matters that is essential to our Audit Committee's and Board of Directors' oversight responsibilities.
W. Joris Brinkerhoff	Mr. Brinkerhoff has participated, and continues to participate, in a number of business interests. Accordingly, he brings knowledge and additional perspectives to our Board of Directors from experiences with those interests.
Charles R. Cummings	Mr. Cummings has an extensive operational and accounting background. His expertise in these matters brings considerable strength to our Audit Committee and Board of Directors in these areas.
Hill A. Feinberg	Mr. Feinberg has extensive knowledge and experience concerning PlainsCapital's financial advisory segment and the industry in which it operates through his extended period of service to First Southwest.
Gerald J. Ford	Mr. Ford has been a financial institutions entrepreneur and private investor involved in numerous mergers and acquisitions of private and public sector financial institutions over the past 35 years. His extensive banking industry experience and educational background provide him with significant knowledge in dealing with financial, accounting and regulatory matters, making him a valuable member of our Board of Directors. In addition, his service on the boards of directors and audit and corporate governance committees of a variety of public companies gives him a deep understanding of the role of the Board of Directors.
Jeremy B. Ford	Mr. Jeremy B. Ford's career has focused on mergers and acquisitions in the financial services industry. Accordingly, he has been actively involved in numerous acquisitions, including our acquisitions of NLC (formerly known as NLASCO, Inc.), PlainsCapital Corporation and substantially all of the assets of FNB. His extensive knowledge of our operations makes him a valuable member of our Board of Directors.
J. Markham Green	Mr. Green has an extensive background in financial services, as well as board service. His investment banking background also provides our Board of Directors with expertise surrounding acquisitions and investments.

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Jess T. Hay	Mr. Hay has broad experience in managing and leading significant enterprises in the financial services industry. His service on the boards of other significant companies provides the Board of Directors with additional perspective on the Company's operations. His prior active involvement with the Democratic National Committee also provides him with broad exposure to the political processes on the national, state and local levels.
William T. Hill, Jr.	Mr. Hill's experience with legal and compliance matters, along with his management of a large group of highly skilled professionals, have given him considerable knowledge concerning many matters that come before our Board of Directors. Mr. Hill has also served on several civic and charitable boards over the past 35 years, which has given him invaluable experience in corporate governance matters.
James R. Huffines	Mr. Huffines' significant banking and managerial experience provide unique insights and experience to our Board of Directors.
Lee Lewis	Through his prior service on PlainsCapital's Board of Directors, Mr. Lewis has many years of knowledge of PlainsCapital and the challenges and opportunities that it is presented. The background of Mr. Lewis as a manager of a Texas-based company also provides unique insight to the Board of Directors.
Andrew J. Littlefair	Mr. Littlefair has significant experience serving as a chief executive officer and as a director of publicly traded companies and provides the Board of Directors with the perspective of one of PlainsCapital's significant customers.
W. Robert Nichols III	Mr. Nichols has broad experience in managing and leading enterprises. This significant experience provides our Board of Directors with additional perspectives on our operations.
C. Clifton Robinson	Mr. Robinson possesses particular knowledge and experience in the insurance industry, as we purchased NLC (formerly known as NLASCO, Inc.) from him in 2007. This provides our Board of Directors with expertise in regards to our insurance operations.
Kenneth D. Russell	Mr. Russell's extensive background in accounting and operating entities provides valuable insight to our Board of Directors, including merger and acquisition activities.
A. Haag Sherman	Mr. Sherman has significant experience concerning investing, legal and accounting matters that is essential to our Board of Director's oversight responsibilities.
Robert C. Taylor, Jr.	Through his prior service on PlainsCapital's Board of Directors, Mr. Taylor has many years of knowledge of PlainsCapital and the challenges and opportunities that it is presented. The background of Mr. Taylor as a manager of a Texas-based company also provides unique insight to the Board of Directors.

Carl B. Webb	Mr. Webb possesses particular knowledge and experience in strategic planning and the financial industry, as well as expertise in finance, that strengthen the Board of Directors' collective qualifications, skills and experience.
Alan B. White	Mr. White possesses knowledge of our business and industry through his lengthy tenure as PlainsCapital's Chief Executive Officer that aids him in efficiently and effectively identifying and executing our strategic priorities.

Executive Officers

We have identified the following officers as "executive officers," consistent with the definition of that term as used by the SEC:

Name	Age	Position
Hill A. Feinberg	67	Chief Executive Officer of First Southwest
Jeremy B. Ford	40	President, Chief Executive Officer and Director
James R. Huffines	63	President and Chief Operating Officer of PlainsCapital
John A. Martin	66	Executive Vice President, Chief Financial Officer of PlainsCapital
Darren E. Parmenter	51	Executive Vice President Principal Financial Officer
Corey G. Prestidge	40	Executive Vice President, General Counsel and Secretary
Todd L. Salmans	65	Chief Executive Officer of PrimeLending
Jerry L. Schaffner	56	President and Chief Executive Officer of the Bank
Alan B. White	65	Chief Executive Officer of PlainsCapital

Business Experience of Executive Officers

Information concerning the business experience of Messrs. Hill A. Feinberg, Jeremy B. Ford, James R. Huffines and Mr. Alan B. White is set forth above under the caption "Directors" on page 183.

John A. Martin. Mr. Martin has served as the Executive Vice President and Chief Financial Officer of PlainsCapital since November 2010 and has continued in that position since our acquisition of PlainsCapital in November 2012. Mr. Martin also serves on the board of directors of the Bank, First Southwest and various other subsidiaries of PlainsCapital. Prior to joining PlainsCapital, Mr. Martin most recently served as executive vice president and chief financial officer of Family Bancorp, Inc. and its subsidiary, San Antonio National Bank, from April 2010 until October 2010. Before joining Family Bancorp, from 2009 to 2010, Mr. Martin served as a consultant to community banks, providing strategic planning services. Beginning in 2005, Mr. Martin served as chief financial officer of Texas Regional Bancshares, Inc. and later served as director of financial planning and analysis for BBVA Compass after its acquisition of Texas Regional Bancshares in 2006.

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Darren E. Parmenter. Mr. Parmenter has served as Executive Vice President Principal Financial Officer of Hilltop since February 2014 and previously served as Senior Vice President of Finance of Hilltop from June 2007 to February 2014. From January 2000 to June 2007, Mr. Parmenter was with Hilltop's predecessor, Affordable Residential Communities Inc., and served as the Controller of Operations from April 2002 to June 2007. Prior to 2000, Mr. Parmenter was employed by Albertsons Inc., as an Assistant Controller.

Corey G. Prestidge. Mr. Prestidge has served as an Executive Vice President of Hilltop since February 2014 and General Counsel and Secretary of Hilltop since January 2008. From November 2005 to January 2008, Mr. Prestidge was the Assistant General Counsel of Mark Cuban Companies. Prior to that, Mr. Prestidge was an associate in the corporate and securities practice group at Jenkens & Gilchrist, a Professional Corporation, which is a former national law firm. Mr. Prestidge is the son-in-law of our Chairman of the Board, Gerald J. Ford, and the brother-in-law of our President and Chief Executive Officer, Jeremy B. Ford.

Todd L. Salmans. Mr. Salmans has served as Chief Executive Officer of PrimeLending since January 2011 and has continued in that position since our acquisition of PlainsCapital in November 2012. He also previously held the office of President of PrimeLending until August 2013. As Chief Executive Officer, Mr. Salmans is responsible for the strategic direction and day-to-day management of PrimeLending, including financial performance, compliance, business development, board and strategic partner communications and team development. He also serves as a member of PrimeLending's Board of Directors. Mr. Salmans joined PrimeLending in 2006 as Executive Vice President and Chief Operating Officer, with responsibility over daily operations, loan processing and sales. He was promoted to President in April 2007. Mr. Salmans has over 30 year of experience in the mortgage banking industry. Prior to joining PrimeLending, he served as regional executive vice president of CTX/Centex, regional senior vice president of Chase Manhattan/Chase Home Mortgage Corp., and regional senior vice president of First Union National Bank/First Union Mortgage Corp. Mr. Salmans is currently a board member of the Texas Mortgage Bankers Association.

Jerry L. Schaffner. Mr. Schaffner has served as the President and Chief Executive Officer of the Bank since November 2010 and has continued in that position since our acquisition of PlainsCapital in November 2012. He currently serves as a director of the Bank, First Southwest and various other subsidiaries, and previously served as a director of PlainsCapital from 1993 until March 2009. Mr. Schaffner has over 25 years of banking experience and joined PlainsCapital in 1988 as part of its original management group. He received his Bachelor of Business Administration in finance from Texas Tech University. Mr. Schaffner is a licensed Texas real estate broker.

Compensation Discussion and Analysis

The Compensation Committee (the "Committee") is responsible for establishing, implementing and monitoring adherence with our compensation philosophy. The Committee ensures that the total compensation paid to senior executives is fair, reasonable, competitive, performance-based and aligned with stockholder interests.

Executive Summary

Year 2013 represented a transformational time for our Company and compensation programs. It was the first year of full integration of PlainsCapital into Hilltop. In support of this significant change, the Committee established a new framework that focused on defined performance objectives. The Committee continues to refine compensation programs to further emphasize pay-for-performance, some of which have already been implemented for 2014.

2013 Highlights

Profitability increased exponentially. We generated a record $121.0 million in net income. We earned $1.40 per diluted share, up $1.50 per share from 2012. Return on average equity (ROAE) was 10.59% and return on average assets (ROAA) was 1.66%, compared to 9.61% and 1.01%, respectively, of our peer median.

Asset quality remained strong compared to peers with non-performing assets as a percentage of total assets of 0.32%.

Hilltop capital ratios remained strong with a Tier 1 Leverage Ratio at 12.81% and a Total Capital Ratio of 19.13% at December 31, 2013.

Completed the acquisition of substantially all of the assets and liabilities, including deposits, of First National Bank, Edinburg, Texas from the FDIC, as receiver, with loss share (the "FNB Transaction"), and reopened the acquired branches under the "PlainsCapital Bank" name. Accordingly, as of December 31, 2013, we had 77 branch locations, more than double than at December 31, 2012, and our total assets increased to $8.9 billion at December 31, 2013.

Redeemed the 7.5% Senior Exchangeable Notes due 2025, which was accretive to book value.

Hilltop continued to retain approximately $164 million of freely useable cash at December 31, 2013, following the redemption of the senior notes and a $35 million capital contribution to the Bank in connection with the FNB Transaction.

All of this contributed to a substantial increase in stockholder value as our stock price closed out the year at $23.13 per share, up 71% from the 2012 close of $13.54 per share. Additional detail regarding our results and achievements can be found in our Annual Report on Form 10-K for the year ended December 31, 2013. Furthermore, we believe that we are well positioned to continue positive growth momentum into 2014 and beyond.

Enhanced Compensation Program

With respect to 2013, the Committee implemented a cash incentive compensation program for all senior executive officers. In that regard, the Committee developed scorecards for each executive, which weighted cash incentive compensation on predefined objectives, including net income. The Committee also awarded long-term incentive compensation in the form of restricted stock that was subject to three-year cliff vesting. This practice was consistent with awards granted at PlainsCapital Corporation prior to the acquisition and was effective during the integration and transition period.

The most recent equity grants in February 2014 included a combination of performance-based and time-based restricted stock units. The Committee developed a long-term incentive plan whereby half of the equity awards granted to senior executive officers are subject to performance criteria over a three-year period and all awards are subject to a one-year hold period following vesting, subject to certain exceptions. The Committee also further refined the 2014 annual cash incentive compensation program to enhance its objectives. The Committee believes the implementation of these programs has benefited the Company in clearly defining short-term and long-term objectives.

Philosophy and Objectives of Our Executive Compensation Program

Our compensation program includes the following components: base salary, annual and long-term incentive awards that are linked to performance and the creation of stockholder value and perquisites. In structuring our compensation programs, the Committee selected the particular components and the weight given to those components based upon our strategic objectives. We believe that it is critical to structure the compensation program in such a manner to retain those with the talent, skill and experience necessary for us to realize our strategic objectives.

With this in mind, the following principles help guide our decisions regarding compensation of our named executive officers:

Compensation opportunities should be competitive with market practices. In order to attract and retain executives with the experience and skills necessary to lead our Company and motivate them to deliver strong performance to our stockholders, we are committed to providing total annual compensation opportunities that are competitive.

A significant portion of compensation should be performance-based. Our executive compensation program now further emphasizes pay-for-performance. This means that compensation based on corporate performance, as assessed under the criteria established pursuant to the Annual Incentive Plan, has the possibility to represent a significant portion of the named executive officer's total compensation. An additional component, which has the ability to reduce annual incentive compensation, is based upon improper risk taking and non-compliance with applicable laws and regulations.

Management's interests should be aligned with those of our stockholders. Our long-term incentive compensation was delivered in the form of restricted stock in 2013 to support our goals for ownership and retention. However, in 2014, long-term incentive compensation is being awarded in restricted stock units, half of which vest upon achievement of performance goals. The value of these awards ultimately depends upon the performance of our stock price or our relative total shareholder return. We also recently implemented stock ownership guidelines applicable to our Section 16 officers, including our named executive officers, and directors.

Compensation should be perceived as fair. We strive to create a compensation program that will be perceived as fair and equitable, both internally and externally.

How We Determine and Assess Executive Compensation Generally

Background

We completed the acquisition of PlainsCapital Corporation on November 30, 2012, and the compensation of our named executive officers who were employed by PlainsCapital Corporation is therefore largely based upon the compensation they were paid by PlainsCapital Corporation prior to the acquisition. Three of our named executive officers, Messrs. White, Huffines and Schaffner, were employed by PlainsCapital Corporation or its subsidiaries prior to the acquisition, and each had an employment agreement. In connection with the acquisition of PlainsCapital Corporation, we entered into retention agreements with Messrs. White and Schaffner to ensure continuity following the closing. All other existing employment arrangements at PlainsCapital Corporation were amended to terminate on November 30, 2014. For a more detailed discussion of these employment contracts, see " Employment Contracts and Incentive Plans Employment Contracts" commencing on page 216.

Messrs. Ford and Parmenter do not have employment agreements and their compensation was largely discretionary prior to 2013.

Role of the Compensation Committee

The Committee is responsible for reviewing and approving all aspects of the compensation programs for our named executive officers and making all decisions regarding specific compensation to be paid or awarded to them. The Committee is responsible for, among its other duties, the following:

- Review and approval of corporate incentive goals and objectives relevant to compensation;
- Evaluation of individual performance results in light of these goals and objectives;
- Evaluation of the competitiveness of the total compensation package; and

Approval of any changes to the total compensation package, including, but not limited to, base salary, annual and long-term incentive award opportunities and payouts and retention programs.

The Committee is responsible for determining all aspects of compensation of the Chief Executive Officers of Hilltop and PlainsCapital, as well as assessing their individual performance.

In setting the compensation of our named executive officers, the Committee, in its discretion, considers (i) the transferability of managerial skills, (ii) the relevance of each named executive officer's experience to other potential employees, and (iii) the readiness of the named executive officer to assume a different or more significant role, either within our organization or with another organization. When making pay-related decisions, the Committee also has considered our specific circumstances and the associated difficulties with attraction, retention and motivation of talent and the importance of compensation in supporting achievement of our strategic objectives.

Information about the Committee and its composition, responsibilities and operations can be found under "Board Committees" beginning on page 194.

Role of the Chief Executive Officers in Compensation Decisions

The Chief Executive Officers of Hilltop and PlainsCapital Corporation recommend to the Committee any compensation changes affecting the other named executive officers. The Chief Executive Officers provide input and recommendations to the Committee with regards to compensation decisions for their direct reports. These recommendations are made within the framework of the compensation programs approved by the Committee and based on market data provided by the Committee's independent consultant. The input includes base salary changes, annual incentive and long-term incentive opportunities, specific individual performance objectives, and individual performance assessments. The Chief Executive Officers make their recommendations based on their assessment of the individual officer's performance, performance of the officer's respective business or function and employee retention considerations. The Committee reviews and considers the Chief Executive Officers' recommendations when determining any compensation changes affecting our officers or executives. Each Chief Executive Officer does not play any role with respect to any matter impacting his own compensation.

Role of Stockholder Say-on-Pay Votes

The Company provides its stockholders with the opportunity to cast an annual advisory vote on executive compensation. At the Company's annual meeting of stockholders held in June 2013, 78% of the votes cast (excluding abstentions and broker non-votes) on the say-on-pay proposal at that meeting were voted in favor of the proposal. Following such vote, the Committee has made significant enhancements to the short-term and long-term programs during 2013 to further focus on pay-for-performance. Highlights of the compensation program for fiscal 2014 are included in this Compensation, Discussion & Analysis in order to assist stockholders in evaluating the additional changes the Committee has implemented. Accordingly, the Committee will continue to consider the outcome of the Company's say-on-pay votes when making future compensation decisions for the named executive officers. A vote on the frequency of advisory votes on executive compensation will be submitted to stockholders at the 2015 annual meeting of stockholders.

Role of Compensation Consultant

Pursuant to its charter, the Committee is authorized to retain and terminate any consultant, as well as to approve the consultant's fees and other terms of the engagement. The Committee also has the authority to obtain advice and assistance from internal or external legal, accounting or other advisors. In January 2013, the Committee engaged Pearl Meyer & Partners ("Pearl Meyer") as its compensation consultant. The Committee had not engaged a compensation consultant during any of the previous five years. In June 2013, the lead consultant with Pearl Meyer transferred to Meridian Compensation Partners, LLC ("Meridian"), and the Committee unanimously agreed to transfer its relationship to Meridian. The Committee believed that it was important to retain that lead consultant in order to complete the work already in progress. Meridian had also previously been the compensation consultant for PlainsCapital Corporation prior to its acquisition by Hilltop. Meridian does not provide any other services to management.

Meridian provides research, data analyses, survey information and design expertise in developing compensation programs for executives and incentive programs for eligible employees. In addition, Meridian keeps the Committee apprised of regulatory developments and market trends related to executive compensation practices. Meridian does not determine or recommend the exact amount or form of executive compensation for any of the named executive officers. A representative of Meridian generally attends meetings of the Committee, is available to participate in executive sessions and communicates directly with the Committee.

Pursuant to the Committee's charter, if the Committee elects to use a compensation consultant, the consultant must be independent. The Committee assesses independence taking into account the following factors:

- compliance with the NYSE listing standards;
- the policies and procedures the consultant has in place to prevent conflicts of interest;
- any business or personal relationships between the consulting firm and the members of the Committee;
- any ownership of Company stock by the individuals at the firm performing consulting services for the Committee; and
- any business or personal relationship of the firm with an executive officer of the Company.

Meridian has provided the Committee with appropriate assurances and confirmation of its independent status pursuant to the charter and other factors. The Committee believes that Meridian has been independent throughout its service for the Committee and there is no conflict of interest between Meridian and the Committee.

Other Factors

The Committee makes executive compensation decisions following a review and discussion of both the financial and operational performance of our businesses and the annual performance reviews of the named executive officers and other members of the management team.

Benchmarking Compensation

During 2013, the Committee consulted with Meridian to assess the competitiveness and effectiveness of our executive compensation program. In December 2013, Meridian provided an analysis of base salary, short-term incentive, long-term incentive and benefit practices of comparable companies in the financial industry. Meridian considered individual compensation elements, as well as the total compensation package, and assessed the relationship of pay to performance.

In performing this analysis, Meridian used a peer group of financial institutions, which was reviewed and approved by the Committee. The peer group included institutions of generally similar asset size and, to the extent possible, organizations with significant other operating segments. At the time the peer group was selected, our Company was positioned at the 55th percentile of the peer group in terms of total assets, with asset size ranging from $3.2 billion to $13.1 billion (approximately one-half to two times the size of our Company). The peer group used in the report presented for consideration consisted of the following financial institutions:

1st Source Corporation	BancFirst Corporation	Banner Corporation
Capital Bank Financial Corp.	Community Trust Bancorp, Inc.	First Financial Bankshares, Inc.
First Financial Holdings, Inc.	First Midwest Bancorp, Inc.	IBERIABANK Corporation
International Banchares Corp.	MB Financial, Inc.	Old National Bancorp
Park National Corporation	Pinnacle Financial Partners, Inc.	SCBT Financial Corporation
Southside Bancshares, Inc.	Sterling Financial Corporation	Texas Capital Bancshares, Inc.
Trustmark Corporation	Umpqua Holdings Corporation	Westamerica Bancorporation

Because a peer group analysis is limited to those positions for which compensation information is disclosed publicly, these studies typically include only the five most highly compensated officers at each company. Therefore, the compensation consultant also relied on published compensation surveys to supplement information for these positions, as well as to provide the basis for analysis for other executives. Similar asset and scope comparisons were used for that benchmarking analysis.

Elements of our Executive Compensation Program

Overall, our executive compensation program is designed to be consistent with the objectives and principles set forth in this discussion. The basic elements of our executive compensation program are summarized below, followed by a more detailed discussion of the programs.

Our compensation policies and programs are considered by the Committee in a total rewards framework, considering both "pay" base salary, annual incentive compensation and long-term incentive compensation; and "benefits" benefits, perquisites and executive benefits and other compensation. Our executive compensation program consists primarily of the following components:

Compensation Component	Purpose
Base Salary	Fixed component of pay intended to compensate the individual fairly for the responsibility level of the position held.
Annual Incentive Awards	Variable component of pay intended to motivate and reward the individual's contribution to achieving our short-term/annual objectives.
Long-term Incentive Awards	Variable component of pay intended to motivate and reward the individual's contribution to achieving our long-term objectives.
Benefits and Perquisites	Fixed component of pay intended to provide an economic benefit to us in attracting and retaining executive talent.

Base Salary

We provide base salaries for each named executive officer, commensurate with the services each provides to us, because we believe a portion of total direct compensation should be provided in a form that is fixed and liquid. In reviewing base salaries, the Committee evaluated the salaries of other named executive officers of the Company and its peers and any increased level of responsibility, among other items. As a result of that analysis, the Committee determined to increase the annual salaries of Messrs. Ford and Parmenter for 2014. With respect to the other named executive officers of the Company, the Committee determined to maintain the current salary for 2014, as they were found to be competitive with the Company's peers. The following are the base salaries for the named executive officers in 2013 and 2014:

	Base Salary		
Name	**2013**	**2014**	**$ Change**
Jeremy B. Ford	$ 500,000	$ 550,000	$ 50,000
Darren Parmenter	$ 300,000	$ 330,000	$ 30,000
Alan B. White	$ 1,350,000	$ 1,350,000(a)	$
James Huffines	$ 690,000	$ 690,000(b)	$
Jerry Schaffner	$ 525,000	$ 525,000(a)	$

(a) Messrs. White's and Schaffner's base salaries are set forth in their respective retention agreements, which became effective upon the closing of the acquisition of PlainsCapital Corporation.

(b) Mr. Huffines' salary is the same as that in effect prior to the acquisition of PlainsCapital Corporation.

Annual Incentive Awards

Our named executive officers and other employees are eligible to receive annual cash incentive awards based upon our financial performance and other factors, including individual performance. The Committee believes that this element of compensation is important to focus management efforts on, and provide rewards for, annual financial and strategic results that are aligned with creating value for our stockholders.

Target incentive awards are defined at the start of the year in consideration of market data provided by the Committee's consultant, each executive's total compensation package and the entity's budgetary considerations. Targets for 2013 were adjusted slightly lower than 2012 in consideration of these factors.

Each executive officer had defined performance objectives during 2013 based upon measurable performance of both the individual and our Company. These awards were made pursuant to the Annual Incentive Plan. Annual Incentive Plan awards are subject to claw back for improper risk management and non-compliance with applicable laws and regulations. This component of the compensation program is pre-determined at the outset of the year and based upon measurable criteria.

The Committee, in its sole discretion, determines the amount of each participant's award based on attainment of the applicable performance goals and assessments of individual performance. For 2013, the applicable performance goals were among the following:

- Consolidated financial results for Hilltop for named executive officers employed by Hilltop;
- Consolidated financial results of PlainsCapital, after removing purchase accounting adjustments, for employees of PlainsCapital and its subsidiaries;
- Financial results of lines of business for business heads after removing any purchase accounting adjustments; and
- Pre-determined individual objectives.

Additionally, a risk forfeiture of up to 15% of any available Annual Incentive Plan award can occur in the event that any improper risk management or non-compliance with applicable laws or regulations is identified.

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The elements of the annual cash incentive award do not become available until net income equals 60% of the budgeted annual earnings for the entity at which that named executive officer is employed. In order to be eligible to receive the target cash annual incentive award, actual earnings must meet budgeted amounts. A maximum of 150% of the target award may be paid in the event actual earnings exceed budgeted amounts. Threshold awards are set at 50% of target. Between the threshold and target amounts, a range of the potential annual cash incentive award is defined. Our 2013 goals were intended to be realistic and reasonable but challenging in order to drive performance. The Committee and management believe that by using these metrics we are encouraging profitable top line growth and value for stockholders. For 2013 and 2014, the Committee set Annual Incentive Plan compensation target payments for named executive officers as follows:

	Annual Incentive Plan Target as a Percent of Annual Base Salary for Calendar Year:	
Name	**2014**	**2013**
Jeremy B. Ford	77%	85%
Darren Parmenter	61%	67%
Alan B. White	100%	100%
James R. Huffines	80%	87%
Jerry L. Schaffner	73%	80%

Based upon evaluation of their respective performance in 2013, together with operations of the Company, the Committee determined the Annual Incentive Plan bonuses for 2013 as follows for the following named executive officers.

	2013 Annual Incentive Plan Target		2013 Annual Incentive Plan Payout	
Name	**Amount ($)**	**% of Base Salary**	**Amount ($)**	**% of Target**
Jeremy B. Ford	$ 425,000	85%	$ 500,000	118%
Darren Parmenter	$ 200,000	77%	$ 200,000	100%
Alan B. White	$ 1,350,000(a)	100%	$ 1,350,000(a)	100%
James R. Huffines	$ 600,000	87%	$ 555,000	93%
Jerry L. Schaffner	$ 420,000	80%	$ 420,000	100%

(a) Determined pursuant to Mr. White's retention agreement for the achievement of earnings threshold.

See "Narrative Disclosure to Summary Compensation Table and Grants of Plan-Based Awards Table Annual Incentive Plan" for more information on possible future payments to the named executive officers.

Long-Term Incentive Awards

As described above, we believe that a portion of each named executive officer's compensation should be tied to the performance of our stock price, aligning the officer's interest with that of our stockholders. In this regard, our long-term incentive compensation for 2013 was delivered in the form of restricted stock, the value of which is ultimately dependent upon the performance of our stock price. Further discussion of the 2012 Equity Incentive Plan pursuant to which such shares of restricted stock were awarded is found after the "Grants of Plan-Based Awards" section below.

Mr. Ford has an award outstanding under the 2003 Equity Incentive Plan. However, with the adoption of the 2012 Equity Incentive Plan, all 2013 equity-based awards, including the named executive officers, have since been made pursuant to the 2012 Equity Incentive Plan. All equity-based

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awards made to the named executive officers are approved by the Committee and not pursuant to delegated authority.

In 2013, long-term incentive awards were made in consideration of each executive's role, competitive market practice, and performance. Grants were made in the form of restricted shares on May 2, 2013, to the following named executive officers as set forth below:

Recipient	Number of Restricted Shares Granted
Jeremy Ford	30,000
Darren Parmenter	5,000
Alan B. White	50,000
James Huffines	30,000
Jerry L. Schaffner	20,000

On February 24, 2014, restricted stock units were granted to the named executive officers as set forth below:

Name	Time-Based RSUs Awarded	Performance-Based RSUs Awarded (at Target)	Total RSUs Awarded
Jeremy B. Ford	12,696	12,696	25,392
Darren Parmenter	3,703	3,703	7,406
Alan B. White	14,812	14,811	29,623
James Huffines	8,887	8,887	17,774
Jerry L. Schaffner	5,925	5,924	11,849

Perquisites and Other Benefits

We provide a limited number of perquisites and other benefits to our named executive officers at Hilltop. The only perquisite currently offered to the named executive officers employed directly by Hilltop is $150 per month to be applied to a gym membership to promote wellness. With respect to named executive officers employed by PlainsCapital and its subsidiaries, those entities provide them with a monthly car allowance and reimbursement for country club membership dues. In addition, Messrs. White and Schaffner are provided access to company aircraft and bank-owned life insurance. Otherwise, generally, our named executive officers receive only medical benefits, life insurance and long-term disability coverage, as well as supplemental contributions to the Company's 401(k) program, on the same terms and conditions as available to all employees of that entity.

Severance and Other Post-Termination Compensation

The named executive officers who are employed by PlainsCapital or its subsidiaries currently have certain contractual post-termination benefits; however, other than Messrs. White and Schaffner, those benefits will expire on November 30, 2014.

For named executive officers employed directly by Hilltop, other than change in control provisions in our 2012 Equity Incentive Plan, we do not currently maintain any severance or change in control programs. We, however, have historically paid severance, the amount of which is generally determined both by length of tenure and level of compensation, when termination occurs other than for cause and pursuant to which certain benefits may be provided to the named executive officers. Absent the negotiation of specific agreements with the named executive officers, severance benefits would be provided on the same basis as provided to other employees of the Company.

In connection with acquisition of PlainsCapital Corporation, we entered into retention agreements with Messrs. White and Schaffner, and Mr. Huffines' employment agreement that was in effect on the

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date of the acquisition entitles Mr. Huffines to certain severance benefits. The summary of the severance terms for each of these agreements is set forth below:

White Retention Agreement

Pursuant to his retention agreement, Mr. White is entitled to the following:

(1) $6,430,890, including interest thereon from November 30, 2012, in full satisfaction of Mr. White's rights under Section 6 (Termination Upon Change in Control) of his previous employment agreement with PlainsCapital Corporation, dated January 1, 2009, payable in a cash lump-sum upon any termination of his employment; and

(2) upon termination of his employment by us other than for cause or death or disability, or after non-renewal, cash severance of (i) the sum of Mr. White's annual base salary and the average of the annual bonus amounts paid to him for the three most recently completed fiscal years ending immediately prior to the date of termination, multiplied by (ii) the greater of (A) two, and (B) the number of full and partial years from the date of termination through the end of the applicable employment period under the retention agreement. Such severance is payable over the "severance period," which is the greater of two years from the date of termination and the number of full and partial years from the date of termination through the end of the applicable employment period under the retention agreement.

The foregoing cash amounts in subparagraph (1) represent "modified single trigger" benefits, payable assuming the termination of employment for any reason, and the foregoing cash amounts in subparagraph (2) represent "double trigger" benefits, payable assuming a qualifying termination of employment. With respect to the amounts described in subparagraph (1) that are paid in full satisfaction of Section 6 of Mr. White's previous employment agreement with PlainsCapital, such amounts are payable upon any termination of employment at any time, subject to any delay required by Section 409A of the Internal Revenue Code and the execution of a release of claims. The cash severance amounts described in subparagraph (2) are payable upon a termination of employment other than for cause, death or disability or a termination due to non-renewal by Hilltop, subject to any delay required by Section 409A of the Internal Revenue Code and the execution of a release of claims.

Schaffner Retention Agreement

Pursuant to his retention agreement, Mr. Schaffner is entitled to the following:

(1) $2,448,000, including interest thereon from November 30, 2012, in full satisfaction of Mr. Schaffner's rights under Section 6 (Termination Upon Change in Control) of his previous employment agreement with PlainsCapital Corporation, dated January 1, 2009, payable in a cash lump-sum upon any termination of his employment; and

(2) upon termination of his employment by us other than for cause or death or disability, cash severance of (i) the sum of Mr. Schaffner's annual base salary and the average of the annual bonus amounts paid to him for the three most recently completed fiscal years ending immediately prior to the date of termination. Such severance is payable in equal installments over a one-year period following the date of termination.

The foregoing cash amounts in subparagraph (1) represent "modified single trigger" benefits, payable assuming the termination of employment for any reason, and the foregoing cash amounts in subparagraph (2) represent "double trigger" benefits, payable assuming a qualifying termination of employment. With respect to the amounts described in subparagraph (1) that are paid in full satisfaction of Section 6 of Mr. Schaffner's previous employment agreement with PlainsCapital Corporation, such amounts are payable upon any termination of employment at any time, subject to any delay required by Section 409A of the Internal Revenue Code and the execution of a release of claims. The cash severance amounts described in subparagraph (2) are payable upon a termination of employment other than for cause, death or disability, subject to any delay required by Section 409A of the Internal Revenue Code and the execution of a release of claims.

Huffines Employment Agreement

Pursuant to the employment agreement of Mr. Huffines with PlainsCapital, he is entitled to cash severance based on three times the sum of (i) annual base salary, and (ii) the higher of the bonus paid for the most recently completed calendar year and the average bonus paid with respect to the three most recently completed calendar years ending immediately prior to the date of termination. The foregoing cash amounts represent "double trigger" benefits, which are payable upon a termination of the applicable executive's employment by us without cause or by the executive for good reason during the six (6) months prior to, or the twenty-four (24) months following, the effective time of the acquisition of PlainsCapital, which constituted a change in control, subject to the execution of a release of claims.

Further discussion of the agreements with Messrs. White, Schaffner and Huffines and payments made pursuant thereto may be found under the headings "Narrative Disclosure to Summary Compensation Table and Grants of Plan-Based Awards Table" and "Potential Payments Upon Termination or Change-in-Control" below.

The 2012 Equity Incentive Plan, under which we have granted awards to the named executive officers, contains specific termination and change in control provisions. We determined to include a change in control provision in the plan to be competitive with what we believe to be the standards for the treatment of equity upon a change in control for similar companies and so that employees who remain after a change in control would be treated the same with regard to equity as the general stockholders who could sell or otherwise transfer their equity upon a change in control. Under the terms of the plan, if a change in control (as defined below in the discussion of the plan) were to occur, all awards then outstanding would become vested and/or exercisable and any applicable performance goals with respect thereto would be deemed to be fully achieved. Further discussion of the change in control payments made pursuant to the 2012 Equity Incentive Plan may be found in the "Potential Payments Upon Termination or Change-in-Control" section below.

The Annual Incentive Plan, pursuant to which annual incentive bonuses are awarded, does not contain specific change in control provisions. Accordingly, the Committee, in its discretion, may determine what constitutes a change in control and what effects such an event may have any awards made pursuant to such plan.

Executive Compensation Changes for 2014

We made the following key compensation decisions with respect to our named executive officers for 2014, which build upon our compensation governance framework and our overall pay-for-performance philosophy:

Annual Incentive Compensation Design

- Scorecards were refined to weight 70% of awards on budgeted net income for Hilltop or PlainsCapital executives and 50% of segment budget and 20% of PlainsCapital budget for executives employed within our banking, financial advisory and mortgage origination segments. The remaining 30% based upon achievement of measurable, individual objectives.
- Increased threshold payouts from 5% of target to 50% of target.
- Payout curve generally remains steep until closer to target award and ratable thereafter.

Long-Term Incentive Compensation Design

- The Committee adopted new long-term incentive compensation award guidelines in December 2013.
- The Committee approved future awards granted to be made as restricted stock units and established design for executive officers at a Tier 1 level and at a Tier 2 level for all other key management employees.
- Tier 1 awards will be equally allocated 50% performance based vesting and 50% time-based vesting subject to three year vesting period and a one-year holding period.
- The performance based restricted stock units will vest based on 3-year cumulative earnings per share and total shareholder return performance relative to the KBW Regional Bank Index.
- Tier 2 awards will be allocated by Chief Executive Officers of Hilltop and PlainsCapital from a pool approved by the Committee. The restricted stock unit awards to Tier 2 recipients will be time-vested awards with a three-year vesting period and a one-year holding period.
- The Committee also adopted, and the Board of Directors approved, stock ownership guidelines for all executive officers and directors.

Risk Considerations in Our Compensation Program

We do not believe that our compensation policies and practices for 2013 give rise to risks that are reasonably likely to have a material adverse effect on our Company. In reaching this conclusion for 2013, we considered the following factors:

- Base salary is fixed and the only compensation components that are variable are the annual bonuses and restricted stock awards to named executive officers, which, other than the annual bonus with respect to Mr. White and Mr. Schaffner, were awarded based upon attainment of a pre-determined level of earnings.
- Annual Incentive Plan payments to the remaining named executive officers were determined or approved following the substantial completion of the audit of the Company's financial statements by the Company's independent registered public accounting firm. Thus, the Committee had ample knowledge of the financial condition and results of the Company, as well as reports of other committees of the Board of Directors, upon which to base any decisions.
- We have a balanced program that includes multiple performance goals, rewards short and multi-year performance, pays in cash and equity and provides a meaningful portion of pay in stock which is tied to our performance long-term.
- The Annual Incentive Plan awards are subject to claw-back and adjustments for improper risk and significant compliance issues.
- Each year the Committee reviews all compensation programs to ensure existing programs are not reasonably likely to have a material adverse effect on our Company.

Other Programs and Policies

Stock Ownership Requirements

In February 2014, the Committee recommended, and the Board of Directors adopted, a stock ownership policy applicable to our executive officers and directors. Within five years of the later of appointment or the date the policy was adopted, executive officers are required to achieve ownership of

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a defined market value of Company common stock equal to a minimum number of equity or equity-based securities as follows:

- Six times annual base salary for the Chief Executive Officer; and

- Three times annual base salary for the other executive officers.

Under this policy, directors are expected to own shares with a value greater than five times their annual retainer for serving on the Board of Directors of the Company. Our director compensation program permits directors to elect to receive their director compensation in cash, Company common stock or a combination of cash and Company common stock.

In calculating equity ownership for purposes of this requirement, we will include all shares beneficially owned by an individual, such as shares owned by an individual in the Company's benefit plans (e.g., 401(k)), shares of restricted stock and shares with respect to which an individual has voting or investment power. Shares underlying unexercised stock options are excluded when determining ownership for these purposes.

Executive officers are expected to hold 50% of any net shares received through compensatory equity based grants until the ownership guidelines are achieved. Once such officer achieves the ownership requirement, he or she is no longer restricted by the holding requirement; provided his or her total stock ownership level does not fall below the ownership guidelines.

In addition, all awards of restricted stock units granted in February 2014 and thereafter are, subject to certain exceptions, required to be held for one year after vesting.

Clawback Policy

Our compensation program also includes a claw-back from any annual cash incentive award for improper risk and significant compliance issues. Annual Incentive Plan awards are subject to any clawback, recoupment or forfeiture provisions (i) required by law or regulation and applicable to Hilltop or its subsidiaries or (ii) set forth in any policies adopted or maintained by Hilltop or any of its subsidiaries.

Tax Considerations

Section 162(m) of the Internal Revenue Code (the "Code") imposes a $1.0 million limit on the tax-deductibility of compensation paid to our five most highly paid executives, which includes the named executive officers. Exceptions are provided for compensation that is "performance-based" and paid pursuant to a plan meeting certain requirements of Section 162(m) of the Code. The Committee has carefully considered the implications of Section 162(m) of the Code and believes that tax deductibility of compensation is an important consideration. Accordingly, where possible and considered appropriate, the Committee strives to preserve corporate tax deductions. The Committee, however, reserves the flexibility, where appropriate, to approve compensation arrangements that may not be tax deductible to the Company, such as base salary and awards of time-based restricted stock. The Committee will continue to review the Company's executive compensation practices to determine if other elements of executive compensation constitute "qualified performance-based compensation" under Section 162(m) of the Code.

Trading Controls and Hedging, Short Sale and Pledging Policies

Executive officers, including the named executive officers, are required to receive the permission of the General Counsel prior to entering into any transactions in our securities, including gifts, grants and those involving derivatives. Generally, trading is permitted only during announced trading periods. Employees who are subject to trading restrictions, including the named executive officers, may enter into a trading plan under Rule 10b5-1 of the Exchange Act. These trading plans may be entered into only during an open trading period and must be approved by the General Counsel. We require trading plans to include a waiting period and the trading plans may not be amended during their term. The named executive officer bears full responsibility if he or she violates our policy by permitting shares to be bought or sold without pre-approval or when trading is restricted.

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Executive officers are prohibited from entering into hedging and short sale transactions and are subject to restrictions on pledging our securities.

Compensation Committee Report

The Compensation Committee of the Board of Directors of Hilltop Holdings Inc. has reviewed and discussed with management the Compensation Discussion and Analysis contained in this Proxy Statement. Based on its review, the Compensation Committee recommended to the Board of Directors that the Compensation Discussion and Analysis be included in the Proxy Statement.

The foregoing report has been submitted by the following members of the Compensation Committee:

Haag Sherman (Chairman)   Rhodes Bobbitt   W. Joris Brinkerhoff
William T. Hill, Jr.   Andrew Littlefair

Executive Compensation

The following tables set forth information concerning the compensation earned for services performed during 2013, 2012 and 2011 by the named executive officers, who were either serving in such capacities on December 31, 2013, or during 2013, or are reportable pursuant to applicable SEC regulations.

Summary Compensation Table

Fiscal Years 2013, 2012 and 2011

Name and principal position	Year	Salary ($)	Bonus(a) ($)	Stock Awards ($)	Option awards ($)	Non-Equity Incentive Plan Compensation(h) ($)	Change in pension value and nonqualified deferred compensation earnings ($)	All other compensation ($)	Total ($)
Jeremy B. Ford									
	2013	466,667(c)				897,500		1,800	1,365,967
President and Chief	2012	400,000	300,000						700,000
Executive Officer	2011	400,000	230,000		782,602(b)				1,412,602
Darren Parmenter									
	2013	296,667(c)				266,250		1,800	564,717
Executive Vice President Principal	2012	290,000(d)	100,000						390,000
Financial Officer	2011	275,000	75,000						350,000
Alan B. White									
	2013	1,350,000	1,350,000			662,500	28,950	142,491(g)	3,533,941
Chief Executive Officer of	2012	112,500(e)	1,350,000				6,431,982	1,716(f)	7,896,198
PlainsCapital Corporation	2011								
James R. Huffines									
	2013	690,000				952,500		51,145(g)	1,693,645
President and Chief Operating Officer of	2012	57,500(e)	600,000					4,039(f)	661,539
PlainsCapital Corporation	2011								
Jerry L. Schaffner									
	2013	525,000	420,000			265,000	11,016	51,815(g)	1,272,831
President and Chief Executive Officer of	2012	43,750(e)	420,000				2,448,936	4,332(f)	2,917,018
PlainsCapital Bank	2011								

(a)

Represents bonuses paid for services during 2013, 2012, and 2011, as applicable.

(b) Represents the FASB ASC Topic 718 expense recognized for stock options granted in fiscal 2011. For more information regarding outstanding stock options held by named executive officers, refer to section "*Outstanding Equity Awards at Fiscal Year-End* " below.

(c) Reflects increase in annual salary on April 1, 2013.

(d) Reflects increase in annual salary on April 1, 2012.

(e) Represents annual salaries (Mr. White $1,350,000; Mr. Schaffner $525,000; Mr. Huffines $690,000) prorated for service from December 1, 2012 to December 31, 2012.

(f) Includes group life insurance premiums, auto allowance, and club expenses paid during December 2013, Employee Stock Ownership Plan contributions made by employer for December 2012, use

(g) Includes group life insurance premiums, auto allowance, and club expenses paid during 2013, 401(k) profit sharing contributions made by employer for 2013, use of a company car (Mr. Schaffner $1,225; Mr. White $1,851.52), use of the company aircraft (Mr. White $58,740.65), and cash incentive payments (Messrs. Huffines and Schaffner $750 each). The table following these footnotes is a breakdown of all other compensation included in the "Summary Compensation Table" for the Named Executive Officers.

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(h)

Reflects the grant date fair values of deferred share awards calculated in accordance with FASB Accounting Standards Codification Topic 718 ("ASC Topic 718"). Reported as "Non-Equity Incentive Plan Compensation" due to adoption of Long-Term Incentive Plan under which grants were made. Prior grants reported as "option awards".

All Other Compensation

Name	Year	Perquisites and Personal Benefits(1)	Gross-Ups or Other Amounts Reimbursed for the Payment of Taxes	Company Contributions to Defined Contribution Plans(2)	Insurance Policies(3)	Director Fees	Total All Other Compensation
Jeremy B. Ford	2013	1,800					1,800
	2012						0
	2011						0
Darren Parmenter	2013	1,800					1,800
	2012						0
	2011						0
Alan B. White	2013	127,729		9,614	5,148		142,491
	2012	429	1,287				1,716
	2011						
James R. Huffines	2013	36,416		9,581	5,148		51,145
	2012	2,704		906	429		4,039
	2011						
Jerry L. Schaffner	2013	38,898		9,564	3,354		51,815
	2012	3,146		906	280		4,332
	2011						

(1)

2013. For Messrs. Ford and Parmenter, reflects $150 per month gym membership allowance. For Mr. White, includes a car allowance of $36,000, club expenses totaling $31,137.17, and the personal use of PlainsCapital airplane ($58,740.65) and automobile ($1,851.52). For Mr. Schaffner, includes a car allowance of $24,000, club expenses totaling $12,922.65, the personal use of PlainsCapital automobile ($1,225) and a holiday present ($750). For Mr. Huffines, includes a car allowance of $24,000, club expenses totaling $11,665.59 and a holiday present ($750).

(2)

2013. For Messrs. White, Schaffner, and Huffines, includes PlainsCapital's contribution to the 401(k) Profit Sharing Plan in each of their names. 2012. For Messrs. White, Schaffner, and Huffines, includes PlainsCapital's prorated contribution to the Employee Stock Ownership Plan.

(3)

Reflects Group term life insurance premiums paid during 2013.

Grants of Plan-Based Awards

Grants of Plan-Based Awards
Fiscal Year 2013

Name	Grant Date(a)	Estimated future payouts under non-equity incentive plan awards(b) Threshold ($)	Target ($)	Maximum ($)	All other stock awards: number of shares of stock or units (#)	Grant date fair value of stock and option awards(c) ($)
Jeremy B. Ford	March 28, 2013	21,250	425,000	637,500		
President and Chief Executive Officer	May 2, 2013				30,000	397,500
Darren Parmenter	March 28, 2013	10,000	200,000	300,000		
Executive Vice President Prinicpal Financial Officer	May 2, 2013				10,000	66,250
Alan B. White	March 28, 2013	1,089,843(d)	1,350,000(d)	1,350,000(d)		
Chief Executive Officer of PlainsCapital Corporation	May 2, 2013				50,000	662,500
James R. Huffines	March 28, 2013	30,000	600,000	900,000		
Chief Operating Officer of PlainsCapital Corporation	May 2, 2013				30,000	397,500
Jerry L. Schaffner	March 28, 2013	371,667(d)	420,000	630,000		
Chief Executive Officer of PlainsCapital Bank	May 2, 2013				20,000	265,000

(a) Represents the effective date of grant of restricted stock under the 2012 Equity Incentive Plan and annual cash incentive awards under the Annual Incentive Plan.

(b) Represent the value of potential payments under the Annual Incentive Plan to the named executive officers based on 2013 performance. Management incentive award amounts shown above represent potential awards that may have been earned based on performance during 2013. The actual Annual Incentive Plan awards earned for 2013 are reported in the "Summary Compensation Table" above. For more information regarding the Annual Incentive Plan, see below and also refer to "Compensation Discussion and Analysis" in this Proxy Statement.

(c) Represents the FASB ASC topic 718 expenses recognized for restricted stock granted in 2013, For more information regarding outstanding awards held by the named executive officer, refer to section "Outstanding Equity Awards at Fiscal Year-End" below.

(d) Represents the amount he would be entitled to under his respective retention agreement.

Narrative Disclosure to Summary Compensation Table and Grants of Plan-Based Awards Table

Employment Contracts and Incentive Plans

Set forth below is a summary of our retention agreements with Messrs. White and Schaffner and our employment agreement with Mr. Huffines. Our employment agreement with Mr. Parmenter expired in 2010, and we do not have an employment agreement with Mr. Jeremy Ford. Also set forth below is a description of our incentive plans, pursuant to which the awards included in the "Outstanding Equity Awards at Fiscal Year-End 2013" below were made to our named executive officers. The Compensation Committee believes that the arrangements described below serve our interests and the interests of our stockholders because they help secure the continued employment and dedication of our named executive officers prior to or following a change in control, without concern for their own continued employment.

Employment Contracts

Mr. White

On November 30, 2012, in connection with our acquisition of PlainsCapital, we entered into a retention agreement with Mr. White. The term of the retention agreement is three years, with automatic one-year renewals at the end of the second year of the agreement and each anniversary thereof unless notice has been given otherwise. Pursuant to the agreement, Mr. White's annual base salary is $1,350,000. He is also entitled to an annual bonus that varies based upon the performance of PlainsCapital. If PlainsCapital's annual net income is less than or equal to $70,000,000 but greater than $15,000,000, Mr. White is entitled to a bonus equal to the average of his annual bonus in the prior three calendar years. If PlainsCapital's annual net income exceeds $70,000,000, he is entitled to a bonus equal to 100% of his annual base salary. Additionally, in accordance with the agreement, Mr. White is entitled to participate in all of the Company's employee benefit plans and programs. Further, the agreement provides that the Company will provide Mr. White with the use of a corporate aircraft and an automobile allowance, each at the same level that such benefits were available to Mr. White immediately prior to our acquisition of PlainsCapital. He continues to have bank-owned life insurance and access to the country club that was available to him through PlainsCapital's membership prior to our acquisition of PlainsCapital. For a description of compensation and benefits to which Mr. White is entitled in the event of his termination or a change in control, see "Potential Payments Upon Termination or Change-in-Control" below.

Mr. Huffines

PlainsCapital previously entered into an employment agreement with Mr. Huffines. In connection with our acquisition of PlainsCapital, we entered into an amendment to the employment agreement with Mr. Huffines, which became effective upon the closing of the acquisition on November 30, 2012 and, among other things, removed his minimum guaranteed bonus. The term of the employment agreement is two years. The annual base salary under the agreement is $650,000. Mr. Huffines is entitled to an annual bonus to be determined by our Compensation Committee. For a description of compensation and benefits to which Mr. Huffines is entitled in the event of his termination or a change in control, see "Potential Payments Upon Termination or Change-in-Control" below.

Mr. Schaffner

On November 30, 2012, in connection with our acquisition of PlainsCapital, we entered into a retention agreement with Mr. Schaffner. The term of the retention agreement is two years, with automatic one-year renewals at the end of the first year of the agreement and each anniversary thereof unless notice has been given otherwise. Pursuant to the agreement, Mr. Schaffner's annual base salary is $525,000. He is also entitled to an annual bonus that varies based upon the performance of PlainsCapital. If PlainsCapital's annual net income is greater than $15,000,000, Mr. Schaffner is entitled to a bonus equal to the average of his annual bonus in the prior three calendar years. Additionally, in accordance with the agreement, Mr. Schaffner is entitled to participate in all of the Company's employee benefit plans and programs. Further, the agreement provides that the Company will provide Mr. Schaffner with the use of corporate aircraft and an automobile allowance, each at the same level that such benefits were available to Mr. Schaffner immediately prior to our acquisition of PlainsCapital. He continues to have bank-owned life insurance and access to the country club that was available to him through PlainsCapital's membership prior to our acquisition of PlainsCapital. For a description of compensation and benefits to which Mr. Schaffner is entitled in the event of his termination or a change in control, see "Potential Payments Upon Termination or Change-in-Control" below.

Equity Incentive Plans

On December 23, 2003, we adopted the 2003 Equity Incentive Plan, which provides for the grant of equity-based awards, including restricted shares of our common stock, stock options, grants of shares and other equity-based incentives, to our directors, officers and other employees and certain of our subsidiaries selected by our Compensation Committee. At inception, 1,992,387 shares were authorized for issuance pursuant to this plan. All shares granted and outstanding pursuant to the plan, whether vested or unvested, are entitled to receive dividends and to vote, unless forfeited. No participant in our 2003 Equity Incentive Plan may be granted awards in any fiscal year representing more than 500,000 shares of our common stock.

On September 20, 2012, our stockholders approved the 2012 Equity Incentive Plan, and as a result, we may no longer grant awards pursuant to the 2003 Equity Incentive Plan. However, all awards that were previously granted and outstanding under the 2003 Equity Incentive Plan will remain in full force and effect according to their respective terms and dividend equivalents may continue to be issued in respect of awards that were outstanding thereunder as of September 20, 2012.

The 2012 Equity Incentive Plan provides for the grant of equity-based awards, including restricted shares of our common stock, restricted stock units, stock options, grants of shares, stock appreciation rights (SARs) and other equity-based incentives, to our directors, officers and other employees and those of our subsidiaries selected by our Compensation Committee. At inception, 4,000,000 shares were authorized for issuance pursuant to this plan. All shares granted and outstanding pursuant to this plan, whether vested or unvested, are entitled to receive dividends and to vote, unless forfeited. No participant in our 2012 Equity Incentive Plan may be granted performance-based equity awards in any fiscal year representing more than 500,000 shares of our common stock or stock options or SARs representing in excess of 750,000 shares of our common stock. The maximum number of shares underlying incentive stock options granted under this plan may not exceed 2,000,000.

The 2003 Equity Incentive Plan and the 2012 Equity Incentive Plan are administered by our Compensation Committee, which has the discretion to, among other things, determine the persons to whom awards will be granted, the number of shares of our common stock to be subject to awards and the other terms and conditions of the awards. The Compensation Committee also has authority to establish performance goals for purposes of determining cash bonuses to be paid under the incentive plans. Such performance goals may be applied to our Company as a whole, any of our subsidiaries or affiliates, and/or any of our divisions or strategic business units, and may be used to evaluate performance relative to a market index or a group of other companies. Further, the Compensation Committee has the authority to adjust the performance goals in recognition of unusual or non-recurring events. The 2003 Equity Incentive Plan and the 2012 Equity Incentive Plan each provide that in no event will the Compensation Committee be authorized to reprice stock options, or to lower the base or exercise price of any other award granted under such plan, without obtaining the approval of our stockholders.

Stock options granted under the 2003 Equity Incentive Plan and the 2012 Equity Incentive Plan may be either "incentive stock options" within the meaning of Section 422 of the Internal Revenue Code, or nonqualified stock options. Generally, holders of restricted stock will be entitled to vote and receive dividends on their restricted shares, but our Compensation Committee may determine, in its discretion, whether dividends paid while the shares are subject to restrictions may be reinvested in additional shares of restricted stock. Except as otherwise permitted by our Compensation Committee, awards granted under the 2003 Equity Incentive Plan and the 2012 Equity Incentive Plan will be transferable only by will or through the laws of descent and distribution, and each stock option will be exercisable during the participant's lifetime only by the participant or, upon the participant's death, by his or her estate. Director compensation paid in the form of our common stock, whether at our or the director's election, is issued through the 2012 Equity Incentive Plan.

Annual Incentive Plan

On September 20, 2012, our stockholders approved the Annual Incentive Plan, which provides for a cash bonus to key employees of Hilltop and our subsidiaries who are selected by the Compensation Committee for participation in the plan. The Annual Incentive Plan is intended to permit the payment of amounts that constitute "performance-based compensation" under Section 162(m) of the Internal Revenue Code and is designed to reward executives whose performance during the fiscal year enabled Hilltop to achieve favorable business results and to assist Hilltop in attracting and retaining executives. A participant may receive a cash bonus under the Annual Incentive Plan based on the attainment, during each performance period, of performance objectives in support of our business strategy that are established by our Compensation Committee. These performance objectives may be based on one or more of the following criteria:

- stock price
- earnings (including earnings before interest, taxes, depreciation and amortization)
- earnings per share (whether on pre-tax, after-tax, operations or other basis)
- operating earnings
- total return to shareholders
- ratio of debt to debt plus equity
- net borrowing
- credit quality or debt ratings
- return on assets or operating assets
- asset quality
- net interest margin
- loan portfolio growth
- efficiency ratio
- deposit portfolio growth
- liquidity
- market share
- objective customer service measures or indices
- shareholder value added

embedded value added

loss ratio

expense ratio

combined ratio

premiums

premium growth

investment income

pre- or after-tax income

net income

cash flow (before or after dividends)

expense or expense levels

economic value added

cash flow per share (before or after dividends)

free cash flow

gross margin

risk-based capital

revenues

revenue growth

sales growth

return on capital (including return on total capital or return on invested capital)

capital expenditures

cash flow return on investment

cost

cost control

gross profit

operating profit

economic profit

profit before tax

net profit

cash generation

unit volume

sales

net asset value per share

asset quality

cost saving levels

market-spending efficiency

core non-interest income

change in working capital

The performance objectives may be applied with respect to Hilltop or any one or more of our subsidiaries, divisions, business units or business segments and may be applied to performance relative to a market index or a group of other companies. The Compensation Committee may adjust the performance goals applicable to any awards to reflect any unusual or non-recurring events.

Participation in the Annual Incentive Plan does not guarantee the payment of an award. All awards payable pursuant to the Annual Incentive Plan are discretionary and subject to approval by our Compensation Committee. After the performance period ends, the Compensation Committee will determine the payment amount of individual awards based on the achievement of the performance objectives. No participant in the Annual Incentive Plan may receive an award that exceeds $10,000,000 per year. Except as otherwise provided in a participant's employment or other individual agreement, the payment of a cash bonus to a participant for a performance period will be conditioned upon the participant's active employment on the date that the final awards are approved by the Compensation Committee. We may amend or terminate the Annual Incentive Plan at any time.

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Outstanding Equity Awards at Fiscal Year End

The following tables presents information pertaining to all outstanding equity awards held by the named executive officers as of December 31, 2013.

Outstanding Equity Awards at Fiscal Year End Table

Fiscal Year 2013

	Option Awards				Stock Awards	
Name	**Number of securities underlying unexercised options (#) exercisable**	**Number of securities underlying unexercised options (#) unexercisable**	**Option exercise price(b) ($)**	**Option expiration date**	**Number of shares or units that have not vested (#)**	**Market value of shares or units of stock that have not vested(c) ($)**
Jeremy B. Ford President & Chief Executive Officer	300,000(a)	200,000(a)	7.70	November 2, 2016	30,000	693,900
Darren Parmenter Executive Vice President Principal Financial Officer					10,000	231,300
Alan B. White Chief Executive Officer of PlainsCapital Corporation					50,000	1,156,500
James R. Huffines Chief Operating Officer of PlainsCapital Corporation					30,000	693,900
Jerry L. Schaffner Chief Executive Officer of PlainsCapital Bank					20,000	462,600

(a) These stock options vested or will vest in five equal installments on each of November 2, 2011, 2012, 2013, 2014 and 2015.

(b) Represents the exercise price of the stock option held by Mr. Jeremy Ford, which is the average of the high and low sales price of Company common stock on the date of grant of the stock option.

(c) Based upon the closing price of Company common stock on December 31, 2013.

Option Exercises and Stock Vested in 2013

During the fiscal year ended December 31, 2013, none of our named executive officers exercised any options to purchase shares of common stock or held any outstanding awards of restricted stock, restricted stock units or similar instruments that vested.

Non-Qualified Deferred Compensation

The following table shows the non-qualified deferred compensation activity for our named executive officers during the fiscal year ended December 31, 2013.

Name	Executive contributions in last fiscal year ($)	Registrant contributions in last fiscal year ($)(1)	Aggregate earnings in last fiscal year ($)(1)	Aggregate withdrawals/ distributions ($)	Aggregate balance at last fiscal year end ($)
Alan B. White			$ 28,950		$ 6,460,932
Jerry L. Schaffner			$ 11,016		$ 2,459,952

(1) All amounts reported as registrant contributions in last fiscal year and aggregate earnings in last fiscal year are reported as compensation in the last completed fiscal year in the Summary Compensation Table.

In connection with acquisition of PlainsCapital, we entered into retention agreements with Messrs. White and Schaffner. Pursuant to those agreements, we agreed to contribute an amount in cash equal to $6,430,890 and $2,448,000 as deferred compensation to Messrs. White and Schaffner, respectively, in satisfaction of their respective rights under Section 6 (Termination Upon Change of Control) of their respective previous employment agreements with PlainsCapital. Such amounts accrue interest at the prevailing money market rate and are payable to Messrs. White and Schaffner on the 55th day following termination of their respective employment.

Potential Payments Upon Termination or Change-in-Control

The 2012 Equity Incentive Plan, under which we have granted awards to the named executive officers, contains specific termination and change in control provisions. We determined to include a change in control provision in the plan to be competitive with what we believe to be the standards for the treatment of equity upon a change in control for similar companies and so that employees who remain after a change in control would be treated the same with regard to equity as the general stockholders who could sell or otherwise transfer their equity upon a change in control. Under the terms of the plan, if a change in control (as defined below in the discussion of the plan) were to occur, all awards then outstanding would become vested and/or exercisable and any applicable performance goals with respect thereto would be deemed to be fully achieved.

Employment Contracts

With respect to each of Messrs. Huffines, Schaffner and White, if his employment or retention contract is terminated by us for cause, by the executive or due to the executive's death or disability (as such terms are defined below), he or his estate, as applicable, is entitled to:

(i) his annual base salary through the date of termination, to the extent not already paid and not deferred;

(ii) any annual bonus earned by the executive for a prior award period, to the extent not already paid and not deferred;

(iii) any business expenses he incurred that are not yet reimbursed as of the date of termination; and

(iv) any other amounts or benefits, including all unpaid and/or vested, nonforfeitable amounts owing or accrued to him, required to be paid or provided or which he is eligible to receive under any plan, program, policy or practice or contract or agreement, to the extent not already paid and not deferred, through the date of termination.

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In addition, Messrs. White and Schaffner or their respective estates, as applicable, are entitled to a lump-sum cash payment equal to $6,430,890 and $2,448,000, respectively, which represents the amount Messrs. White and Schaffner, respectively, would have been entitled to receive under their respective prior employment agreements with PlainsCapital if their respective employment there was terminated. Such amounts described in the preceding paragraph are referred to as the "Accrued Amounts."

For Mr. Huffines, if his employment is terminated by us without cause (as such term is defined below), he is entitled to the Accrued Amounts, as well as a cash amount equal to the sum of:

(i) his annual base salary rate; and

(ii) the average of the bonuses he received for each of the three calendar years immediately preceding the year of termination of his employment.

Such amount is payable in a lump-sum within 60 days of the effective date of the termination of the executive's employment.

If Mr. White's employment is terminated by us other than for cause (as such term is defined below) or his death or disability, or if his employment terminates due to non-renewal by us, he is entitled to the Accrued Amounts, including the lump-sum cash payment equal to $6,430,890 and interest thereon from November 30, 2012, as well as payments generally equal to the sum of the average of Mr. White's prior annual bonuses over the preceding three years plus his annual base salary, multiplied by the greater of (i) the number of full and partial years remaining until the end of the term of his retention agreement and (ii) two. Mr. White will retain the right to be grossed-up for any excise tax relating to "excess parachute payments" (as defined in Section 280G of the Internal Revenue Code), which is set forth in his prior employment agreement, provided that the gross-up will only relate to any excise taxes arising in connection with our acquisition of PlainsCapital. These severance amounts are payable subject to Mr. White's execution of a release of claims.

If Mr. Schaffner's employment is terminated by us other than for cause (as such term is defined below) or his death or disability, he is entitled to the Accrued Amounts, including the lump-sum cash payment equal to $2,448,000 and interest thereon from November 30, 2012, as well as payments generally equal to the sum of the average of Mr. Schaffner's prior annual bonuses over the preceding three years plus his annual base salary. Mr. Schaffner will retain the right to be grossed-up for any excise tax relating to "excess parachute payments" (as defined in Section 280G of the Internal Revenue Code), which is set forth in his prior employment agreement, provided that the gross-up will only relate to any excise taxes arising in connection with our acquisition of PlainsCapital. These severance amounts are payable subject to Mr. Schaffner's execution of a release of claims.

For Mr. Huffines, in the event that his employment is terminated (a) by us without cause within the 24 months immediately following, or the six months immediately preceding, a change in control (as such term is defined below), or (b) by Mr. Huffines for good reason (as such term is defined below) within the 24 months immediately following, or the six months immediately preceding, a change in control, he is entitled to the Accrued Amounts, as well as a cash amount equal to three times the sum of:

(i) his annual base salary rate; and

(ii) the greater of (A) the annual bonus paid or payable with respect to the calendar year prior to the calendar year in which the effective date of such termination of employment occurs and (B) the average of the bonuses he received for each of the three calendar years immediately preceding the year of termination of his employment.

Such amount is payable in a lump-sum within 60 days of the effective date of the termination of his employment, subject to the execution of a release of claims. In addition, Mr. Huffines is entitled to continued participation in our benefit plans for a period of two years following the date of his termination, and full vesting of all outstanding stock options then held, with the option to receive a cash payment equal to the then difference between the option price and the current fair market value of the stock as of the effective date of such termination of employment in lieu of the right to exercise such options. In the event that any of the benefits payable upon a termination of employment in connection with a change in control would constitute "excess parachute payments," such benefits would be reduced to the level necessary such that no excise tax will be due. Messrs. White's and Schaffner's respective retention agreements do not provide for such payments upon a change in control.

Pursuant to his employment agreement, Mr. Huffines will not, during the term of his employment agreement and for a period of one year following the earlier of his termination or the termination of the agreement, compete with any business that provides services similar to us anywhere within the State of Texas. Pursuant to their respective retention agreements, Messrs. White and Schaffner will not, during the period of their employment and for three and two years, respectively, following their respective termination: (i) solicit any person who is employed by us or any of our affiliates; (ii) interfere with our relationships with our customers, suppliers or other business contacts; nor (iii) compete with any business that provides services similar to us anywhere within the State of Texas. Messrs. White and Schaffner have also agreed that all confidential records, material and information concerning us or our affiliates shall remain our exclusive property and they shall not divulge such information to any person.

For the purposes of each employment or retention contract described above:

- "cause" means: (i) an intentional act of fraud, embezzlement or theft in connection with the executive's duties or in the course of his employment with the Company or our affiliates; (ii) intentional wrongful damage to property of the Company or our affiliates; (iii) intentional wrongful disclosure of trade secrets or confidential information of the Company or our affiliates; (iv) intentional violation of any law, rule or regulation (other than traffic violations or similar offenses) or a final "Cease and Desist Order;" (v) intentional breach of fiduciary duty involving personal profit; or (vi) intentional action or inaction that causes material economic harm to the Company or our affiliates.

For the purposes of Messrs. White's and Schaffner's retention agreements:

- "disability" means he shall have been absent from full-time performance of his duties for 180 consecutive days as a result of incapacity due to physical or mental illness that is determined to be total and permanent by a physician.

For the purposes of the employment agreement with Mr. Huffines:

- the acquisition of PlainsCapital constituted a "change in control";

- "disability" is defined in accordance with our disability policy in effect at the time of the disability; and

- "good reason" means (i) without his express written consent, the assignment to Mr. Huffines of any duties materially inconsistent with his positions, duties, responsibilities and status as then in effect or a significant material diminishment in his titles or offices as then in effect, or any removal of Mr. Huffines from or any failures to re-elect executive to any of such positions, in any case, subject to certain exceptions; (ii) a significant and material adverse diminishment in the nature or scope of the authorities, powers, functions or duties attached to the position with which Mr. Huffines had immediately prior to a change in control or a reduction in Mr. Huffines's aggregate base salary without his prior written consent; (iii) the Company relocates its principal executive offices or requires Mr. Huffines to have as his principal location of work any location which is in excess of fifty (50) miles from the location thereof immediately prior to a change in control; or (iv) any substantial and material breach of his employment agreement by the Company.

Set forth below are the amounts that Messrs. Ford, Parmenter, White, Huffines and Schaffner would have received if the specified events had occurred on December 31, 2013.

Jeremy B. Ford	Termination for Cause	Termination due to death or disability	Termination without cause	Change of Control
Accrued Amounts	$	$	$	$
Cash Payment				
Cash Severance				
Stock Options(1)				3,086,000
Restricted Stock(2)		154,200	154,200	693,900
Welfare Benefits				
Total	$	$ 154,200	$ 154,200	$ 3,779,900

(1) Pursuant to the provisions of the 2003 Equity Incentive Plan under which issuances of stock option awards were made, if a change in control event, as defined under the plan, were to occur, all awards then outstanding would become vested and, if applicable, exercisable and any applicable performance goals with respect thereto would be deemed to be fully achieved. The Company has the discretion to require payment by the option holder of any amount it deems necessary to satisfy its liability to withhold income or any other taxes incurred by reason of exercise of options. Further, pursuant to the terms of the non-qualified stock option agreements that govern the issuance of options, upon the death of the option holder all options become fully vested and exercisable. Represents the value of unvested stock option grants that would vest upon a change in control, assuming a change in control event on the last business day of 2013. The value realized assumes the exercise of all stock options that became vested as a result of the event and is calculated as the difference between the option exercise price per share and the closing market price of $23.13 on December 31, 2013.

(2) The restricted stock vests ratably upon the death or disability of the participant or termination of the participant without cause. The foregoing assume the death or disability or termination of the participant without cause on December 31, 2013. If a change of control under the 2012 Equity Incentive Plan occurs, all unvested restricted stock vest upon such event, which for purposes of the foregoing assumes December 31, 2013.

Darren Parmenter	Termination for Cause	Termination due to death or disability	Termination without cause	Change of Control
Accrued Amounts	$	$	$	$
Cash Payment				
Cash Severance				
Stock Options				
Restricted Stock(1)		51,400	51,400	231,300
Welfare Benefits				
Total	$	$ 51,400	$ 51,400	$ 231,300

(1) The restricted stock vests ratably upon the death or disability of the participant or termination of the participant without cause. The foregoing assume the death or disability or termination of the participant without cause on December 31, 2013. If a change of

control under the 2012 Equity Incentive Plan occurs, all unvested restricted stock vest upon such event, which for purposes of the foregoing assumes December 31, 2013.

Alan B. White	**Termination for Cause**	**Termination due to death or disability or by Executive for any Reason**	**Termination without cause or non-renewal of retention agreement**	**Change of Control**
Accrued Amounts(1)	$ 1,350,000	$ 1,350,000	$ 1,350,000	$
Cash Payment(2)	6,431,982	6,431,982	6,431,982	
Cash Severance(3)			4,879,753	
Stock Options				
Restricted Stock(4)		257,000	257,000	1,156,500
Welfare Benefits				
Total	$ 7,781,982	$ 8,038,982	$ 12,918,735	$ 1,156,500

(1) Accrued Amounts calculation based upon the sum of: (i) Mr. White's annual base salary through December 31, 2013, to the extent not already paid and not deferred; (ii) any annual bonus earned, to the extent not already paid and not deferred; (iii) any business expenses incurred that have not yet been reimbursed as of the date of termination; and (iv) any other amounts or benefits, including all unpaid and/or vested, nonforfeitable amounts owing or accrued to Mr. White.

(2) Cash Payments refers to a lump-sum cash payment that represents the amount, including interest thereon, Mr. White would have been entitled to receive under his prior employment agreement with PlainsCapital if his employment had been terminated.

(3) Cash Severance calculation based upon the sum of the average of Mr. White's prior annual bonuses for each of the preceding three years plus his annual base salary, multiplied by the greater of: (i) the number of full and partial years remaining until the end of the term of his employment agreement and (ii) two.

(4) The restricted stock vests ratably upon the death or disability of the participant or termination of the participant without cause. The foregoing assume the death or disability or termination of the participant without cause on December 31, 2013. If a change of control under the 2012 Equity Incentive Plan occurs, all unvested restricted stock vest upon such event, which for purposes of the foregoing assumes December 31, 2013.

James R. Huffines	**Termination for Cause**	**Termination due to death or disability**	**Termination without cause**	**Change of Control**
Accrued Amounts(1)	$	$	$	$
Cash Payment				
Cash Severance(2)			1,027,567	3,726,000
Stock Options				
Restricted Stock(3)		154,200	154,200	693,900
Welfare Benefits				
Total	$	$ 154,200	$ 1,181,767	$ 4,419,900

(1) Accrued Amounts calculation based upon the sum of: (i) Mr. Huffines annual base salary through December 31, 2013, to the extent not already paid and not deferred; (ii) any annual bonus earned, to the extent not already paid and not deferred; (iii) any business expenses incurred that have not yet been reimbursed as of the date of termination; and

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(iv) any other amounts or benefits, including all unpaid and/or vested, nonforfeitable amounts owing or accrued to Mr. Huffines.

(2)

Cash severance calculation if Mr. Huffines is terminated without cause is based upon the sum of: (i) Mr. Huffines' annual base salary rate and (ii) the average of the bonuses he received for each of the last three calendar years immediately preceding the year of termination of his employment. If his employment is terminated upon a change in control, the cash severance calculation is based upon three times the sum of: (i) Mr. Huffines' annual base salary rate and (ii) the greater of (A) the annual bonus paid or payable with respect to the calendar year prior to the calendar year in which termination occurs and (B) the averages of the bonuses he received for each of the last three calendar years immediately preceding the year of termination of his employment.

(3)

The restricted stock vests ratably upon the death or disability of the participant or termination of the participant without cause. The foregoing assume the death or disability or termination of the participant without cause on December 31, 2013. If a change of control under the 2012 Equity Incentive Plan occurs, all unvested restricted stock vest upon such event, which for purposes of the foregoing assumes December 31, 2013.

Jerry L. Schaffner	**Termination for Cause**	**Termination due to death or disability or by Executive for any Reason**	**Termination without cause**	**Change of Control**
Accrued Amounts(1)	$ 525,000	$ 525,000	$ 525,000	$
Cash Payment(2)	2,448,000	2,448,000	2,448,000	
Cash Severance(3)			896,667	
Stock Options				
Restricted Stock(4)		102,800	102,800	462,600
Welfare Benefits				
Total	$ 2,973,000	$ 3,075,800	$ 3,972,467	$ 462,600

(1)

Accrued Amounts calculation based upon the sum of: (i) Mr. Schaffner's annual base salary through December 31, 2013, to the extent not already paid and not deferred; (ii) any annual bonus earned, to the extent not already paid and not deferred; (iii) any business expenses incurred that have not yet been reimbursed as of the date of termination; and (iv) any other amounts or benefits, including all unpaid and/or vested, nonforfeitable amounts owing or accrued to Mr. Schaffner.

(2)

Cash Payments refers to a lump-sum cash payment that represents the amount, including interest thereon, Mr. Schaffner would have been entitled to receive under his prior employment agreement with PlainsCapital if his employment had been terminated.

(3)

Cash Severance calculation based upon the sum of the average of Mr. Schaffner's prior annual bonuses for each of the preceding three years plus his annual base salary.

(4)

The restricted stock vests ratably upon the death or disability of the participant or termination of the participant without cause. The foregoing assume the death or disability or termination of the participant without cause on December 31, 2013. If a change of control under the 2012 Equity Incentive Plan occurs, all unvested restricted stock vest upon such event, which for purposes of the foregoing assumes December 31, 2013.

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Incentive Plans

Each of the incentive plans has a complex definition of "change in control". Generally speaking, under the 2003 Equity Incentive Plan, a change in control occurs if: (i) with certain exceptions, any person becomes the owner of 50% or more of the combined voting power of our outstanding stock and other voting securities; (ii) a majority of the directors serving on our Board of Directors are replaced other than by new directors approved by at least two-thirds of the members of our Board of Directors; (iii) we are not the surviving company after a merger or consolidation; or (iv) with certain exceptions, our stockholders approve a plan of complete liquidation or dissolution or an agreement for the sale or disposition of all or substantially all of our assets is consummated. Under the 2012 Equity Incentive Plan, a change in control occurs if: (i) with certain exceptions, any person becomes the owner of 33% or more of the outstanding shares of our common stock or the combined voting power of our outstanding stock and other voting securities; (ii) a majority of the directors serving on our Board of Directors are replaced other than by new directors approved by at least two-thirds of the members of our Board of Directors; (iii) we are not the surviving company after a merger or consolidation or sale of all or substantially all of our assets; or (iv) with certain exceptions, our stockholders approve a plan of complete liquidation or dissolution.

Both our 2003 Equity Incentive Plan and our 2012 Equity Incentive Plan are "single trigger" plans, meaning that stock option acceleration occurs upon a change in control even if the award holder remains with us after the change in control, regardless of whether awards are assumed or substituted by the surviving company. We believe a "single trigger" change in control provision was appropriate because it allows management to pursue all alternatives for us without undue concern for their own financial security.

In the event of a change in control, all awards then outstanding under the 2003 Equity Incentive Plan will become vested and, if applicable, exercisable, and any performance goals imposed with respect to then-outstanding awards will be deemed to be fully achieved. With respect to awards granted pursuant to the 2012 Equity Incentive Plan, in the event of a change in control: (i) all outstanding stock options and SARs will become fully vested and exercisable; (ii) all restrictions on any restricted stock, restricted stock units or other stock-based awards that are not subject to performance goals will become fully vested; and (iii) all restrictions on any restricted stock, restricted stock units, performance units or other stock-based awards that are subject to performance goals will be deemed to be fully achieved.

In addition to acceleration of benefits upon a change in control event, the non-qualified stock option agreements pursuant to which all option awards are granted provide for acceleration of vesting upon the death of the option holder. No other rights of acceleration are provided for under the terms of the Company's benefit plans.

Compensation Committee Interlocks and Insider Participation

During fiscal year 2013, directors Rhodes Bobbitt, W. Joris Brinkerhoff, William T. Hill, Jr., Andrew J. Littlefair and A. Haag Sherman served on the Compensation Committee. During fiscal year 2013:

- none of the members of our Compensation Committee is, or has ever been, one of our officers or employees;
- none of the members of our Compensation Committee had any relationships with the Company requiring disclosure under "Certain Relationships and Related Party Transactions";
- none of our executive officers served as a member of the compensation committee of another entity, one of whose executive officers served on our Compensation Committee;

none of our executive officers served as a director of another entity, one of whose executive officers served on our Compensation Committee; and

none of our executive officers served as a member of the compensation committee of another entity, one of whose executive officers served as one of our directors.

Each of Mr. White, PlainsCapital's Chief Executive Officer, Mr. Martin, PlainsCapital's Executive Vice President and Chief Financial Officer, Mr. Huffines, PlainsCapital's Chief Operating Officer, and Mr. Schaffner, President and Chief Executive Officer of PlainsCapital Bank, serves as a director of First Southwest, a wholly owned subsidiary of PlainsCapital. Hill A. Feinberg serves as the Chief Executive Officer of First Southwest and on the Board of Directors of Hilltop. Hilltop's Compensation Committee is comprised of independent directors, reviews and sets the compensation of each of Messrs. White, Martin, Feinberg, Huffines and Schaffner and does not believe that these interlocks pose any risks that are likely to have a material adverse effect on us.

Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Exchange Act requires officers and directors, and persons who beneficially own more than ten percent of our stock, to file initial reports of ownership and reports of changes in ownership with the SEC. Officers, directors and greater than ten percent beneficial owners are required by SEC regulations to furnish us with copies of all Section 16(a) forms they file.

Based solely on a review of the copies furnished to us and representations from our officers and directors, we believe that all Section 16(a) filing requirements for the year ended December 31, 2013, applicable to our officers, directors and greater than ten percent beneficial owners were timely satisfied except for the failure to file one Form 4 by each of Gerald J. Ford and Carl B. Webb, each of whom received a distribution of common stock in a transaction that he did not initiate. Further, Diamond A Financial, L.P. did not file a Form 3 or subsequent Forms 4; however, such transactions were reported on Mr. Gerald Ford's Section 16 filings. Mr. Green has failed to file a Form 4 reporting the redemption by the Company of partnership units in July 2007.

Based on written representations from our officers and directors, we believe that all Forms 5 for directors, officers and greater than ten percent beneficial owners that have been filed with the SEC are the only Forms 5 required to be filed for the period ended December 31, 2013.

Certain Relationships and Related Party Transactions

General

Transactions with related persons are governed by our General Code of Ethics and Business Conduct, which applies to all officers, directors and employees. This code covers a wide range of potential activities, including, among others, conflicts of interest, self-dealing and related party transactions. Waiver of the policies set forth in this code will only be permitted when circumstances warrant. Such waivers for directors and executive officers, or that provide a benefit to a director or executive officer, may be made only by the Board of Directors, as a whole, or the Audit Committee of the Board of Directors and must be promptly disclosed as required by applicable law or regulation. Absent such a review and approval process in conformity with the applicable guidelines relating to the particular transaction under consideration, such arrangements are not permitted.

Management Services Agreement

Prior to December 2012, Diamond A Administration Company, LLC, or Diamond A, an affiliate of Gerald J. Ford, the current Chairman of the Board of Hilltop and the beneficial owner of 17.2% of Hilltop common stock as of April 8, 2014, provided certain management services to Hilltop and its subsidiaries, including, among others, financial and acquisition evaluation, and office space to Hilltop, pursuant to a Management Services Agreement. The services and office space were provided at a cost of $91,500 per month, plus reasonable out-of-pocket expenses. The services provided under this agreement included those of several of Hilltop's directors, including Gerald J. Ford, Kenneth Russell and Carl B. Webb. Prior to Jeremy B. Ford assuming the role of Chief Executive Officer of Hilltop, he provided services to Hilltop under the Management Services Agreement. The Management Services Agreement was terminated upon our acquisition of PlainsCapital. Hilltop also agreed to indemnify and hold harmless Diamond A for its performance or provision of these services, except for gross negligence and willful misconduct. Further, Diamond A's maximum aggregate liability for damages under this agreement is limited to the amounts paid to Diamond A under this agreement during twelve months prior to that cause of action.

Jeremy B. Ford, a director and the Chief Executive Officer of Hilltop, is the beneficiary of a trust that owns a 49% limited partnership interest in Diamond A Financial, L.P. Diamond A Financial, L.P. owns 17.2% of the outstanding Hilltop common stock at April 8, 2014. He also is a director and the Secretary of Diamond A, which provided management services to Hilltop under the Management Services Agreement described in the preceding paragraph. Diamond A is owned by Hunter's Glen/Ford, Ltd., a limited partnership in which a trust for the benefit of Jeremy B. Ford is a 46% limited partner. The spouse of Corey G. Prestidge is the beneficiary of a trust that also owns a 46% limited partnership interest in Hunter's Glen/Ford, Ltd. and a trust that owns a 49% limited partnership interest in Diamond A Financial, L.P.

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

Hilltop Sublease

In connection with our acquisition of PlainsCapital, we terminated the Management Services Agreement described above. Hilltop, however, desired to continue to occupy the office space provided pursuant to the Management Services Agreement. Accordingly, Hilltop entered into a sublease with Hunter's Glen/Ford, Ltd., an affiliate of Mr. Gerald J. Ford and the tenant of the office space (See "Management Services Agreement" above for further discussion regarding Hunter's Glen/Ford, Ltd.) on December 1, 2012. The Sublease is subject to the base Lease and on the same terms as the base Lease. Pursuant to the Sublease, until February 27, 2014, Hilltop leased 5,491 square feet for $219,640 annually, plus additional rent due of $1,168 for the month of December 2012 and $14,975 for 2013 under the base Lease. On February 28, 2014, the parties amended the Sublease to increase the square footage subleased to 6,902 square feet, increase the rent based on such additional square footage, and extend the term to July 31, 2018. Hilltop pays the same rate per square foot as Hunter's Glen/Ford, Ltd. is required to pay under the base Lease, as amended.

The NLASCO Acquisition

ARC Insurance Holdings Inc., or Holdings, a subsidiary of us, on the one hand, and C. Clifton Robinson, C.C. Robinson Property Company, Ltd. and The Robinson Charitable Remainder Unitrust, on the other hand, entered into a stock purchase agreement, dated as of October 6, 2006, or the NLASCO Agreement. Pursuant to the NLASCO Agreement, on January 31, 2007, Holdings acquired all of the outstanding shares of capital stock of NLASCO, Inc., or NLASCO, a privately held property and casualty insurance holding company domiciled in the state of Texas. In exchange for the stock, NLASCO's shareholders, consisting of C. Clifton Robinson and affiliates, as specified above, received $105.75 million in cash and 1,218,880 shares of our common stock issued to Mr. Robinson, for a total consideration of $122.0 million. The NLASCO Agreement included customary representations, warranties and covenants, as well as indemnification provisions. The purchase price was subject to specified post-closing adjustments that resulted in the following additional aggregate consideration paid to Mr. Robinson and his affiliates: $2,852,879 on March 16, 2010 and $252,997 on March 25, 2011. As a result of these payments, no further post-closing adjustments are required under the stock purchase agreement. The parties also entered into several ancillary agreements, including a non-competition agreement, a registration rights agreement, a release, employment agreements and a share lock-up agreement.

C. Clifton Robinson Relationship with Hilltop

In furtherance of the terms of the NLASCO Agreement, C. Clifton Robinson, Chairman of NLASCO and a member of our Board of Directors, entered into certain ancillary agreements with us or NLASCO, including, among others, an employment agreement, a non-competition agreement, a lock-up agreement and a registration rights agreement.

In conjunction with the closing of the NLASCO acquisition, NLASCO entered into an employment agreement with C. Clifton Robinson that provides that he was to serve as chairman of NLASCO and would be paid $100,000 a year. In addition, NLASCO entered into an employment agreement with Mr. Robinson's son, Gordon B. Robinson, the former vice chairman and deputy chief executive officer of NLASCO, pursuant to which he was to serve in an advisory capacity to NLASCO and for which he would be paid $100,000 per year. Each employment agreement was for a one-year term with automatic one-year extensions by agreement of the parties. Both of these agreements were terminated on January 1, 2011. The employment agreements also included non-competition and non-solicitation provisions similar to that in the non-competition agreement discussed below, but with terms until two years after the termination of employment. Further, each of the Robinsons entered into a non-competition agreement pursuant to which he agreed not to, directly or indirectly, engage or invest in, own, manage, operate, finance, control, or participate in the ownership, management, operation, financing, or control of, be employed by, lend credit to, or render services to, any business whose products, services or activities compete with those of NLASCO or any of its subsidiaries within certain states. Each non-competition agreement included customary non-solicitation provisions. The term of the non-competition agreements was five years, and such agreements expired in January 2012. Finally, C. Clifton Robinson executed a share lock-up agreement pursuant to which he agreed not to offer, sell, contract to sell, hypothecate, pledge, sell or grant any option, right or warrant to purchase, or otherwise dispose of, or contract to dispose of, our common stock until 20 months after the closing date of the NLASCO acquisition. This lock-up agreement expired in September 2008. Upon the closing of the NLASCO acquisition in January 2007, NLASCO became our wholly-owned subsidiary.

Mr. Robinson was elected to our board of directors in March 2007 pursuant to the terms of the NLASCO Agreement.

Assumption of NLASCO, Inc. Subsidiary Office Leases

With the acquisition of all of the capital stock of NLASCO, we also assumed all assets and liabilities of its wholly-owned subsidiaries. Prior to Mr. Robinson's disposition of his office building on August 24, 2011, NLASCO and its affiliates in Waco, Texas leased office space from affiliates of Mr. Robinson. There were three separate leases. The first lease was a month-to-month lease for office space at a rate of $900 per month. The second lease was a month-to-month lease at a monthly rental rate of $3,500 per month. The first and second leases were terminated in August 2010. The third lease, as amended, currently requires payments of $40,408 per month and expires on December 31, 2014, but does have renewal options at the discretion of the lessee. Aggregate office space under lease with regard to the foregoing is approximately 28,863 square feet.

The PlainsCapital Acquisition

Hilltop and PlainsCapital entered into an Agreement and Plan of Merger, dated as of May 8, 2012, pursuant to which we acquired PlainsCapital on November 30, 2012. Pursuant to the Agreement and Plan of Merger, PlainsCapital's shareholders, which included Ms. Anderson and Messrs. Bolt, Feinberg, Huffines, Lewis, Littlefair, Martin, Salmans, Schaffner, Sherman, Taylor and White, received 0.776 shares of Hilltop common stock and $9.00 in cash for each share of PlainsCapital's outstanding common stock they held. Based on Hilltop's closing stock price on November 30, 2012, the total purchase price in the PlainsCapital acquisition was $813.5 million, consisting of $311.8 million in cash and the issuance of 27.1 million shares of common stock and 114,068 shares of Non-Cumulative Perpetual Preferred Stock, Series B. In addition, Mrs. Anderson and Messrs. Bolt, Feinberg, Huffines, Lewis, Littlefair, Sherman, Taylor and White were appointed to serve as members of our Board of Directors. The Agreement and Plan of Merger contained customary representations, warranties and covenants, as well as indemnification provisions.

Consultant

We are currently paying Richard P. Hodge $80,000 per year for tax services. Mr. Hodge also provides tax services to Mr. Gerald Ford and his affiliates.

Employment of Certain Family Members

During 2013, Corey Prestidge, the brother-in-law of Jeremy B. Ford, our President and Chief Executive Officer, and the son-in-law of Gerald J. Ford, the Chairman of our Board, served as Hilltop's General Counsel and Secretary; Lee Ann White, the wife of Alan B. White, PlainsCapital's Chairman and Chief Executive Officer, served as our Senior Vice President, Director of Public Relations; and Kale Salmans, the son of Todd Salmans, Chief Executive Officer of PrimeLending, served as a Regional Manager of PrimeLending. Pursuant to our employment arrangements with these individuals, we paid Corey Prestidge $575,000, Lee Ann White $147,500 and Kale Salmans $275,000 as compensation for their services as employees during 2013.

Cowboys Stadium Suite

In 2007, PlainsCapital Bank contracted with Cowboys Stadium, L.P., a company affiliated with the employer of Ms. Anderson and that is beneficially owned by Ms. Anderson and certain of her immediate family members, for the 20-year lease of a suite at Cowboys Stadium beginning in 2009. Pursuant to the lease agreement, PlainsCapital Bank has agreed to pay Cowboys Stadium, L.P. annual payments of $500,000, subject to possible annual escalations, not to exceed 3% per year, beginning with the tenth year of the lease.

Indebtedness

The Bank has had, and may be expected to have in the future, lending relationships in the ordinary course of business with our directors and executive officers, members of their immediate families and affiliated companies in which they are employed or in which they are principal equity holders. In our management's opinion, the lending relationships with these persons were made in the ordinary course of business and on substantially the same terms, including interest rates, collateral and repayment terms, as those prevailing at the time for comparable transactions with persons not related to us and do not involve more than normal collection risk or present other unfavorable features.

Principal Stockholders of Hilltop

The following table sets forth information regarding our common stock beneficially owned on April 8, 2014 by any person or "group," as that term is used in Section 13(d)(3) of the Exchange Act, known to us to beneficially own more than five percent of the outstanding shares of our common stock.

Name and Addresss of Beneficial Owner	Amount and Nature of Beneficial Ownership	Percent of Class(a)
Gerald J. Ford(b) 200 Crescent Court, Suite 1350 Dallas, Texas 75201	15,548,160	17.2%
Burgundy Asset Management Ltd.(c) 181 Bay Street, Suite 4510 Toronto, Ontario M5J 2T3	4,655,202	5.2%

(a) Based on 90,177,991 shares of common stock outstanding on April 8, 2014. Shares issuable under instruments to purchase our common stock that are exercisable within 60 days of April 8, 2014 are treated as if outstanding for computing the percentage ownership of the person holding these instruments, but are not treated as outstanding for purposes of computing the percentage ownership of any other person.

(b) The shares of common stock beneficially owned by Mr. Ford include 15,544,674 shares owned by Diamond A Financial, LP. Mr. Ford is the sole general partner of Diamond A Financial, LP. Mr. Ford has sole voting and dispositive power of these shares.

(c) Based upon Schedule 13G/A (Amendment No. 3) filed on February 3, 2014. Burgundy Asset Management Ltd. has sole voting power with respect to 2,953,642 of these shares and sole dispositive power with respect to all of these shares. Clients for whom Burgundy Asset Management Ltd. acts as investment adviser may withdraw dividends or proceeds from the sale securities from the accounts managed by Burgundy Asset Management Ltd. No one client of Burgundy Asset Management Ltd. has an interest in the common stock of Hilltop in excess of five percent of the total outstanding shares.

Security Ownership of Hilltop Management

The following table sets forth information regarding the number of shares of our common stock beneficially owned on April 8, 2014, by:

- each of our directors;
- each of our named executive officers; and
- all of our directors and executive officers presently serving, as a group.

Except as otherwise set forth below, the address of each of the persons listed below is c/o Hilltop Holdings Inc., 200 Crescent Court, Suite 1330, Dallas, Texas 75201. Except as otherwise indicated in the footnotes to this table, the persons named in the table have specified that they have sole voting and investment power with respect to all shares of stock shown as beneficially owned by them, subject to any applicable community property law.

Name of Beneficial Owner	Common Stock Amount and Nature of Beneficial Ownership	Percent of Class(a)
Charlotte Jones Anderson	4,405	*
Rhodes Bobbitt	126,059(b)	*
Tracy A. Bolt	6,608	*
W. Joris Brinkerhoff	35,228	*
Charles R. Cummings	37,476	*
Hill A. Feinberg	1,376,552(c)	1.5%
Gerald J. Ford 200 Crescent Court, Suite 1350 Dallas, Texas 75201	15,548,160(d)	17.2%
Jeremy B. Ford	392,500(e)	*
J. Markham Green	119,152	*
Jess T. Hay		*
William T. Hill, Jr.	48,350(f)	*
James R. Huffines	354,731(g)	*
Lee Lewis	656,199(h)	*
Andrew J. Littlefair	12,948	*
W. Robert Nichols, III	41,000(i)	*
Darren Parmenter	5,361(j)	*
C. Clifton Robinson	1,218,880	1.4%
Kenneth D. Russell		*
Jerry L. Schaffner	88,546(k)	*
A. Haag Sherman	14,422	*
Robert C. Taylor, Jr.	29,918	*
Carl B. Webb	104,462	*
Alan B. White	2,327,338(l)	2.6%
All Directors and Named Executive Officers, as a group (26 persons)	22,776,434(m)	25.2%

* Represents less than 1% of the outstanding shares of such class.

(a) Based on 90,177,991 shares of common stock outstanding on April 8, 2014. Shares issuable under instruments to purchase our common stock that are exercisable within 60 days of April 8, 2014 are treated as if outstanding for computing the percentage ownership of the person holding these instruments, but are not treated as outstanding for purposes of computing the percentage ownership of any other person.

(b) Includes 62,100 shares of common stock held in an IRA account for the benefit of Mr. Bobbitt.

(c) Includes 25,776 shares of common stock held directly by Mr. Feinberg's wife. Also includes 776 shares of common stock held by the Max McDermott Trust for the benefit of Mr. Feinberg's stepson. Mr. Feinberg's wife is the trustee of the trust. Includes 15,000 restricted shares of common stock that cliff vest on April 11, 2016. Mr. Feinberg can vote such restricted shares but may not dispose of them until they have vested. Excludes 8,887 shares of common stock deliverable upon the vesting of restricted stock units that will not vest within 60 days of April 8, 2014.

(d)
The shares of common stock beneficially owned by Mr. Ford include 15,544,674 shares owned by Diamond A Financial, LP. Mr. Ford is the sole general partner of Diamond A Financial, LP. Mr. Ford has sole voting and dispositive power of these shares.

(e)
Jeremy Ford is a beneficiary of a trust that owns a 49% limited partnership interest in Diamond A Financial, LP (see footnote (d)). Includes (a) 300,000 shares of common stock acquirable upon the exercise of a stock option and (b) 30,000 restricted shares of common stock that cliff vest on April 1, 2016. Mr. Jeremy Ford can vote such restricted shares but may not dispose of them until they have vested. Excludes (x) 200,000 shares of common stock acquirable upon the exercise of a stock option that will not vest within 60 days of April 8, 2014, (y) 25,392 shares of common stock deliverable upon the vesting of restricted stock units that will not vest within 60 days of April 8, 2014 and (z) 15,544,674 shares of common stock held by Diamond A Financial, LP.

(f)
Includes 7,300 shares of common stock held in a SEP IRA account for the benefit of Mr. Hill and 15,750 shares of common stock held by the William T. Hill P.C. retirement account for the benefit of Mr. Hill.

(g)
Includes 952 shares of common stock allocated to an account pursuant to the Plains Capital Corporation Employee Stock Ownership Plan (the "ESOP") for the benefit of Mr. Huffines. Each ESOP participant has the right to direct the ESOP trustees how to vote the shares allocated to his account and may therefore be deemed to beneficially own such shares. Also includes (a) 47,000 shares of common stock held by the James Huffines 1994 Trust for the benefit of Mr. Huffines, (b) 11,077 shares of common stock held in a self-directed individual retirement account and (c) 30,000 restricted shares of common stock that cliff vest on April 1, 2016. Mr. Huffines can vote such restricted shares but may not dispose of them until they have vested. Excludes 17,774 shares of common stock deliverable upon the vesting of restricted stock units that will not vest within 60 days of April 8, 2014.

(h)
Includes 603,417 shares of common stock held by Lee Lewis Construction. Mr. Lewis is the sole owner of Lee Lewis Construction and may be deemed to have voting and/or investment power with respect to the shares owned by Lee Lewis Construction.

(i)
Includes 11,000 shares of common stock held in an IRA account for the benefit of Mr. Nichols.

(j)
Includes 5,000 restricted shares of common stock that cliff vest on April 1, 2016. Mr. Parmenter can vote such restricted shares but may not dispose of them until they have vested. Excludes 7,406 shares of common stock deliverable upon the vesting of restricted stock units that will not vest within 60 days of April 8, 2014.

(k)
Includes 36,920 shares of common stock allocated to an account pursuant to the ESOP for the benefit of Mr. Schaffner. Each ESOP participant has the right to direct the ESOP trustees how to vote the shares allocated to his account and may therefore be deemed to beneficially own such shares. Also includes (a) 3,931 shares of common stock held directly by Mr. Schaffner's wife, (b) 11,970 shares of common stock held in a self-directed individual retirement account and (c) 20,000 restricted shares of common stock that cliff vest on April 1, 2016. Mr. Schaffner can vote such restricted shares but may not dispose of them until they have vested. Excludes 11,849 shares of common stock deliverable upon the vesting of restricted stock units that will not vest within 60 days of April 8, 2014.

(l)
Includes (a) 9,785 shares of common stock held directly by Mr. White's wife, (b) 454 shares of common stock allocated to the ESOP account of Mr. White's wife, (c) 23,806 shares of common stock held by Double E Investments ("Double E"), (d) 12,883 shares of common stock held by EAW White Family Partnership, Ltd. ("EAW"), (e) 8,045 shares of common stock held by Maedgen, White and Maedgen ("MW&M"), (f) 1,853,958 shares of common stock held by Maedgen & White, Ltd., and (g) 952 shares of common stock allocated to an account pursuant to

the ESOP for the benefit of Mr. White. Each ESOP participant has the right to direct the ESOP trustees how to vote the shares allocated to his account and may therefore be deemed to beneficially own such shares. As the manager of Double E, the managing partner of MW&M and the sole member of the general partner of EAW, Mr. White has exclusive authority to vote and/or dispose of the securities held by Double E, MW&M and EAW, respectively, and may, therefore, be deemed to have sole voting and dispositive power over the shares of common stock held by Double E, MW&M and EAW. Mr. White is the sole general partner of Maedgen & White, Ltd. and may be deemed to beneficially own the shares held by Maedgen & White, Ltd. As the sole general partner of Maedgen & White, Ltd., Mr. White has the power to vote the shares held by Maedgen & White, Ltd. The Agreement of Limited Partnership of Maedgen & White, Ltd. requires the approval of 80% of the limited partnership interests in Maedgen & White, Ltd. before its general partner may dispose of the shares held by Maedgen & White, Ltd. Mr. White, directly and indirectly, controls approximately 77% of the limited partnership interests of Maedgen & White, Ltd. and therefore may be deemed to share dispositive power over the shares held by Maedgen & White, Ltd. Includes 50,000 restricted shares of common stock that cliff vest on April 1, 2016. Mr. White can vote such restricted shares but may not dispose of them until they have vested. Excludes 29,623 shares of common stock deliverable upon the vesting of restricted stock units that will not vest within 60 days of April 8, 2014.

(m) Represents 26 persons and includes (a) 360,000 shares of common stock acquirable pursuant to the exercise of stock options and (b) 210,000 restricted shares of common stock that cliff vest on April 1, 2016. The holders of such restricted shares can vote the restricted shares but may not dispose of them until they have vested. Excludes (x) 240,000 shares of common stock acquirable by our executive officers pursuant to the exercise of stock options that will not vest within 60 days of April 8, 2014 and (y) 140,076 shares of common stock deliverable upon the vesting of restricted stock units that will not vest within 60 days of April 8, 2014.

INFORMATION ABOUT THE COMPANIES SWS

SWS, a Delaware corporation, is a savings and loan holding company with principal executive offices at 1201 Elm Street, Suite 3500, Dallas, Texas 75270. The telephone number of SWS's executive offices is (214) 859-1800, and its Internet website address is www.swsgroupinc.com. SWS is focused on delivering a broad range of investment banking, commercial banking and related financial services to corporate, individual and institutional investors, broker/dealers, governmental entities and financial intermediaries. SWS is the largest full-service brokerage firm headquartered in the Southwestern United States (based on the number of financial advisors). SWS conducts its banking business through its wholly owned subsidiary, Southwest Securities, FSB, a federally chartered savings bank.

SWS's common stock is listed on the New York Stock Exchange under the symbol "SWS."

INFORMATION ABOUT THE COMPANIES PERUNA LLC

Peruna LLC, a Delaware limited liability company, is a wholly owned subsidiary of Hilltop. Peruna LLC is newly formed, and was organized for the purpose of effecting the merger. Other than those incident to its formation and the matters contemplated by the merger agreement, Peruna LLC has engaged in no business activities to date and it has no material assets or liabilities of any kind.

THE MERGER

Terms of the Merger

Each of Hilltop's and SWS's respective boards of directors has approved the merger agreement. The merger agreement provides for the merger of SWS with and into Peruna LLC, a subsidiary of Hilltop, with Peruna LLC continuing as the surviving entity. In the merger, each share of SWS common stock, par value $0.10 per share, issued and outstanding immediately prior to the completion of the merger will be converted into the right to receive $1.94 in cash and 0.2496 of Hilltop common stock. No fractional shares of Hilltop common stock will be issued in connection with the merger, and holders of SWS common stock will be entitled to receive cash in lieu thereof. Immediately following the completion of the merger, SWS's wholly owned bank subsidiary, Southwest Securities, FSB, will merge with and into Hilltop's wholly owned bank subsidiary, PlainsCapital Bank. PlainsCapital Bank will be the surviving bank in the bank merger.

SWS stockholders are being asked to approve the merger agreement. See "The Merger Agreement" included elsewhere in this proxy statement/prospectus for additional and more detailed information regarding the legal documents that govern the merger, including information about the conditions to the completion of the merger and the provisions for terminating and amending the merger agreement.

Background of the Merger

As part of their ongoing consideration and evaluation of SWS's long-term prospects and strategies, the SWS Board and senior management have regularly reviewed and assessed SWS's business strategies and objectives, including potential strategic opportunities, all with the goal of enhancing value for its stockholders. These potential strategic opportunities, from time to time, have included, among other things, the consideration of potential business combination transactions.

On July 29, 2011, in response to ongoing challenging business conditions and to ensure that Southwest Securities, FSB, the bank subsidiary of SWS, was able to maintain its required level of regulatory capital, SWS entered into a credit agreement (the "Credit Agreement") with Hilltop and Oak Hill Capital Partners III, L.P. and Oak Hill Capital Management Partners III, L.P. (together, "Oak Hill") pursuant to which each of Hilltop and Oak Hill made a $50 million loan to SWS, certain proceeds of which were invested in Southwest Securities, FSB. SWS also issued each of Hilltop and Oak Hill warrants to purchase 8,695,652 shares of common stock at an exercise price of $5.75 per share (the "Warrants").

The terms of the Credit Agreement include a covenant prohibiting SWS, subject to certain exceptions, from undergoing a "Fundamental Change," which includes any merger, amalgamation or consolidation (the "Merger Covenant"), and which SWS would breach by engaging in a merger, amalgamation or consolidation unless compliance were waived by each lender thereunder.

The Merger Covenant specifically provides that while any loans are outstanding under the Credit Agreement, SWS may not merge, consolidate or amalgamate, or liquidate, wind up or dissolve itself (or suffer any liquidation or dissolution), or dispose of all or substantially all of its assets or business, except that SWS or any of its subsidiaries may merge or consolidate with any person; provided that (A) in the case of any merger or consolidation involving SWS, SWS shall be the continuing or surviving corporation and the stockholders of SWS immediately prior to such merger or consolidation shall hold at least a majority of the outstanding shares of the combined entity immediately after the consummation of such merger or consolidation; (B) in the case of any merger or consolidation involving SWS or its subsidiaries that are party to the Credit Agreement, the surviving entity shall be a party to the Credit Agreement; and (C) in the case of any merger or consolidation involving a subsidiary of SWS that is a registered broker-dealer, the surviving entity shall be a registered broker-dealer;

The Credit Agreement also prohibits SWS from prepaying the loan other than following a period during which the closing price for SWS common stock exceeds 150% of the exercise price of the Warrants (or $8.625) for twenty out of any thirty consecutive trading days. In connection with these transactions, Mr. Gerald J. Ford of Hilltop and Mr. J. Taylor Crandall of Oak Hill were appointed to the SWS Board. These transactions were approved by the SWS stockholders.

On January 9, 2014, Hilltop delivered an unsolicited offer to the President and Chief Executive Officer of SWS proposing, subject to the approval of the SWS Board and subsequent approval by SWS stockholders, a transaction in which the public stockholders of SWS would receive $7.00 per share, to be paid 50% in cash and 50% in Hilltop common stock. On January 10, 2014, Hilltop issued a press release and filed an amended Schedule 13D disclosing the proposal. Also on January 10, 2014, SWS issued a press release announcing its receipt of Hilltop's proposal letter.

On January 15, 2014, the SWS Board met and discussed Hilltop's offer and appropriate next steps to consider taking, including the creation of a committee of the SWS Board to be composed solely of directors not affiliated with Hilltop, in light of the potential for actual or perceived conflicts of interest presented by Hilltop's relationship with SWS. The SWS Board discussed SWS's business plan, industry trends and the potential for increasing stockholder value through implementation of SWS's business initiatives. The SWS Board also considered the prospects of SWS, the public markets' valuation of SWS and other companies in SWS's industry and the potential challenges to achieving its business plan. The SWS Board also discussed the need to repay the loans under the Credit Agreement in full on July 28, 2016, or to refinance such loans. After evaluation of Hilltop's offer and discussion of potential strategic alternatives, the SWS Board determined that SWS should explore potential strategic alternatives available to SWS, including a possible sale of SWS to Hilltop or another party, with the goal of maximizing stockholder value. To address the potential for actual or perceived conflicts of interest, the SWS Board determined that it would be prudent to form a committee of directors from SWS's Board not affiliated with Hilltop or Oak Hill consisting of Robert A. Buchholz, Christie S. Flanagan and Tyree B. Miller, to lead the review of Hilltop's offer and other strategic alternatives. The Special Committee members were selected due to their disinterested and non-executive status, their knowledge and experience, and their ability and willingness to devote a sufficient amount of time to their service on the Special Committee. The SWS Board also authorized the Special Committee to retain any external advisors that it deemed necessary to fulfill its duties. The Special Committee retained Davis Polk & Wardwell LLP ("Davis Polk") as its legal advisor on January 29, 2014 and Sandler O'Neill + Partners, L.P. ("Sandler O'Neill") as its financial advisor on February 3, 2014, after discussion with a number of investment banks and law firms. On January 30, 2014, the Special Committee held a meeting to discuss the role, responsibilities and composition of the Special Committee, and after further consideration recommended that the SWS Board replace Christie S. Flanagan as a member of the Special Committee with Joel T. Williams III.

On February 3, 2014, the SWS Board adopted formal resolutions ratifying the formation of the Special Committee and the establishment of its powers. The SWS Board selected Robert A. Buchholz, Tyree B. Miller and Joel T. Williams III as the members of the Special Committee with Mr. Miller as chairman. The SWS Board authorized the Special Committee to explore, review, reject, evaluate and negotiate Hilltop's offer and the strategic alternatives that were available to SWS, including empowering the Special Committee to, among other things, determine and recommend to the SWS Board whether a potential transaction was advisable and fair to and in the best interests of the stockholders of SWS and to retain and compensate advisors to the Special Committee. The Special Committee was not obligated to recommend either Hilltop's offer or any other strategic alternative and the resolutions provided that (i) the Special Committee could not approve the execution of any definitive agreement evidencing the final terms of any strategic alternative but would instead submit its

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recommendation of any such agreement to the SWS Board and (ii) the SWS Board would not approve any strategic alternative without the affirmative recommendation of the Special Committee.

On February 4, 2014, Sandler O'Neill received a call from Esposito Global, LLC ("Esposito Global") expressing interest in acquiring SWS's retail business, but not its bank subsidiary. Following that call, on February 12, 2014, the Special Committee received a letter from Esposito Global which stated that Esposito Global was prepared to make a proposal, conditioned on Esposito Global undertaking and completing due diligence, to acquire all the outstanding shares of SWS common stock for per share consideration of $8.00 in cash.

At a February 13, 2014 meeting of the Special Committee, in which members of SWS senior management and representatives of the Special Committee's financial and legal advisors participated, Sandler O'Neill made a presentation to the Special Committee on various financial aspects of potential strategic alternatives available to SWS, including Hilltop's offer and the Esposito Global proposal, taking into account various factors such as financial projections prepared by SWS management. Representatives of Davis Polk reviewed with the Special Committee the fiduciary duties of the Special Committee members applicable to their consideration of Hilltop's offer and other potential strategic alternatives. Further, the Special Committee discussed with Sandler O'Neill recent communications received by Sandler O'Neill from parties expressing interest in a possible transaction with SWS, including the letter from Esposito Global. The Special Committee discussed, among other things, the alternatives to a sale of SWS as a whole including the significant risks of SWS continuing to operate some or all of its lines of business on a standalone basis. The Special Committee noted, among other things, that SWS was not generating earnings, that it was subscale in all of its principal business lines, that it continually failed to meet budgets, which led to concerns as to the ability to achieve targets in the future, and that it would be required to repay or refinance amounts due under the Credit Agreement in 2016. The Special Committee agreed that it would be in the best interests of SWS and its stockholders to explore the range of strategic alternatives, including a possible sale of SWS, that were reasonably available to SWS with the goal of maximizing stockholder value.

The Special Committee considered the possible disruption to SWS's business that could result from the public announcement of an exploratory process that might involve the sale of SWS and the resulting distraction of the attention of SWS management and employees, concluding that such risks could be minimized by proceeding with an exploratory process on a non-public basis. In particular the Special Committee was concerned with the risk of loss of key employees. The Special Committee felt that such employee losses not only would adversely affect SWS in the event there were no transaction for SWS, but, under some circumstances, might also adversely affect SWS's ability to enter into, or maximize stockholder value in, a transaction.

The Special Committee also noted the fact that Hilltop's unsolicited offer had been publicized in a press release by Hilltop and described in Hilltop's Amended Statement on Schedule 13D, and the fact that SWS had issued a press release with respect to this offer, including indicating that a Special Committee had been formed. As a result, the Special Committee believed that the financial markets were fully aware that SWS was the subject of takeover interest and that any party having an interest in a strategic transaction with SWS was likely to contact one or both of SWS and its financial advisor.

The Special Committee therefore requested that Sandler O'Neill assist with a confidential outreach to an identified group of third parties that the Special Committee and Sandler O'Neill felt might be interested in acquiring SWS and by detailing to such parties the benefits of a transaction with SWS. A group of potential acquirors was identified by selecting parties that were financially capable of effecting such a transaction, would be reasonably likely to obtain the necessary regulatory approvals without material conditions to consummate such a transaction and might be interested in acquiring SWS or, subsequent to the public disclosure of Hilltop's offer, had expressed to SWS or Sandler O'Neill an interest in a strategic transaction with SWS.

Following the February 13, 2014 meeting, and in accordance with the Special Committee's instructions, Sandler O'Neill began to contact potential interested parties to encourage and determine levels of interest in a transaction involving the potential acquisition of SWS. During the course of its engagement, Sandler O'Neill contacted a total of seventeen parties (which included all of the parties that had contacted SWS or Sandler O'Neill on their own) that the Special Committee and Sandler O'Neill believed might be interested in a strategic transaction with SWS, including, on February 18, 2014, making contact with representatives of a financial institution referred to as "Party A".

On February 14, 2014, in order to provide the Special Committee with greater flexibility in soliciting and considering offers from third parties, representatives of Davis Polk, at the request of the Special Committee, called Wachtell, Lipton, Rosen & Katz, counsel to Hilltop ("Wachtell Lipton"), to request that Hilltop agree to waive the Merger Covenant. Wachtell Lipton stated that it would convey the request to Hilltop. Also, at the request of the Special Committee, representatives of Sandler O'Neill had preliminary discussions with a representative of Hilltop regarding Hilltop's offer, including with respect to regulatory matters and due diligence.

On February 18, 2014, Esposito Global publicly disclosed its proposal to acquire all the outstanding shares of SWS common stock for $8.00 per share in cash. The proposal was expressly contingent on third party financing being arranged.

On February 20, 2014, the Special Committee held a meeting in which members of SWS senior management and representatives of the Special Committee's financial and legal advisors participated. At the meeting, Sandler O'Neill reviewed with the Special Committee the results of certain financial analyses Sandler O'Neill had performed and its exploration of certain alternatives to a sale of SWS as a whole, including SWS continuing as a standalone business, SWS selling Southwest Securities, FSB, the bank subsidiary of SWS, and continuing to operate its other lines of business, and SWS breaking itself up through the separate sale of each of SWS's business units. Sandler O'Neill informed the Special Committee that the results of its analysis showed, as compared to a sale of SWS as a whole, that none of these options was likely to increase stockholder value and that each would carry significant timing and/or execution risks. It was also noted that separating the lines of business would be problematic because of linkages between them. The representatives of Sandler O'Neill also stated that they believed that they had made initial contact with all of the parties that would likely be interested in acquiring SWS. Following discussion, the Special Committee directed Sandler O'Neill to schedule a meeting with Hilltop to discuss its offer, to contact Esposito Global to obtain additional information relating to its acquisition proposal, including its plans for arranging outside financing and its ability to obtain required regulatory approvals, and to continue discussions with other potentially interested parties, including Party A.

During this period, Sandler O'Neill and SWS received various unsolicited calls from other third parties expressing a preliminary interest in a possible transaction involving SWS and Sandler O'Neill also had preliminary discussions with a number of parties it contacted at the direction of the Special Committee. However, for a variety of reasons, including that a number of these parties expressed an interest only in purchasing select assets or divisions (which, as discussed above and taking into consideration the analysis of Sandler O'Neill, the Special Committee believed would not maximize stockholder value) and the regulatory hurdles that some parties would face in order to acquire the whole of SWS, none of these third parties continued to pursue a transaction with SWS after the early stage contact.

On February 21, 2014, representatives of Davis Polk and Wachtell Lipton had a call regarding the Merger Covenant. Wachtell Lipton indicated that Hilltop was not prepared to grant a waiver of the Merger Covenant to permit a third party transaction.

At the request of the Special Committee, on February 24, 2014, representatives of Davis Polk discussed with Esposito Global's counsel, Esposito Global's plans with respect to the regulatory process approvals that would be required to consummate their proposed transaction, particularly with respect to SWS's bank subsidiary. Esposito Global's counsel acknowledged that Esposito Global would require additional resources to meet applicable regulatory requirements and pay the purchase price and stated that it was in the process of assembling those resources.

On or about February 26, 2014, representatives of Davis Polk called Oak Hill's outside counsel to request that Oak Hill consider waiving the Merger Covenant. Oak Hill's outside counsel subsequently informed representatives of Davis Polk that, assuming as part of any merger transaction the debt held by Oak Hill pursuant to the Credit Agreement would be prepaid in accordance with the terms of the Credit Agreement (at an amount equal to principal plus the "make whole" payment specified in the Credit Agreement), the director appointed by Oak Hill to the SWS Board would expect to recommend to Oak Hill's investment committee that Oak Hill waive the Merger Covenant with regard to any transaction at or above Hilltop's offer of $7.00 per share. Oak Hill's outside counsel also confirmed that Oak Hill was not requesting different consideration in respect of its Warrants than it would be entitled to as a stockholder on exercise of its Warrants.

On February 26, 2014, the Special Committee held a meeting, in which members of SWS senior management and representatives of the Special Committee's financial and legal advisors participated, to discuss the status of Sandler O'Neill's and Davis Polk's communications with various interested parties. Following discussion, the Special Committee directed Sandler O'Neill to schedule a meeting with Hilltop to discuss its offer, to contact Esposito Global to obtain additional information relating to its acquisition proposal, including its plans for arranging outside financing, and to continue discussions with other potentially interested parties, including Party A.

On February 27, 2014, representatives of Davis Polk and Sandler O'Neill had a call with representatives of Esposito Global and its counsel to discuss Esposito Global's plans to arrange the outside financing required to support its offer and to manage the regulatory process with respect to acquiring a bank. Esposito Global stated that it planned to work with an established bank holding company, Party B, that would take the lead role in any potential transaction.

In late February 2014, representatives of Party A and Sandler O'Neill had several calls discussing Party A's interest in acquiring SWS at a price that Party A said it expected would be close to the tangible book value of SWS's "liquid assets," which Sandler O'Neill believed to approximate the fully diluted tangible book value of $8.15 per share. In subsequent conversations prior to March 18, 2014, Party A referred to its indication of interest at a price of $8.15 per share.

On February 28, 2014, at the request of the Special Committee, Sandler O'Neill sent draft non-disclosure agreements to each of Party A and Hilltop.

On March 3, 2014, representatives of Sandler O'Neill and of Davis Polk spoke with representatives of Esposito Global and Party B. During that conversation, Party B stated that it was interested in acquiring SWS, but that it and Esposito Global would need to obtain significant external financing in order to consummate a transaction with SWS, that they expected that at least three separate private equity firms would need to participate in the financing to avoid additional regulatory issues and that the financing process would likely take eight weeks or longer.

On March 3, 2014, the Special Committee held a meeting, in which members of SWS senior management and representatives of the Special Committee's financial and legal advisors participated, to discuss the status of Sandler O'Neill's and Davis Polk's communications with various interested parties. The representatives of Sandler O'Neill stated at this meeting that they believed that Sandler O'Neill had been in contact with all of the parties that would likely be interested in acquiring SWS, and that only four parties remained interested (Hilltop, Esposito Global, Party A and, working with Esposito Global, Party B). Representatives of Sandler O'Neill and Davis Polk discussed with the Special Committee their call earlier in the day with representatives of Esposito Global and Party B. The

Special Committee discussed concerns related to the financing and timing risks of a potential transaction with Esposito Global and Party B. In addition, the representatives of Sandler O'Neill reported that on March 3, 2014, they received a call from representatives of Hilltop requesting the Special Committee to respond to Hilltop's offer and enter into direct negotiations.

Following discussion, the Special Committee concluded that Hilltop's offer of $7.00 per share undervalued SWS and was inadequate. The Special Committee directed Sandler O'Neill to inform Hilltop that the Special Committee rejected the offer of $7.00 per share. After the representatives of Sandler O'Neill left the meeting, the Special Committee concluded that it would be desirable, in the interest of maximizing the possible price obtained for a sale of SWS, to amend the Special Committee's engagement letter with Sandler O'Neill to provide for an incentive fee to be paid in the event that SWS were acquired at a per share price above $7.75, and on March 5, 2014, the Special Committee and Sandler O'Neill entered into an amendment to the Sandler O'Neill engagement letter providing for such an incentive fee arrangement.

On March 4, 2014, a representative of Sandler O'Neill discussed with representatives of Hilltop the Special Committee's rejection of Hilltop's offer of $7.00 per share and informed Hilltop that SWS had received indications of interest from other credible bidders at prices approximating fully diluted tangible book value ($8.15 per share). Hilltop's representatives stated that Hilltop would not waive the Merger Covenant including with respect to a transaction with a third party at that value.

On March 5, 2014, the Special Committee held a meeting, in which members of SWS senior management and representatives of the Special Committee's financial and legal advisors participated, to discuss Hilltop's refusal to waive the Merger Covenant and how the existence of the Merger Covenant might affect discussions with other potential acquirers. The Special Committee also discussed further the risks inherent in sharing certain confidential information with the interested parties, particularly Party A, as a direct competitor of SWS, including the importance of protecting SWS's business by ensuring that SWS's confidential information was only shared pursuant to a non-disclosure agreement with, among other things, an appropriate employee non-solicit provision and ensuring that any proposals received from such interested parties were genuine before providing extensive confidential information.

Later on March 5, 2014, representatives of Sandler O'Neill and Davis Polk had a call with representatives of Esposito Global and Party B. Esposito Global and Party B indicated that they would need at least thirty to sixty days to complete their due diligence review and arrange for the financing required for their offer and that they would not be able to confirm their price until the due diligence review was complete and they had arranged for all required financing.

Following the March 5, 2014 Special Committee meeting, at the request of the Special Committee Sandler O'Neill called Hilltop to tell its representatives that the Company was worth at least tangible book value of $8.15 per share. Hilltop indicated that it did not believe that book value was the correct method to value SWS, based on, among other things, its lack of earnings and prospective earnings.

On the morning of March 6, 2014, Party A sent Sandler O'Neill a due diligence request for SWS of items they considered high priority. On a call between representatives of Party A and Sandler O'Neill that same day, Party A inquired whether Hilltop and Oak Hill were willing to waive the Merger Covenant, and the representative of Sandler O'Neill indicated its understanding that Oak Hill might be willing to do so, but that Hilltop had stated that it would not.

On March 7, 2014, the Special Committee held a meeting, in which members of SWS senior management and representatives of the Special Committee's financial and legal advisors participated, to discuss the status of Sandler O'Neill's and Davis Polk's communications with various interested parties. The Special Committee discussed its concerns that (i) providing certain confidential information about its employees, and in particular its top revenue-generating employees, to Party A would expose SWS to the risk that Party A might recruit such employees, (ii) if it became publicly known that Party A were interested in acquiring SWS, SWS's employees might become concerned about possible employment reductions or other employment changes and start seeking alternative employment, and (iii) there was a risk Party A might be seeking confidential information of SWS for competitive purposes rather than to pursue a transaction. The Special Committee concluded that at this stage Party A should be permitted to share SWS's confidential information with only a select group of its employees and representatives and SWS should provide only certain due diligence materials to Party A, and not information identifying individual SWS employees. The Special Committee also directed Sandler O'Neill to arrange for an in-person meeting to discuss Hilltop's offer and the appropriate valuation of SWS.

On March 13, 2014, representatives of Sandler O'Neill and Esposito Global/Party B had a call to discuss the status of Esposito Global/Party B's efforts to obtain the financing they required to complete a transaction with SWS. The representatives of Party B indicated that they were in the process of interviewing investment banks but had not reached out to any potential financing sources. In addition, Party B's representatives stated that they estimated that their process for diligence and raising financing would take approximately eight weeks.

On March 13, 2014, the Special Committee held a meeting, in which members of SWS senior management and representatives of the Special Committee's financial and legal advisors participated, to discuss the status of negotiations with Hilltop, Party A and Esposito Global/Party B. At this meeting, the Special Committee discussed the timing and process for providing the due diligence information requested by Party A. The members of the Special Committee also discussed their concern that Esposito Global/Party B would be unable to obtain the outside financing they require in a timely manner, if at all, and the inherent execution risks that this would pose.

On March 15, 2014, SWS and Hilltop executed a non-disclosure agreement to allow for the sharing of confidential information relating to the parties.

On March 16, 2014 and March 17, 2014, Sandler O'Neill and Party A had a series of calls regarding the Merger Covenant and its impact on a potential sale. The Chief Executive Officer of Party A inquired specifically about whether Hilltop would agree to waive the Merger Covenant. Sandler O'Neill told Party A that Hilltop had stated that it would not be willing to do so.

On March 17, 2014, representatives of Sandler O'Neill requested that Esposito Global/Party B provide SWS with a focused due diligence request list and additional details on their plans for arranging financing for their offer, including the timing of such financing. Party B's financial advisor indicated that Esposito Global/Party B would require sixty days in order to secure such financing and finalize its price.

On March 17, 2014, representatives of the Special Committee, Hilltop and Sandler O'Neill met to discuss Hilltop's offer. During this meeting, Hilltop indicated that its goals were to have SWS's debt to Hilltop under the Credit Agreement repaid in accordance with its terms and to have an opportunity to acquire SWS. Hilltop also indicated that its offer had been outstanding for over two months and that Hilltop was unwilling to continue to participate in a lengthy process. Mr. Miller told Hilltop that the Special Committee and SWS would be willing and able to consider moving quickly to a possible transaction if Hilltop were to offer a price approximating SWS's fully diluted tangible book value of $8.15 per share. Hilltop indicated to Mr. Miller that it did not believe that book value was the correct method to value SWS and that the value of SWS was meaningfully below book value. Because the Special Committee believed that Hilltop stock was an attractive currency, Mr. Miller also asked Hilltop to increase the stock portion of its offer from 50% to 100% and, on this point, Hilltop responded that, although it could not increase the stock portion of its offer to 100%, it would increase it to an amount greater than 50%. At the conclusion of this meeting, Hilltop expressed frustration with the time the process was taking and stated that it would submit a revised offer to SWS within two days.

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Later on March 17, 2014, the Special Committee held a meeting, in which members of SWS senior management and representatives of the Special Committee's financial and legal advisors participated, to discuss recent communications with Hilltop, Party A and Esposito Global/Party B and how to move forward with each interested party. The Special Committee also discussed the risks that Esposito Global/Party B would not be able to find the outside financing they required, and the delays inherent with such process, and that Hilltop might withdraw its offer if the Special Committee's discussions with other interested parties entailed significant additional delay. Following discussion, the Special Committee directed Sandler O'Neill to ask Party A to sign the non-disclosure agreement and to request from Esposito Global/Party B their due diligence request list.

On March 18, 2014, representatives of Party A and Sandler O'Neill had a call to discuss Party A's interest in acquiring SWS. The Chief Executive Officer of Party A stated that Party A valued SWS at a price of approximately $8.00 per share, although it could potentially be higher, and that Party A had discussed the Merger Covenant with Hilltop's financial advisor and that Hilltop's financial advisor told Party A that Hilltop would not waive the Merger Covenant to permit a third party sale.

On March 19, 2014, Hilltop submitted a revised offer to SWS to acquire all of the outstanding common stock of SWS that Hilltop did not already own at a price of $7.50 per share, composed of 25% cash and 75% Hilltop common stock. In delivering the revised offer, Hilltop indicated to representatives of Sandler O'Neill that it was approaching its limit, in terms of price, and was not prepared to leave its offer outstanding for a prolonged period. Hilltop also stated that it was prepared to move forward quickly, had already begun preparing a draft merger agreement, and would require minimal due diligence.

On March 19, 2014, the Special Committee held a meeting, in which members of SWS senior management and representatives of the Special Committee's financial and legal advisors participated, to discuss the status of Sandler O'Neill's and Davis Polk's communications with various interested parties. During the meeting, representatives of Davis Polk discussed the Credit Agreement and whether Hilltop and Oak Hill would waive the Merger Covenant, as well as exploring possible transaction structures that could possibly address the Merger Covenant without the need for a waiver from Hilltop. Although the Special Committee concluded that there might be possible ways to address the Merger Covenant in connection with a transaction involving a party other than Hilltop, it was recognized that these approaches entailed litigation risk and therefore that any such structures would involve closing risk. With respect to Hilltop's offer, the Special Committee discussed their concern that Hilltop might withdraw its offer if SWS delayed reaching a definitive agreement with Hilltop in order to continue discussions with other interested parties. With respect to Esposito Global/Party B's offer, the Special Committee discussed the timing and other risks associated with Esposito Global/Party B's need to arrange financing. With respect to the proposal from Party A, representatives of Sandler O'Neill reported that they had received a call from the Chief Executive Officer of Party A, reporting that Party A valued the Company at approximately $8.00 per share and that Party A had discussed with Hilltop's financial advisors the Credit Agreement and was aware of the Merger Covenant. The Special Committee discussed that Party A's $8.00 figure represented a lower price than they understood had previously been indicated by Party A and this led to questions regarding the level of commitment of Party A to pursuing a transaction. The Special Committee also discussed its desire to maximize the value of any offer to SWS's stockholders, the appropriate valuation of SWS, the stockholder vote required to approve of any acquisition of SWS and the range of prices that the Special Committee would consider recommending to the SWS Board as being advisable and fair to and in the best interests of the stockholders of SWS. Following discussion, the Special Committee directed Sandler O'Neill to contact Hilltop to request that Hilltop increase its offer to $8.00 per share and to inform Hilltop that the Special Committee was discussing transaction structures that could address the Merger Covenant without the need for a waiver from Hilltop.

On March 20, 2014, representatives of Sandler O'Neill and Hilltop discussed Hilltop's offer. Representatives of Sandler O'Neill requested that Hilltop increase its offer to $8.00 per share and also noted that the Special Committee had discussed potential transaction structures that could address the Merger Covenant without the need for a waiver from Hilltop. Hilltop reacted unfavorably to Sandler O'Neill's statements and indicated that SWS would need to move quickly if it wished to accept Hilltop's offer.

Later on March 20, 2014, the Special Committee held a meeting, in which members of SWS senior management and representatives of the Special Committee's financial and legal advisors participated, to discuss Sandler O'Neill's discussion with Hilltop earlier that day. The Special Committee discussed the risks that Esposito Global/Party B would not be able to secure the outside financing they required, whether Esposito Global/Party B would be able to confirm the $8.00 price and, even assuming they could raise the financing and confirm the price, the estimated amount of time it would take to do so. The Special Committee also discussed the risk that further delays in reaching an agreement with Hilltop in order to continue discussions with other interested parties might cause Hilltop to withdraw its offer, and whether if Hilltop were to withdraw its offer, there would be any other bona fide offers to acquire SWS and, if there would be, at what price. After considering the risk of Hilltop withdrawing its offer and the lack of any other firm offers, the Special Committee concluded that it would consider an offer from Hilltop of $7.75 per share as being advisable and fair to and in the best interests of the stockholders of SWS and directed Sandler O'Neill to call Hilltop and push for a further increase of Hilltop's offer to $7.75 per share. Representatives of Sandler O'Neill left the meeting and called Hilltop, and Hilltop agreed to increase its offer to $7.75 per share, composed of 25% cash and 75% Hilltop common stock. Hilltop told Sandler O'Neill that Hilltop wanted to move as quickly as possible to definitive documentation and asked the Special Committee to cease discussions with any other interested parties. Representatives of Sandler O'Neill then rejoined the Special Committee meeting and conveyed Hilltop's revised offer. The Special Committee determined that it was in the best interests of SWS's stockholders to move forward with the negotiations with Hilltop on the basis of Hilltop's offer of $7.75 per share.

Later on March 20, 2014, as directed by the Special Committee, representatives of Sandler O'Neill called representatives of Party B to inform them that the Special Committee was uncomfortable with the uncertainty surrounding their extended timeline to secure financing, complete due diligence and affirm their price.

Between March 20, 2014 and March 24, 2014, representatives of Sandler O'Neill and Party A had a number of communications regarding Party A's interest in acquiring SWS and the status of the non-disclosure agreement between SWS and Party A. Party A's representatives reiterated to Sandler O'Neill's representatives that Party A was interested in a transaction and stated that, depending on the outcome of its due diligence, the price could be above $8.00. Party A's representative stated, however, that Party A might now be unwilling to sign a non-disclosure agreement containing a "standstill" provision, a provision that had been agreed earlier in the negotiations relating to the terms of the non-disclosure agreement. The Special Committee remained concerned about the potential loss of employees to, and sharing confidential information with, a competitor like Party A, and the possibility that Party A might simply be attempting to disrupt a sale to Hilltop. The Special Committee concluded, however, that if Party A would sign the previously negotiated version of the non-disclosure agreement, it would move forward with Party A on a parallel track with Hilltop.

On March 24, 2014, representatives of the Special Committee and Sandler O'Neill informed Hilltop that another party was seeking to participate in the process at a price higher than Hilltop's offer of $7.75 per share and that the Special Committee was intending to sign a non-disclosure agreement with the interested party. Hilltop's representatives reiterated Hilltop's intention not to waive the Merger Covenant with respect to any deal with another party. Furthermore, Hilltop's representatives stated that if a definitive agreement was not reached by March 31, 2014, Hilltop would withdraw its offer and Mr. Ford would resign from the SWS Board.

Later on March 24, 2014, the Special Committee held a meeting, in which members of SWS senior management and representatives of the Special Committee's financial and legal advisors participated, to discuss the conversation with Hilltop earlier in the day and how to proceed with Party A. The Special Committee discussed Hilltop's stated intention to withdraw its offer if a definitive agreement were not reached by March 31, 2014 and concluded that the risk and potential negative consequences for the stockholders of this potential outcome were significant. The Special Committee also directed Sandler O'Neill to inform Party A that if it wished to proceed with a transaction, it must sign the previously agreed non-disclosure agreement and it would need to be able to provide a firm offer within a few days.

On March 25, 2014, Wachtell Lipton sent Davis Polk a proposed draft merger agreement, which contemplated, among other things, that SWS would be required to submit the merger agreement to a vote of SWS's stockholders even if the SWS Board changed its recommendation with respect to the merger and would not have a standalone termination right in the event it wished to enter into an agreement with a third party with respect to a "superior proposal" (a so-called "force the vote" provision), and a termination fee of an unspecified amount payable by SWS in certain circumstances.

On March 25, 2014, representatives of Sandler O'Neill and Party A had a call regarding the status of the non-disclosure agreement between SWS and Party A and Party A's interest in acquiring SWS. Party A agreed to sign a non-disclosure agreement on the previously agreed terms and representatives of Sandler O'Neill reiterated to Party A that SWS wished to move very quickly and if Party A wished to proceed with a transaction, they would need to be able to provide a firm offer within a few days.

Later on March 25, 2014, SWS and Party A executed a non-disclosure agreement. As previously negotiated, the non-disclosure agreement contained a "standstill" provision limiting Party A's ability to acquire SWS stock or offer to acquire SWS for a period of time, subject to a "fallaway" provision that would permit Party A to make such an offer in the event that SWS executed a definitive transaction agreement with a party other than Party A.

On March 26, 2014, the Special Committee held a meeting, in which members of SWS senior management and representatives of the Special Committee's financial and legal advisors participated, to discuss the proposed merger agreement received from Wachtell Lipton on March 25, 2014. Representatives of Davis Polk and Sandler O'Neill discussed the proposed merger agreement with the Special Committee and focused particularly on the proposed "force the vote" provision. The Special Committee also considered the range of possible structures for determining the exchange ratio for the share element of the consideration and concluded that while the "fixed exchange ratio" proposed by Hilltop presented some risk if there were a decline in Hilltop's share price prior to closing, the fixed exchange ratio was preferable because it would allow SWS stockholders to benefit from the upside of any increase in the Hilltop share price that might occur as a result of the announcement of a transaction. The Special Committee discussed these provisions, and others, with representatives of Davis Polk and Sandler O'Neill, and requested that Davis Polk discuss the key issues with Wachtell Lipton. The Special Committee also requested that Davis Polk explore with Wachtell Lipton the possibility of requiring the transaction to be approved by a majority of SWS's disinterested stockholders (a so-called "majority of the minority" vote).

Between March 26, 2014 and March 31, 2014, representatives of SWS and Hilltop, together with representatives of Hilltop's legal and financial advisors and the Special Committee's legal and financial advisors, held a series of conference calls to negotiate the terms of the merger agreement and exchanged multiple drafts of the merger agreement.

On March 27, 2014, the SWS Board held a meeting, at which Mr. Ford was not present and in which members of SWS senior management and representatives of the Special Committee's financial and legal advisors participated, to discuss the status of Sandler O'Neill's and Davis Polk's communications with Hilltop, Party A and Esposito Global/Party B. Representatives of Davis Polk

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reviewed with the SWS Board the fiduciary duties of the SWS Board members applicable to their consideration of Hilltop's offer and strategic alternatives. The representatives of Sandler O'Neill reviewed with the SWS Board Sandler O'Neill's financial analysis of SWS, Hilltop and the proposed transaction with Hilltop, including discussing the various financial methodologies used in its analyses. The representatives of Sandler O'Neill also reviewed with the SWS Board the outcome of the confidential market check the Special Committee had previously requested Sandler O'Neill to perform, noting that Sandler O'Neill had been in contact with seventeen parties, including Hilltop, and that at this time only Hilltop, Party A and Esposito Global/Party B remained interested in an acquisition of SWS in its entirety. Representatives of Davis Polk and Sandler O'Neill discussed the proposed merger agreement with the SWS Board and focused particularly on the proposed "force the vote" provision.

Later on March 27, 2014, on a call between representatives of Sandler O'Neill and representatives of Party A, Party A's representatives provided a non-binding indication of interest to acquire SWS for $8.65 per share, subject to its satisfactory completion of due diligence.

Later on March 27, 2014, representatives of Davis Polk had a conversation with Wachtell Lipton, during which they discussed, among other things, the inclusion of a "force the vote" provision, the possible inclusion of a "majority of the minority" vote condition, the circumstances under which each party might terminate the merger agreement and the size and form of the termination fee. The representatives of Wachtell Lipton stated that, among other things, Hilltop would not be prepared to sign a merger agreement that did not contain a "force the vote" provision and further, that Hilltop was not prepared to accept a "majority of the minority" vote requirement.

Later on March 27, 2014, the Special Committee held a meeting, in which members of SWS senior management and representatives of the Special Committee's financial and legal advisors participated, to further discuss the proposed merger agreement received from Wachtell Lipton and to discuss Party A's non-binding indication of interest. The representatives of Davis Polk reviewed with the Special Committee their call earlier in the day with Wachtell Lipton. Representatives of Davis Polk and Sandler O'Neill continued their previous discussions with the Special Committee of the proposed merger agreement from Hilltop and focused particularly on the proposed "force the vote" provision and the possibility of including a two-tier termination fee that would provide for a lower payment in the event that the termination fee became payable because SWS executed an agreement with Party A. The Special Committee directed Sandler O'Neill to contact Party A and request that it describe the process, including due diligence and negotiation of a merger agreement, that Party A would require for it to be in a position to sign a definitive agreement on March 31, 2014. Subsequently, in a letter dated March 27, 2014, Party A confirmed its non-binding proposal to acquire SWS for $8.65 per share, subject to completing due diligence, and described the process that it would require to meet a March 31, 2014 deadline.

On March 28, 2014, representatives of Sandler O'Neill and Party A had a call during which Party A stated that it would work to be, and believed it could be, in a position to execute a definitive agreement with SWS by March 31, 2014, but requested that the Special Committee extend the March 31, 2014 deadline. In addition, Party A informed SWS that it would like to have employee retention agreements in place before any definitive agreement is executed.

On March 28, 2014, representatives of Sandler O'Neill had a call with representatives of Hilltop. During that conversation, Hilltop expressed concern regarding the Special Committee's willingness to meet the March 31, 2014 deadline, which Hilltop's representatives reiterated was critical to it, and would not be extended.

Following the call from Party A, on March 28, 2014, the Special Committee held a meeting, in which members of SWS senior management and representatives of the Special Committee's financial and legal advisors participated, to discuss Party A's request for additional diligence materials and employee retention agreements. The Special Committee discussed with their financial and legal advisors the risks presented if Party A sought to enter into employee retention agreements prior to the execution of a definitive agreement as well as the risk of allowing execution of employee retention agreements to be a condition to the closing of any transaction. Representatives of Sandler O'Neill reviewed with the Special Committee a call they received earlier in the day from representatives of Hilltop. The Special Committee discussed whether Hilltop would be willing to extend its March 31, 2014 deadline. The Special Committee directed Sandler O'Neill to call the representatives of Hilltop to discuss the amount of the termination fee (which Hilltop proposed to be $12 million) and to request that Hilltop agree to extend its March 31, 2014 deadline. The Special Committee also directed Sandler O'Neill to inform Party A that SWS would not be willing to engage in discussions regarding employee retention agreements prior to executing a definitive agreement. Finally, the Special Committee directed the representatives of Davis Polk to send a proposed draft merger agreement to counsel to Party A. Davis Polk sent a draft merger agreement to counsel to Party A on March 29, 2014.

Later on March 28, 2014, the Special Committee received a letter from Party A requesting additional time, beyond the March 31, 2014 deadline, to complete its due diligence and negotiate a merger agreement.

On March 29, 2014, Davis Polk had a call with Oak Hill's outside counsel. In this call, Oak Hill's outside counsel conveyed that Oak Hill would be willing, in connection with a transaction, to waive the Merger Covenant and consent to the exchange of Oak Hill's loans under the Credit Agreement and the Warrants for the equivalent consideration paid in any merger and an amount equal to the Applicable Premium (as defined in the Credit Agreement) payable upon prepayment of its loans, and Oak Hill's counsel also indicated that Oak Hill would be willing to sign a letter waiving the Merger Covenant on those terms, to the extent its consent was needed, with respect to any merger transaction the Special Committee approved (the "Oak Hill Letter Agreement").

Later on March 29, 2014, the Special Committee held a meeting, in which members of SWS senior management and representatives of the Special Committee's financial and legal advisors participated, to discuss the status of Sandler O'Neill's and Davis Polk's communications with advisors for and representatives of Hilltop and Party A and how to proceed with each party. Representatives of Sandler O'Neill reviewed with the Special Committee Party A's request for additional due diligence materials, including data on SWS's revenue-generating employees and interviews with SWS management as well as Party A's continued interest in executing employee retention agreements prior to executing a definitive agreement. During the meeting, representatives of Davis Polk discussed the Credit Agreement and the Merger Covenant, discussed possible transaction structures that could address the Merger Covenant without the need for a waiver from Hilltop and discussed the attendant execution and litigation risk involved with such transaction structures. The representatives of Davis Polk also discussed with the Special Committee their recent call with Oak Hill's outside counsel regarding the treatment of Oak Hill's loan and Warrants in the transaction. It was noted that what Oak Hill's counsel was requesting with its proposed structure was essentially to collapse two steps (i.e. first, Oak Hill receives prepayment of its loan for an amount equal to the principal plus an amount equal to the Applicable Premium (as defined in the Credit Agreement) and, second, Oak Hill uses the principal repayment amount to exercise the Warrants and receive the merger consideration) into one step that would obviate the need for SWS to repay the principal amount and then immediately receive it back, but that this structure would otherwise result in the same economic outcome as prepayment of the loans (including the payment of the Applicable Premium as required by the Credit Agreement) followed by exercise of the Warrants. Representatives of Davis Polk and Sandler O'Neill continued their previous discussions with the Special Committee of the proposed merger agreement from Hilltop and focused on, among other things, the proposed "force the vote" provision.

Between March 29 and March 31, 2014, representatives of Party A conducted in-person due diligence at SWS' Dallas offices.

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On March 30, 2014, Mr. Miller, on behalf of the Special Committee, and the Chief Executive Officer of Party A met to discuss Party A's interest in acquiring SWS. Mr. Miller asked the Chief Executive Officer of Party A whether Party A would be willing to agree to a transaction that day at $9.00 per share, a price that was discussed as sufficient to avoid the need for Hilltop to waive the Merger Covenant. Party A's Chief Executive Officer declined to agree to a transaction at $9.00 per share. Furthermore, the Chief Executive Officer of Party A indicated that Party A would not agree to a transaction with SWS if Hilltop did not agree to waive the Merger Covenant because Party A was concerned about the risk of litigation in the event Party A executed a definitive agreement with SWS without such waiver. In addition, the Chief Executive Officer of Party A stated that Party A needed more time to complete its due diligence review.

On March 30, 2014, the Special Committee held a series of calls, on which members of SWS senior management and representatives of the Special Committee's financial and legal advisors participated, to discuss the status of Sandler O'Neill's and Davis Polk's communications with advisors for and representatives of Hilltop and Party A and how to proceed with each party. Mr. Miller reviewed with the Special Committee the results of his discussion with representatives of Party A, noting that starting on March 29, 2014 Party A had representatives at SWS's Dallas headquarters conducting due diligence. Among other things, the Special Committee discussed Party A's concern over the existence of the Merger Covenant and the Special Committee's concern that Hilltop would withdraw its offer on March 31, 2014 if SWS did not execute a definitive agreement by such date. On the call that evening, the representatives of Davis Polk reviewed a recent call with counsel to Party A to discuss the Credit Agreement, the Merger Covenant, and possible transaction structures to address the Merger Covenant without the need for a waiver from Hilltop.

Later on March 30, the SWS Board held a meeting at which the Special Committee and its financial and legal advisors provided an update on negotiations with Hilltop and with Party A. Representatives of Davis Polk and Sandler O'Neill also discussed in detail with the SWS Board the status of negotiations with Hilltop on the draft merger agreement, and feedback from Sandler O'Neill's call with Hilltop, noting that the outstanding issues included Hilltop's refusal to eliminate the "force the vote" provision and Hilltop's refusal to accept a possible two-tier termination fee that would provide for a lower payment in the event that the fee became payable because SWS executed an agreement with Party A.

On March 31, 2014, the Special Committee received a letter from Party A confirming that Party A would not be able to execute a definitive agreement with SWS that day because Party A was concerned about the need for Hilltop to waive the Merger Covenant and the risk of litigation in the event that Party A executed a definitive agreement with SWS without such a waiver. In its letter, Party A noted that it valued certainty. The letter noted that Party A would normally expect the support of large shareholders, such as Hilltop and Oak Hill (assuming they exercised their Warrants), before entering into any transaction to acquire the company. In addition, Party A's letter stated that Party A needed "a couple more days" to complete its due diligence review.

Based on this letter, and prior conversations with Party A, the Special Committee concluded that there was no possibility that Party A would be able to enter into a definitive agreement by March 31, 2014. In addition, the Special Committee believed that Party A would not enter into a definitive agreement to acquire SWS without an explicit waiver by Hilltop of the Merger Covenant, which Hilltop had indicated repeatedly that it would refuse to grant. The Special Committee also believed that it was highly likely that Hilltop would withdraw its offer if not accepted by the March 31, 2014 deadline and if Hilltop withdrew its offer and disclosed such withdrawal, the stock price of SWS might decline significantly. In that event, the Special Committee was concerned that with a lower stock price, and no competitive dynamic, there was a significant risk that even if Party A were to complete due diligence satisfactorily and be willing to proceed without a waiver by Hilltop of the Merger Covenant, it would lower any price it was prepared to pay in a transaction.

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Later on March 31, 2014, the SWS Board held a meeting, at which Mr. Ford was not present. Representatives of Sandler O'Neill and Davis Polk were present and reviewed the letter from and communications with Party A, and in particular Party A's concerns about the Merger Covenant, the lack of support of Hilltop for Party A's proposed transaction and Party A's concerns about the consequent litigation risk of proceedings without such support. Mr. Miller then updated the SWS Board on the status of discussions with Hilltop. Mr. Miller reported that he intended to continue pressing Hilltop to remove the "force the vote" provision and to agree to a two-tier termination fee. Representatives of Sandler O'Neill then reviewed their financial analysis and indicated that Sandler O'Neill would be prepared to deliver an opinion that the consideration to be paid by Hilltop for each share of the Company's common stock would be fair to the holders of SWS common stock (other than Hilltop) from a financial point of view. As part of this discussion, Sandler O'Neill expressed its view that it had identified and contacted all of the parties that it expected would be interested in an acquisition of SWS based on its professional judgment. The SWS Board then discussed the risks associated with continuing SWS's business on a standalone basis and the impact on its ability to sell SWS to Party A or anyone else, and the pricing of such a potential transaction, if Hilltop withdrew its offer. The SWS Board noted, among other things, that SWS was not generating earnings, that it was subscale in all of its principal business lines and that it continually failed to meet budgets, which led to concerns as to the ability to achieve targets in the future.

Following the SWS Board meeting, Messrs. Miller and Williams met with Hilltop to request the elimination of the "force the vote" provision in Hilltop's proposed merger agreement and to request a two-tier termination fee. The representatives of Hilltop reiterated to Messrs. Miller and Williams that Hilltop would not execute a merger agreement that did not contain a "force the vote" provision and that Hilltop viewed the "force the vote" provision as integral to its offer. Hilltop's representatives also did not agree to a two-tier termination fee but did agree, however, to a reduction in the termination fee to $8 million (a $4 million reduction compared to the original Hilltop proposal of $12 million).

Later on March 31, 2014, the Special Committee held a meeting, in which members of SWS senior management and representatives of the Special Committee's financial and legal advisors participated. Messrs. Miller and Williams reported to the Special Committee the results of their meeting with Hilltop. A representative of Sandler O'Neill reviewed with the Special Committee his call with Hilltop's representatives earlier in the day to request an extension of the March 31, 2014 deadline and for Hilltop to agree to meeting with a potential buyer (Party A), as had been requested by Party A, to discuss a possible waiver of the Merger Covenant. Hilltop had rejected both requests. The Special Committee discussed the results of these conversations. Representatives of Davis Polk reviewed with the Special Committee the fiduciary duties of the Special Committee members applicable to their consideration of Hilltop's offer and then summarized the material terms of Hilltop's then current proposed form of merger agreement, including, among others, a description of the consideration to be paid, the representations, warranties, and covenants, the provisions relating to exclusivity, "no-shop" and changing the SWS Board recommendation, the "force the vote" provision, the events of termination and the termination fee. At the request of the Special Committee, representatives of Sandler O'Neill reviewed with the Special Committee Sandler O'Neill's financial analysis of the merger consideration and delivered to the Special Committee its oral opinion, which was subsequently confirmed in writing, that, based upon and subject to the assumptions, limitations, qualifications and conditions set forth in its written opinion, as of the date of the meeting the merger consideration to be paid by Hilltop for each share of SWS's common stock was fair to the holders of SWS common stock other than Hilltop from a financial point of view. The members of the Special Committee deliberated, considering, among other factors, the certainty of Hilltop's offer as compared to the indications of interest from Esposito Global/Party B and Party A, its view as to the high likelihood that Hilltop would withdraw its offer if not accepted by its March 31 deadline and the potential detrimental impact to SWS and its stockholders if that were to happen and the fact that Sandler O'Neill had conducted a comprehensive market check. Following the deliberations, the Special Committee unanimously adopted resolutions recommending that the SWS Board adopt and approve the proposed merger agreement and proposed transaction with Hilltop. The Special Committee then requested that Mr. Miller present the Special Committee's determination and recommendation to accept Hilltop's offer to the SWS Board at its meeting later that day.

At the SWS Board meeting later that day, Mr. Miller presented the Special Committee's recommendation to accept Hilltop's offer, substantially on the terms set forth in the proposed merger agreement and related documents. The members of the Special Committee, together with the Special Committee's financial and legal advisors, reviewed with the SWS Board the status of negotiations with Hilltop, Party A and Esposito Global/Party B, and provided updates regarding their recent communications with each such interested party. Representatives of Davis Polk reviewed with the SWS Board the fiduciary duties of the SWS Board members applicable to their consideration of Hilltop's offer and then summarized the material terms of Hilltop's proposed form of merger agreement, including a description of the consideration to be paid, the representations, warranties, and covenants, the provisions relating to exclusivity, "no-shop" and changing the SWS Board recommendation, the "force the vote" provision, the events of termination and the termination fee. At the request of the Special Committee, representatives of Sandler O'Neill reviewed with the SWS Board Sandler O'Neill's financial analysis of the merger consideration and shared with the SWS Board its oral opinion that had been given to the Special Committee, which was subsequently confirmed in writing, that, based upon and subject to the assumptions, limitations, qualifications and conditions set forth in its written opinion, as of the date of the meeting the merger consideration to be paid by Hilltop for each share of SWS's common stock was fair to the holders of SWS common stock other than Hilltop from a financial point of view. The members of the SWS Board discussed, among other things, the concern that, in the absence of a transaction with Hilltop or any other party, the repayment of the loans outstanding under the Credit Agreement presented serious issues, including that it may raise a going concern issue for the next fiscal year's audit. The members of the SWS Board (other than Mr. Ford) then deliberated and considered the Special Committee's recommendation and then, with Mr. Crandall, the director appointed by Oak Hill, recusing himself due to a potential conflict of interest based on his firm's ownership of securities other than common stock and being a party to the Oak Hill Letter Agreement, by unanimous vote of those directors that voted (i) determined that the merger agreement and the transactions contemplated thereby, including the Oak Hill Letter Agreement, were advisable and fair to and in the best interests of the stockholders of SWS, (ii) approved and adopted the merger agreement and approved the merger and the other transactions contemplated thereby and (iii) recommended the approval and adoption of the merger agreement and the transactions contemplated thereby by SWS's stockholders.

Subsequently, the merger agreement and Oak Hill Letter Agreement were executed and delivered and the transaction was announced on the morning of April 1, 2014 in a press release issued jointly by SWS and Hilltop.

SWS's Reasons for the Merger

The SWS Board and the Special Committee believe that the merger agreement and the transactions contemplated thereby, including the merger, are advisable and fair to and in the best interests of the SWS stockholders (other than Hilltop). Accordingly, the SWS Board (other than Mr. Ford and Mr. Crandall, who were recused from the voting), acting upon the unanimous recommendation of the Special Committee, has approved the merger agreement and the transactions contemplated thereby, and recommends that SWS stockholders vote "FOR" adoption of the merger agreement and the transactions contemplated thereby, including the merger.

As described above under "Background of the Merger," the SWS Board, prior to and in reaching its decision at its meeting on March 31, 2014 to approve the merger agreement and the transactions contemplated thereby, consulted with SWS's management, the Special Committee and financial and

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legal advisors and considered a variety of potentially positive factors relating to the merger, including, but not limited to, the following:

- its knowledge of SWS's business, operations, financial condition, asset quality, earnings and prospects, and of Hilltop's business, operations, financial condition, asset quality, earnings and prospects, taking into account input from SWS senior management and information provided by SWS's financial advisor;

- its knowledge of the current environment in the financial services industry, including national, regional and local economic conditions and the interest rate environment, continued consolidation, the uncertainties in the regulatory climate for financial institutions, increased operating costs resulting from regulatory initiatives and compliance mandates, increasing competition, the current environment for community banks and broker-dealers, and current financial market conditions and the likely effects of these factors on SWS's potential growth, development, productivity and strategic options, and the historical market prices of SWS common stock;

- the financial terms of the merger, including the fact that, based on the closing price on the New York Stock Exchange of Hilltop common stock on March 31, 2014 (the trading day on which the SWS Board approved the merger), the per-share merger consideration as of such date represented an approximate premium of:

  - 27.9% over the closing price of SWS shares on the New York Stock Exchange as of January 8, 2014 (the last trading day prior to SWS's receipt of Hilltop's acquisition proposal);

  - 4.0% over the closing price of SWS shares on the New York Stock Exchange as of March 31, 2014;

- the SWS Board's belief that the merger consideration exceeds SWS's likely value as a standalone company, including its potential for future growth, and exceeds the likely value that would be realized if SWS sold its banking operations and operated its other lines of business on a standalone basis or broke itself up through separate sales of its business lines, which belief was based on a number of factors, including:

  - the risks and uncertainties associated with SWS's potential performance as a standalone company;

  - the SWS Board's analysis of other strategic alternatives available to SWS;

  - the analyses provided by Sandler O'Neill.

- the benefits that SWS and its advisors were able to obtain as a result of extensive negotiations with Hilltop, including a significant increase in Hilltop's bid from the beginning of the process to the end of the negotiations, a reduction in the termination fee and an increase in the percentage of merger consideration represented by Hilltop common stock;

- the complementary aspects of SWS's and Hilltop's businesses, including customer focus, geographic coverage, business orientation and compatibility of the companies' cultures and management and operating styles, and the potential expense-saving and revenue-enhancing opportunities in connection with the merger and the related potential impact on the combined company's earnings;

- that Hilltop had the substantial resources needed to finance a transaction at this value and to make the potential merger successful;

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the fact that the merger consideration consists substantially of Hilltop common stock, which would allow SWS stockholders to benefit from the upside of the future performance of the combined company generally;

Hilltop's successful track record, including, among other things, with respect to the integration of acquisitions;

the fact that, absent the merger, SWS would have been required to repay $50 million to each of Hilltop and Oak Hill on July 28, 2016 pursuant to the Credit Agreement and to raise the financing to make these payments;

its assessment of the likelihood that the merger would be completed in a timely manner and that the management team of Hilltop would be able to successfully integrate and operate the businesses of the combined company after the merger;

the financial analyses presented by Sandler O'Neill to the SWS Board, and the opinion delivered by Sandler O'Neill to the effect that, as of the date of the opinion, and subject to and based on the qualifications and assumptions set forth in the opinion, the consideration to be received by the holders of common stock of SWS in the merger was fair, from a financial point of view, to such stockholders, other than Hilltop;

in deciding to accept Hilltop's final offer and enter into the merger agreement, the SWS Board also considered:

that Hilltop had advised that its proposal would expire if it were not accepted before March 31, 2014 and that, in such event, Hilltop would terminate its participation in the process and cause Mr. Ford to resign as a director of SWS;

the SWS Board's belief that it would have the strongest leverage to obtain the best terms while two interested parties were bidding against each other, before one of the parties terminated its participation in the process;

that, based on the deadline imposed by Hilltop, SWS had negotiated vigorously with Party A prior to the deadline, and had made available to Party A all due diligence materials made available to Hilltop, as well as additional materials requested by Party A, and had advised Party A of the deadline imposed by Hilltop;

that Party A had not submitted a binding proposal for the acquisition of SWS prior to the deadline;

that Party A had indicated that it was not prepared to enter into a definitive agreement without an agreement with Hilltop with respect to a negotiated resolution of the Merger Covenant under the Credit Agreement, and that Hilltop had indicated that it would not waive the Merger Covenant;

that, if Hilltop withdrew its offer after its deadline of March 31, 2014, the SWS Board believed there to be significant risk that no alternative acquisition proposal would come from Party A or anyone else and that, even if an acquisition proposal ensued, a subsequent offer (by Party A or anyone else), if any, would likely be lower than the merger consideration;

that the standstill provisions in the confidentiality agreement between SWS and Party A would fall away on SWS entering into the merger agreement with Hilltop and therefore Party A would not be precluded from making an offer to acquire SWS on terms superior to those in the merger agreement;

the SWS Board's belief that the merger consideration represented Hilltop's best and final offer;

- the SWS Board's belief that all potential parties reasonably likely to have an interest in and the financial and regulatory capability to complete a strategic transaction with SWS had been contacted and that it was unlikely that any other party would be willing to acquire SWS at a price in excess of the merger consideration, even if SWS were to continue to solicit alternative acquisition proposals (and risk causing Hilltop to withdraw its offer);
- the greater market capitalization and anticipated trading liquidity of Hilltop common stock after the transaction in the event SWS stockholders desired to sell the shares of Hilltop common stock to be received by them upon completion of the merger;
- the expectation that the merger of SWS with and into Peruna, with Peruna continuing as the surviving entity, would qualify as a "reorganization" for United States federal income tax purposes;
- the regulatory and other approvals required in connection with the merger and the likelihood that the approvals needed to complete the merger would be obtained without unacceptable conditions;
- the fact that the Special Committee unanimously recommended that the SWS Board approve the merger agreement and the merger;
- the fact that SWS stockholders who do not vote to adopt the merger agreement and who follow certain prescribed procedures are entitled to appraisal rights under applicable law;
- the terms of the merger agreement; and
- the terms of the Oak Hill Letter Agreement, including that Oak Hill consented to the merger agreement and will receive only the consideration it would be entitled to receive if its loans were prepaid in full in accordance with the Credit Agreement and Oak Hill's Warrants were then exercised in full, and that Oak Hill agreed not to enter into a voting agreement with Hilltop (which, if Oak Hill were to exercise its Warrants and hold common stock of SWS, would ensure that it would be permitted to vote against the merger agreement if, for example, the SWS Board changed its recommendation in light of a superior offer from a third party). The Special Committee and the Board also noted that the Oak Hill Letter Agreement expressly contemplated that Oak Hill could provide a similar consent for any other merger transaction that the Special Committee might recommend.

In the course of its deliberations, the SWS Board, in consultation with SWS management, the Special Committee and legal and financial advisors, also considered a variety of risks and other potentially negative factors relating to the merger, including the following:

- the risks associated with the operations of the combined company including the challenges both of integrating SWS's businesses, operations and employees with those of Hilltop and of achieving the anticipated cost savings;
- the potential risk of diverting management focus and resources from other strategic opportunities and from operational matters while working to implement the merger;
- the deal protection measures in the merger agreement, including the "force the vote" provision, the termination fee, the non-solicitation provision and the potential impact of such measures on the willingness of other potential acquirers to propose alternative transactions, although the SWS Board believed that the market check undertaken by SWS with the assistance of Sandler O'Neill was a thorough process, that the termination fee was reasonable and customary and that neither the "force the vote" provision, the termination fee, the non-solicitation provision nor any other deal protection measures in

the merger agreement would preclude a serious and financially capable potential acquirer from making a superior proposal to acquire SWS following the announcement of the merger in which case the SWS Board could withdraw its recommendation and explain its reasons for doing so;

the fact that Esposito Global made a non-binding proposal to acquire SWS at a price $0.12 higher than the merger consideration (valued as of the date of the merger agreement) although, as discussed above, the SWS Board believed that there were significant risks that Esposito Global/Party B's proposal would not lead to a definitive agreement, including because an acquisition by Esposito Global would be subject to significant financing risk, and would take longer to consummate than the merger with Hilltop, and further the SWS Board considered the form of merger consideration offered by Hilltop (75% of which was Hilltop common stock) more attractive than the proposed consideration (consisting solely of cash) included by Esposito Global/Party B as part of its non-binding proposal;

the fact that Party A made a non-binding proposal to acquire SWS at a price $0.77 higher than the merger consideration (valued as of the date of the merger agreement) although, as discussed above, the SWS Board believed Party A's proposal was unlikely to lead to a definitive agreement, and further the SWS Board considered the form of merger consideration offered by Hilltop (75% of which was Hilltop common stock) more attractive than the proposed consideration (consisting of cash and Party A common stock) included by Party A as part of its non-binding proposal;

the fact that accepting Hilltop's offer in compliance with the deadline imposed by Hilltop required SWS to terminate discussions with Party A, although for the reasons described above, setting forth the SWS Board's considerations in deciding to accept Hilltop's final offer, the SWS Board considered it unlikely that Party A's proposal would result in a definitive agreement and believed it to be in the best interests of SWS's stockholders to terminate discussion with Party A in order to accept the Hilltop offer in advance of Hilltop's deadline;

the potential negative effect of the pendency of the merger on SWS's business and relationships with customers, vendors, business partners and employees, including the risk that key employees might not choose to remain employed with SWS prior to the completion of the merger, regardless of whether or not the merger is completed;

the fact that, because the merger agreement does not provide SWS with a price-based termination right or other similar protection for SWS or its stockholders, such as a "collar" with respect to Hilltop's stock price, the market value of the merger consideration may vary from the closing price of Hilltop common stock on the date the merger was announced, and any such change will affect the market value of the merger consideration that SWS stockholders will receive upon completion of the merger;

the fact that the receipt of the cash portion of the merger consideration will be taxable to SWS's stockholders for U.S. federal income tax purposes; and

the fact that some of the directors and executive officers of SWS have interests in the merger and have arrangements that are different from or in addition to those of SWS stockholders generally, as described in the section entitled "The Merger Interests of SWS Directors and Executive Officers in the Merger" included elsewhere in this proxy statement/prospectus.

The foregoing discussion of the factors considered by the SWS Board is not intended to be exhaustive, but rather a summary of the material factors considered by the SWS Board. In reaching its decision to approve and adopt the merger agreement, including the merger and the other transactions contemplated by the merger agreement, the SWS Board did not quantify or assign any relative weights to the factors considered, and individual directors may have given different weights to different factors. The SWS Board considered the various factors as a whole, including discussions with, and questioning of, SWS management and SWS's financial and legal advisors, and overall considered the factors to be favorable to, and to support, its determination.

The foregoing discussion of the information and factors considered by the SWS Board is forward-looking in nature. This information should be read in light of the factors described under the section entitled "Forward-Looking Statements" included elsewhere in this proxy statement/prospectus.

Hilltop's Reasons for the Merger

In reaching its decision to adopt and approve the merger agreement, the merger and the other transactions contemplated by the merger agreement, the Hilltop board of directors consulted with Hilltop management, as well as its financial and legal advisors, and considered a number of factors, including the following material factors:

- each of Hilltop's and SWS's business, operations, financial condition, asset quality, earnings and prospects. In reviewing these factors, the Hilltop board of directors considered its view that SWS's business and operations complement those of Hilltop and that the merger would result in a combined company with a diversified revenue stream, a well-balanced portfolio and an attractive funding base;

- its understanding of the current and prospective environment in which Hilltop and SWS operate, including national and local economic conditions, the competitive environment for financial institutions generally, and the likely effect of these factors on Hilltop both with and without the proposed transaction;

- its existing knowledge of SWS's business and its review and discussions with Hilltop's management concerning the additional due diligence examination of SWS conducted in connection with the merger;

- the complementary nature of the cultures of the two companies, which management believes should facilitate integration and implementation of the transaction;

- management's expectation that Hilltop will retain its strong capital position upon completion of the transaction;

- the financial and other terms of the merger agreement, including the fixed exchange ratio, tax treatment and deal protection and termination fee provisions, which it reviewed with its outside financial and legal advisors;

- the potential risks associated with achieving anticipated cost synergies and savings and successfully integrating SWS's business, operations and workforce with those of Hilltop;

- the nature and amount of payments to be received by SWS management in connection with the merger;

- the potential risk of diverting management attention and resources from the operation of Hilltop's business and towards the completion of the merger; and

- the regulatory and other approvals required in connection with the merger and the expectation that such regulatory approvals will be received in a timely manner and without the imposition of unacceptable conditions.

Opinion of Sandler O'Neill & Partners, L.P.

By letter dated February 3, 2014, and amended on March 5, 2014, the Special Committee retained Sandler O'Neill, to act as financial advisor to the Special Committee in connection with a possible business combination transaction. Sandler O'Neill is a nationally recognized investment banking firm whose principal business specialty is financial institutions. In the ordinary course of its investment banking business, Sandler O'Neill is regularly engaged in the valuation of financial institutions and their securities in connection with mergers and acquisitions and other corporate transactions. The Special Committee selected Sandler O'Neill to act as the Special Committee's advisor in connection with a possible business combination based on its qualifications, expertise, reputation and experience in mergers and acquisitions involving financial institutions.

Sandler O'Neill acted as financial advisor to the Special Committee in connection with the proposed transaction and participated in certain of the negotiations leading to the execution of the merger agreement. At the March 31, 2014 meeting of the Special Committee, Sandler O'Neill delivered to the Special Committee its oral opinion, which was subsequently confirmed in writing on March 31, 2014, that, as of March 31, 2014, the merger consideration was fair to the holders of SWS common stock, other than Hilltop, from a financial point of view. **The full text of Sandler O'Neill's opinion is attached as Annex B to this proxy statement/prospectus. The opinion outlines the procedures followed, assumptions made, matters considered and qualifications and limitations on the review undertaken by Sandler O'Neill in rendering its opinion. The description of the opinion set forth below is qualified in its entirety by reference to the full text of the opinion. Holders of SWS common stock are urged to read the entire opinion carefully in connection with their consideration of the proposed merger.**

Sandler O'Neill's opinion speaks only as of the date of the opinion. The opinion was directed to the Special Committee and is directed only to the fairness of the merger consideration to the holders of SWS common stock, other than Hilltop, from a financial point of view. It does not address the underlying business decision of SWS to engage in the merger or any other aspect of the merger and is not a recommendation to any holder of SWS common stock as to how such holder of SWS common stock should vote at the special meeting with respect to the merger or any other matter. Sandler O'Neill did not express any opinion as to the fairness of the amount or nature of the compensation to be received in connection with the merger by SWS's officers, directors, or employees, or any class of such persons, relative to the merger consideration to be received in the merger by any other shareholders of SWS.

In connection with rendering its opinion on March 31, 2014, Sandler O'Neill reviewed and considered, among other things:

- The merger agreement;
- Certain publicly available financial statements and other historical financial information of SWS that Sandler O'Neill deemed relevant;
- Certain publicly available financial statements and other historical financial information of Hilltop that Sandler O'Neill deemed relevant;
- Certain internal financial information and other data relating to the business and financial prospects of SWS that were provided to Sandler O'Neill by the management of SWS and not publicly available, including financial forecasts and estimates prepared by the management of SWS (the "SWS Forecasts");
- Publicly available median analyst earnings estimates for Hilltop for the years ending December 31, 2014 through December 31, 2015, and a consensus long-term earnings growth rate for the years thereafter;
- The pro forma financial impact of the merger on Hilltop, based on assumptions relating to transaction expenses, purchase accounting adjustments and cost savings as discussed with senior management of Hilltop;
- The publicly reported historical price and trading activity for SWS's and Hilltop's common stock, including a comparison of certain financial and stock market information for SWS and Hilltop

and similar publicly available information for certain other companies similar to each of SWS and Hilltop, the securities of which are publicly traded;

The financial terms of certain recent business combinations involving other similar and related party transactions in the financial services industry, to the extent publicly available;

The current market environment generally and the financial services environment in particular; and

Such other information, financial studies, analyses and investigations and financial, economic and market criteria as Sandler O'Neill considered relevant.

Sandler O'Neill also discussed with certain members of the senior management of SWS the business, financial condition, results of operations and prospects of SWS and held similar discussions with the senior management of Hilltop regarding the business, financial condition, results of operations and prospects of Hilltop.

In performing its reviews and analyses and in rendering its opinion, Sandler O'Neill relied upon the accuracy and completeness of all of the financial and other information that was available to Sandler O'Neill from public sources, that was provided to Sandler O'Neill by SWS or Hilltop or their respective representatives or that was otherwise reviewed by Sandler O'Neill, and Sandler O'Neill assumed such accuracy and completeness for purposes of rendering its opinion. Sandler O'Neill relied, at the direction of SWS, without independent verification or investigation, on the assessments of the management of SWS as to SWS's existing and future relationships with key employees and partners, clients, products and services and Sandler O'Neill assumed, with the Special Committee's consent, that there would be no developments with respect to any such matters that would affect its analyses or opinion. Sandler O'Neill further relied on the assurances of the respective senior managements of SWS and Hilltop that they were not aware of any facts or circumstances that would make any of such information inaccurate or misleading. Sandler O'Neill was informed by SWS that certain provisions of a credit agreement to which SWS is a party that may place significant constraints on SWS's ability to sell itself or certain of its assets. With respect to the SWS Forecasts, Sandler O'Neill assumed that they had been reasonably prepared on a basis reflecting the best currently available estimates and judgments of the management of SWS as to the future financial performance of SWS. Sandler O'Neill was not asked to undertake, and did not undertake, an independent verification of any of such information and Sandler O'Neill assumes no responsibility or liability for the accuracy or completeness thereof.

Sandler O'Neill used median publicly available earnings estimates and long-term growth rates for Hilltop in its analyses. The management of Hilltop confirmed to Sandler O'Neill that they reflected the best currently available estimates and judgments of the future financial performance of Hilltop, and Sandler O'Neill assumed that such performance would be achieved. With respect to the projections of transaction expenses, purchase accounting adjustments and cost savings discussed with the senior management of Hilltop, the management of Hilltop confirmed to Sandler O'Neill that they reflected the best currently available estimates and judgments of such management and Sandler O'Neill assumed that such performances would be achieved.

Sandler O'Neill expressed no opinion as to the trading values of the common stock of SWS and Hilltop after the date of the opinion or what the value of Hilltop common stock will be once it is actually received by the holders of SWS common stock. Sandler O'Neill expressed no opinion as to any of the legal, accounting and tax matters relating to the merger and any other transaction contemplated by SWS. Sandler O'Neill's opinion was necessarily based on financial, economic, market and other conditions as in effect on, and the information made available to Sandler O'Neill as of, the date of its opinion. Events occurring after the date thereof could materially affect Sandler O'Neill's opinion. Sandler O'Neill has not undertaken to update, revise, reaffirm or withdraw its opinion or otherwise comment upon events occurring after the date of its opinion.

In rendering its March 31, 2014 opinion, Sandler O'Neill performed a variety of financial analyses. The following is a summary of the material analyses performed by Sandler O'Neill, but it is not a complete description of all the analyses underlying Sandler O'Neill's opinion. The summary includes information presented in tabular format. **In order to fully understand the financial analyses, these tables must be read together with the accompanying text.** The tables alone do not constitute a complete description of the financial analyses. The preparation of a fairness opinion is a complex process involving subjective judgments as to the most appropriate and relevant methods of financial analysis and the application of those methods to the particular circumstances. The process, therefore, is not necessarily susceptible to a partial analysis or summary description. Sandler O'Neill believes that its analyses must be considered as a whole and that selecting portions of the factors and analyses to be considered without considering all factors and analyses, or attempting to ascribe relative weights to some or all such factors and analyses, could create an incomplete view of the evaluation process underlying its opinion. Also, no company included in Sandler O'Neill's comparative analyses described below is identical to SWS or Hilltop and no transaction is identical to the merger. Accordingly, an analysis of comparable companies or transactions involves complex considerations and judgments concerning differences in financial and operating characteristics of the companies and other factors that could affect the public trading values or merger transaction values, as the case may be, of SWS and Hilltop and the companies to which they are being compared.

Transaction Multiples

Sandler O'Neill reviewed the financial terms of the proposed transaction. As described in the merger agreement, SWS shareholders have the right to receive consideration consisting of (i) 0.2496 shares of Hilltop common stock and (ii) an amount in cash equal to $1.94 in exchange for each share of SWS's common stock. Based upon Hilltop's closing price of $23.29 as of March 20, 2014, Sandler O'Neill calculated a merger consideration value of $7.75 per share of SWS common stock. Based upon 40,288,293 common shares outstanding and using Hilltop's closing price of $23.29 as of March 20, 2014, Sandler O'Neill calculated an aggregate merger consideration value of $312.2 million. Based upon financial information as of December 31, 2013, Sandler O'Neill calculated the following transaction ratios:

Transaction Value / Book Value Per Share:	81%
Transaction Value / Tangible Book Value Per Share:	83%
Transaction Value / Tangible Book Value Per Share (all warrants exercised):	95.1%
Transaction Value / Estimated FY 2015 EPS (Street):	86.1x

Comparable Companies Analysis

Sandler O'Neill used publicly available information to compare selected financial information for SWS and a group of financial institutions selected by Sandler O'Neill based on Sandler O'Neill's professional judgment and experience. The peer group consisted of NASDAQ and NYSE traded institutional broker dealers and broker dealers with retail distribution.

The following financial institutions were selected for the comparison:

Institutional Broker Dealers:
Cowen Group, Inc.
FBR & Co.
JMP Group Inc.
Ladenburg Thalmann Financial Services Inc.
Piper Jaffray Companies

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Broker Dealers with Retail Distribution:
Oppenheimer Holdings Inc.
Raymond James Financial, Inc.
RCS Capital Corporation
Stifel Financial Corp.

The analysis compared publicly available financial information for SWS as of December 31, 2013 and the high, mean, median and low financial and market trading data for the peer group as of March 28, 2014. The results of these analyses are summarized in the following table.

	SWS (01/09/14 pricing)	SWS 03/28/14 pricing)	Institutional Broker Dealers and Broker Dealers w/Retail Distribution (03/28/14 pricing)			
			High	Mean	Median	Low
Market Value ($ in millions)	$ 198	$ 246	$ 7,671	$ 1,591	$ 542	$ 150
Trading as % of High	97.1%	89.9%	98.9%	89.4%	90.5%	73.2%
Price Change (Last Twelve Months)	2.5%	23.1%	80.1%	35.9%	34.4%	(0.4)%
Price Change (Year To Date)	(0.0)%	22.5%	99.3%	13.0%	4.4%	(7.2)%
Price / Book Value	63%	78%	202%	118%	97%	72%
Price / Tangible Book Value	65%	80%	240%	147%	119%	89%
Price / Last Twelve Months Earnings Per Share	NM	NM	107%	32.4%	19.6%	3.4%
Price / Estimated 2014 Earnings Per Share	NM	NM	17.0x	15.1x	16.1x	9.8x
Price / Estimated 2015 Earnings Per Share	NM	NM	33.2x	15.8x	14.3x	8.7x
Median Long Term Growth Rate	N/A	N/A	15.0%	13.8%	14.0%	12.5%
Current Dividend Yield	0.00%	0.00%	5.63%	1.35%	1.17%	0.00%
Last Twelve Months Return On Equity	(10.95)%	(10.95)%	32.18%	8.98%	5.90%	1.82%

Sandler O'Neill used publicly available information to compare selected financial information for Hilltop and a group of financial institutions selected by Sandler O'Neill based on Sandler O'Neill's professional judgment and experience. The peer group consisted of NASDAQ and NYSE traded bank holding companies headquartered in the Southwest or Southeast regions and with total assets ranging from $5 to $15 billion as of September 30, 2013.

The following companies were selected for the comparison:

BancFirst Corporation
BancorpSouth, Inc.
BankUnited, Inc.
Capital Bank Financial Corp.
First Citizens Bancorporation, Inc.
First Financial Bankshares, Inc.
First Financial Holdings, Inc.
Home BancShares, Inc.
IBERIABANK Corporation
International Bancshares Corporation
National Bank Holdings Corporation
Pinnacle Financial Partners, Inc.
Renasant Corporation
Texas Capital Bancshares, Inc.
Trustmark Corporation
United Bankshares, Inc.
United Community Banks, Inc.
WesBanco, Inc.

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The analysis compared publicly available financial information for Hilltop as of December 31, 2013 and the high, mean, median and low financial and market trading data for the peer group as of March 28, 2014. The results of these analyses are summarized in the following table.

	Hilltop (01/09/14 pricing)	Company			
		High	Mean	Median	Low
Total Assets ($ in millions)	$ 8,903	$ 15,047	$ 8,697	$ 7,678	$ 4,914
Tangible Common Equity to Tangible Assets	10.19%	16.89%	9.31%	8.48%	6.64%
Leverage Ratio	12.78%	16.63%	10.53%	9.77%	8.32%
Total Risk-Based Capital Ratio	19.10%	39.53%	16.53%	14.22%	10.73%
Return On Average Assets	1.66%	3.86%	1.10%	1.02%	0.13%
Return On Average Equity	10.59%	37.30%	9.58%	8.57%	0.67%
Net Interest Margin	4.47%	5.73%	3.90%	3.76%	2.57%
Efficiency Ratio	79.6%	82.5%	62.0%	62.5%	45.4%
Loan Loss Ratio / Gross Loans	0.61%	1.76%	1.19%	1.21%	0.67%
Non-Performing Assets(2)/Total Assets	0.33%	2.88%	1.32%	1.30%	0.34%
Net Charge Offs / Average Loans	0.10%	0.43%	0.16%	0.15%	(0.09%)
Price / Tangible Book Value	232%	424%	216%	190%	85%
Price/ Last Twelve Months Earnings Per Share	16.1x	33.7x	20.3x	22.1x	4.3x
Price / Estimated 2014 Earnings Per Share	15.8x	22.4x	17.9x	18.3x	13.8x
Price / Estimated 2015 Earnings Per Share	13.7x	26.2x	16.3x	15.4x	13.2x
Current Dividend Yield	0.0%	4.3%	1.6%	1.5%	0.0%
Last Twelve Months Dividend Ratio	0.0%	142.9%	43.6%	37.2%	2.1%
Market Value ($ in millions)	$ 2,034	$ 3,441	$ 1,589	$ 1,553	$ 452
Adjusted Beta	0.81	1.20	0.96	0.96	0.55

(2) Non-Performing Assets include nonaccrual loans and leases, renegotiated loans and leases, and other real estate.

SWS Net Present Value Analysis

Sandler O'Neill performed an analysis that estimated the net present value per share of SWS common stock through December 31, 2017.

Sandler O'Neill based the analysis on SWS's projected earnings stream (as provided in the SWS Forecasts) for the years ending December 31, 2014 through 2017, which projections assumed (i) a reversal of the deferred tax assets valuation allowance on December 31, 2015 and (ii) that the current holders of SWS's outstanding warrants would exercise such warrants in 2016, with the proceeds of such exercise used to repay approximately $100 million of SWS's outstanding debt. SWS's projections are summarized in the section entitled "Certain SWS Prospective Financial Information."

To approximate the terminal value of SWS's common stock at December 31, 2017, Sandler O'Neill applied price to earnings multiples of 10.0x to 15.0x and multiples of tangible book value ranging from 100% to 180% as determined by Sandler O'Neill in its professional judgment and experience. Sandler O'Neill selected the price to earnings multiples based on price to earnings multiples of the SWS peer group. Sandler O'Neill selected the tangible book value multiples based on tangible book value multiples of the SWS peer group. The income streams and terminal values were then discounted to present values using different discount rates ranging from 10.0% to 15.0%, which were assumed deviations, both up and down, as selected by Sandler O'Neill based on the SWS discount rate of 14.49% as determined by Sandler O'Neill. Sandler O'Neill determined the discount rate based on the 10-year treasury bond yield of 2.73%, an equity risk premium of 5.70%, a size premium of 3.81%, and an industry premium of 2.25%. These analyses resulted in the following reference ranges of implied present values per share of SWS common stock:

Range of Implied Present Values Per Share Based on Price / Earnings	Range of Implied Present Values Per Share Based on Tangible Book Value
$3.20 - $5.74	$5.80 - $12.47

Sandler O'Neill also considered and discussed with the Special Committee how this analysis would be affected by changes in the underlying assumptions, including variations with respect to net income. To illustrate this impact, Sandler O'Neill performed a similar analysis assuming SWS's net income varied from 25% above projections to 25% below projections. Using a discount rate of 14.49% for this analysis, Sandler O'Neill noted a range of $2.67 $6.68 per share of SWS common stock.

During the March 31, 2014 meeting of the Special Committee, Sandler O'Neill noted that the net present value analysis is a widely used valuation methodology, but the results of such methodology are highly dependent upon the numerous assumptions that must be made, and the results thereof are not necessarily indicative of actual values or future results.

Hilltop Net Present Value Analysis

Sandler O'Neill also performed an analysis that estimated the net present value per share of Hilltop common stock through December 31, 2017.

Sandler O'Neill based the analysis on Hilltop's projected earnings stream as derived from median consensus publicly available analyst estimates through the year ended December 31, 2015 and a consensus long-term earnings growth rate of 10% for the years ending 2016 and 2017. These projections are summarized in the section entitled "Opinion of Sandler O'Neill & Partners, L.P. Other Information Reviewed By Sandler O'Neill Hilltop's Projected Earnings Stream."

To approximate the terminal value of Hilltop's common stock at December 31, 2017, Sandler O'Neill applied price to earnings multiples of 14.0x to 24.0x and multiples of tangible book value ranging from 175% to 300% as determined by Sandler O'Neill in its professional judgment and experience. Sandler O'Neill selected the price to earnings multiples based on the price to earnings multiples of the Hilltop peer group. Sandler O'Neill selected the tangible book value multiples based on tangible book value multiples of the Hilltop peer group. The income streams and terminal values were then discounted to present values using different discount rates ranging from 9.0% to 15.0%, which were assumed deviations, both up and down, as selected by Sandler O'Neill based on the Hilltop discount rate of 12.75% as determined by Sandler O'Neill. Sandler O'Neill determined the discount rate based on the 10-year treasury bond yield of 2.73%, an equity risk premium of 5.70%, a size premium of 1.12%, and an industry premium of 3.20%. These analyses resulted in the following reference ranges of implied present values per share of Hilltop common stock:

Range of Implied Present Values Per Share Based on Price / Earnings	Range of Implied Present Values Per Share Based on Tangible Book Value
$16.02 - $34.04	$17.07 - $36.27

Sandler O'Neill also considered and discussed with the Special Committee how this analysis would be affected by changes in the underlying assumptions, including variations with respect to net income. To illustrate this impact, Sandler O'Neill performed a similar analysis assuming Hilltop's net income varied from 25% above projections to 25% below projections. Using a discount rate of 12.75% for this analysis, Sandler O'Neill noted a range of $13.36 $38.17 per share of Hilltop common stock.

During the March 31, 2014 meeting of the Special Committee, Sandler O'Neill noted that the net present value analysis is a widely used valuation methodology, but the results of such methodology are highly dependent upon the numerous assumptions that must be made, and the results thereof are not necessarily indicative of actual values or future results.

Analysis of Selected Merger Transactions

Sandler O'Neill reviewed two groups of comparable mergers and acquisitions. The first group consisted of mergers and acquisitions with deal values greater than $75 million that involved institutional, regional, national or multinational broker dealers. The second group consisted of mergers and acquisitions of companies in the financial services industry where the buyer and the target had ownership or other relationships similar to those between SWS and Hilltop.

The first group of mergers and acquisitions included seven transactions announced between August 17, 2011 and January 16, 2014, selected based on Sandler O'Neill's professional judgment and experience. The group was composed of the following transactions:

Buyer / Target

American International Group, Inc. / Woodbury Financial Services, Inc.

Chestnut Venture Holdings, LLC / Genworth Financial Investment Services Inc.

Ladenburg Thalmann Financial Services Inc. / Securities America Financial Corporation

Leucadia National Corporation / Jefferies Group, Inc.

Raymond James Financial, Inc. / Morgan Keegan & Company, Inc. / MK Holding Inc.

RCS Capital Corporation / Cetera Financial Holdings, Inc.

Stifel Financial Corp. / KBW, Inc.

Sandler O'Neill then reviewed the following multiples for each of the transactions: transaction price to last twelve months' revenue, transaction price to book value, transaction price to tangible book value and transaction price to market price of target's stock before announcement. Sandler O'Neill then compared the imputed per share valuation for the high, mean, median and low data for the transactions with the book value per share and tangible book value per share valuations of SWS based on last twelve month's total revenue for FY2013. The results of these analyses are summarized in the following tables.

	Precedent Broker Dealer Transactions			
	High	**Mean**	**Median**	**Low**
Price / Last Twelve Months Revenue	2.4x	1.3x	1.0x	0.5x
Price / Book Value	171%	123%	118%	88%
Price / Tangible Book Value	171%	129%	120%	95%
Market Premium	15.6%	11.5%	11.5%	7.4%

	Imputed Per Share Valuation for Precedent Broker Dealer Transactions			
	High	**Mean**	**Median**	**Low**
Price / Last Twelve Months Revenue	$ 12.26	$ 6.46	$ 5.20	$ 2.52
Price / Book Value	$ 14.18	$ 10.25	$ 9.77	$ 7.27
Price / Tangible Book Value	$ 13.93	$ 10.48	$ 9.78	$ 7.72

	SWS Basis as of December 31, 2013	
2013 LTM Total Revenue ($ in millions)	Book Value / Share	Tangible Book Value / Share
$259.68	$8.30	$ 8.15

The second group of mergers and acquisitions included ten transactions announced between November 20, 2006 and December 16, 2013, selected based on Sandler O'Neill's professional judgment and experience. The group was composed of the following transactions:

Buyer / Target

Alfa Mutual / Alfa Corp.

Annaly Capital Management Inc. / CreXus Investment Corp

Banco Santander SA / Sovereign Bancorp Inc.

Bank of Tokyo-Mitsubishi UFJ Ltd. / UnionBanCal Corp, CA

CETCO Holding Company / Knight Capital Group

Fairfax Financial Holdings Limited / Odyssey Re Holdings Corp.

KKR & Co / KKR Financial Holdings

Leucadia National Corp / Jefferies Group Inc.

Nationwide Mutual Insurance Co / Nationwide Finl Svcs Inc.

Toronto-Dominion Bank / TD Banknorth Inc.

Sandler O'Neill then reviewed the following multiples for each of the transactions: initial offer to initial stock price, final offer to initial stock price and final offer to initial offer. Sandler O'Neill compared the proposed merger multiples to the high, mean, median and low multiples of these comparable transactions. The results of these analyses are summarized in the following table.

	Hilltop / SWS	Related Party Financial Services Transactions High	Mean	Median	Low
Initial Offer / Initial Stock Price	15.5%	40.6%	14.4%	14.0%	0.0%
Final Offer / Initial Stock Price	27.9%	50.6%	27.7%	29.3%	0.0%
Increase from Initial Offer	10.7%	26.7%	11.7%	7.8%	0.0%

Pro Forma Results

Sandler O'Neill analyzed certain potential pro forma effects of the merger, assuming the following: (i) the merger closes on September 30, 2014; (ii) per share merger consideration value of $7.75, based on Hilltop's closing stock price on March 20, 2014 of $23.29; (iii) SWS repays $100 million loan immediately prior to closing plus the applicable make-whole amount for early repayment of the loans to Oak Hill; (iv) the warrants held by Oak Hill are exercised prior to closing; (v) the warrants and shares held by Hilltop are cancelled prior to closing; (vi) SWS's performance is consistent with the financial forecasts and estimates prepared by the management of the Company; (vii) Hilltop's performance is consistent with publicly available mean analyst estimated earnings per share for the year ending December 31, 2015 and an estimated long-term growth rate of 10% for the years thereafter; (viii) the SWS common stock owned by Hilltop is eliminated immediately prior to closing, resulting in a $11.4 million negative purchase accounting adjustment; (ix) the impact of a $17.4 million negative purchase accounting adjustment relating to the cancellation of shares received from the exercise of the warrants; (x) Hilltop is able to achieve annualized cost savings of $25 million per year; (xi) pre-tax deal

related costs for Hilltop and SWS amount to $30 million and $2 million, respectively; (xii) a gross loan mark of $20 million at closing; (xiii) a $1 million mark on other real estate owned at closing; (xiv) customer relationship identifiable intangible of $7 million; (xv) reversal of only 40% of the deferred tax asset valuation at closing; and (xvi) an estimated bargain purchase gain of $31 million. The actual results achieved by the combined company, however, may vary from projected results and the variations may be material.

The table below shows Sandler O'Neill's projected accretion/dilution percentages for Hilltop as of closing and for each of the years 2014-2017.

	Closing	Year Ending 12/31/2014	Year Ending 12/31/2015	Year Ending 12/31/2016	Year Ending 12/31/2017
Hilltop Earnings Per Share Accretion / (Dilution) excluding transaction expenses		25.6%	9.4%	12.5%	12.0%
Hilltop Tangible Book Value Accretion / (Dilution)	13.2%	12.6%	11.3%	11.3%	11.3%

Other Information Reviewed By Sandler O'Neill

Historical Stock Trading Review

Sandler O'Neill also noted certain additional factors that were not considered part of its financial analyses with respect to its opinion but were referenced for informational purposes, including, among other things, the premium reflected in the merger consideration as compared to the unaffected stock price of approximately 27.9%; the premium reflected in the merger consideration as compared to the market price as of March 28, 2014 of approximately 4.0%; the premium reflected in the merger consideration as compared to the 52 week high of approximately (5.4%); the premium reflected in the merger consideration as compared to the 52 week low of approximately 49.3%; and the premium reflected in the merger consideration as compared to the one-month average of approximately (2.3%).

Stock Price Performance

Sandler O'Neill also reviewed for informational purposes the publicly reported trading prices of SWS's common stock for the three-year periods ended January 9, 2014, the date upon which SWS received the initial proposal from Hilltop, and March 25, 2014. Sandler O'Neill then compared the relationship between the movements in the price of SWS's common stock against the movements in the prices of the SWS peer group referenced above and the SNL U.S. Broker/Dealer Index.

Three-Year Comparative Stock Performance

	Beginning Value January 9, 2011	Ending Value January 9, 2014
SWS	100%	123.4%
SWS Peers	100%	140.6%
U.S. Broker Dealers	100%	122.6%

	Beginning Value March 25, 2011	Ending Value March 25, 2014
SWS	100%	128.5%
SWS Peers	100%	130.0%
U.S. Broker Dealers	100%	123.1%

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Sandler O'Neill also reviewed for informational purposes the publicly reported trading prices of Hilltop's common stock for the one-year and three-year periods ended March 28, 2014. Sandler O'Neill then compared the relationship between the movements in the price of Hilltop's common stock against the movements in the prices of the Hilltop peer group referenced above and the SNL U.S. Bank Index.

One-Year Comparative Stock Performance

	Beginning Value March 28, 2013	**Ending Value March 28, 2014**
Hilltop	100%	167.2%
Hilltop Peers	100%	132.9%
U.S. Banks	100%	127.3%

Three-Year Comparative Stock Performance

	Beginning Value March 28, 2011	**Ending Value March 28, 2011**
Hilltop	100%	224.8%
Hilltop Peers	100%	151.1%
U.S. Banks	100%	139.2%

Research Analyst Estimates and Price Targets

Sandler O'Neill reviewed analyst estimated earnings per share for SWS for 2014 and 2015 along with analyst estimated future price targets. The 2014 and 2015 earnings per share estimates and the future price target for SWS were based on a report from one research analyst.

Summary of SWS Analyst Estimates

Earnings Per Share		**Future Price**
2014	**2015**	**Target**
$ 0.01	$ 0.09	$ 8.00

Sandler O'Neill reviewed analyst estimated earnings per share for Hilltop for 2014 and 2015 along with analyst estimated future price targets. The median for 2014 and 2015 earnings per share was based on reports from three research analysts. The mean and median future price target for Hilltop was based on reports from four research analysts.

Summary of Hilltop Analyst Estimates

	Earnings Per Share		**Future Price**
	2014	**2015**	**Target**
Mean			$ 27.25
Median	$ 1.43	$ 1.65	$ 27.50

Reconciliation of Fully Converted Tangible Book Value

Sandler O'Neill noted the reconciliation of the fully converted tangible book value of SWS as of December 31, 2013, as summarized in the following table. The fully converted tangible common equity represents the tangible common equity as adjusted for the exercise of the Warrants. Such adjustments included the addition of the proceeds from the exercise of the Warrants (offset by certain tax-effected adjustments) to eliminate the balance sheet items related to SWS's outstanding debt and the Warrants.

The fully converted shares outstanding represents the shares outstanding adjusted for the exercise of the Warrants.

Reconciliation of Fully Converted Tangible Book Value

Fully Converted Tangible Common Equity	$ 411,351,000
Fully Converted Shares Outstanding	50,459,422
Fully Converted Tangible Book Value Per Share	$ 8.15

Hilltop's Projected Earnings Stream

As summarized in the following table, Sandler O'Neill noted Hilltop's projected earnings stream as derived from median consensus publicly available analyst estimates through the year ended December 31, 2015 and a consensus long-term earnings growth rate of 10% for the years ending 2016 and 2017.

	12/31/2013	12/31/2014	12/31/2015	12/31/2016	12/31/2017
Net Income (dollar value in thousands)	$ 121,015	$ 129,262	$ 149,286	$ 164,731	$ 181,191
Earnings Per Share	$ 1.40	$ 1.43	$ 1.65	$ 1.82	$ 2.00
Dividends Per Share	$ 0.00	$ 0.00	$ 0.00	$ 0.00	$ 0.00
Tangible Book Value Per Share	$ 9.70	$ 11.26	$ 13.03	$ 14.96	$ 17.06

Miscellaneous

Sandler O'Neill acted as the financial advisor to the Special Committee in connection with the merger and will receive a fee comprised of (i) $150,000 upon execution of the engagement letter, (ii) $250,000 for each time it indicates it is prepared to deliver a fairness opinion, subject to a maximum fee of $500,000 for all opinions, (iii) $350,000 upon the consummation of the merger and (iv) an incentive fee based on the price of a consummated merger of (a) $18,750.00 for each penny ($0.01) by which the per share price exceeds $7.75, up to $8.15; plus (b) $31,250.00 for each penny ($0.01) by which the per share price exceeds $8.15, up to $8.63; plus (c) $14,598.54 for each penny ($0.01) by which the per share price exceeds $8.63, up to $10.00. SWS has also agreed to reimburse Sandler O'Neill's reasonable out-of-pocket expenses incurred in connection with its engagement and to indemnify Sandler O'Neill and its affiliates and their respective partners, directors, officers, employee and agents against certain expenses and liabilities, including liabilities under the securities laws.

In the ordinary course of its respective broker and dealer businesses, Sandler O'Neill may purchase securities from and sell securities to SWS and Hilltop and their respective affiliates. Sandler O'Neill may also actively trade the debt and/or equity securities of SWS or Hilltop or their respective affiliates for their own accounts and for the accounts of their customers and, accordingly may at any time hold a long or short position in such securities. In the two years prior to the execution of the merger agreement, Sandler O'Neill has not provided investment banking services to, or received fees for such services from, SWS, Hilltop or Oak Hill, except for its services to the Special Committee in connection with the merger.

Certain SWS Prospective Financial Information

SWS management does not as a matter of course make public projections as to future performance or earnings and is especially wary of making projections for extended periods due to the significant unpredictability of the underlying assumptions and estimates. However, SWS provided, among other information, certain financial projections prepared by SWS management to Hilltop in connection with its consideration of the merger and to Sandler O'Neill, the financial advisor to the Special Committee.

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The financial projections reflect numerous estimates and assumptions with respect to industry performance, general business, economic, regulatory, market and financial conditions and other future events, as well as matters specific to SWS's business, all of which are inherently uncertain and difficult to predict and many of which are beyond SWS's control. These financial projections are subjective in many respects and thus are susceptible to multiple interpretations and periodic revisions based on actual experience and business developments. These projections may also be affected by SWS's ability to achieve strategic goals, objectives and targets over the applicable periods. As such, these financial projections constitute forward-looking information and are subject to risks and uncertainties, including the various risks set forth in the sections of this proxy statement/prospectus entitled "Forward Looking Statements" and "Risk Factors" and in SWS's Form 10-K for the fiscal year ended June 30, 2014 and the other reports filed by SWS with the SEC. The financial projections cover multiple years and such information by its nature becomes less reliable with each successive year.

The financial projections were not prepared with a view toward public disclosure or complying with GAAP, the published guidelines of the SEC regarding projections or the guidelines established by the American Institute of Certified Public Accountants for preparation and presentation of prospective financial information. Neither SWS's independent registered public accounting firm, nor any other independent accountants, have compiled, examined or performed any procedures with respect to the financial projections included below, nor have they expressed any opinion or any other form of assurance on such information or its achievability, and they assume no responsibility for, and disclaim any association with, the financial projections. Furthermore, the financial projections do not take into account any circumstances or events occurring after the date they were prepared.

You are strongly cautioned not to place undue reliance on the financial projections set forth below. The inclusion of the projections in this proxy statement/prospectus should not be regarded as an indication that any of SWS, Hilltop or their affiliates, advisors or representatives considered or consider the projections to be predictive of actual future events, and the projections should not be relied upon as such. None of SWS, Hilltop or their respective affiliates, advisors, officers, directors or representatives can give any assurance that actual results will not differ from the projections, and none of them undertakes any obligation to update or otherwise revise or reconcile the projections to reflect circumstances existing after the date such projections were generated or to reflect the occurrence of future events even in the event that any or all of the assumptions underlying the projections are shown to be in error. None of SWS, Hilltop or their respective affiliates, advisors or representatives makes any representation to any other person regarding the projections. The projections are not being included in this proxy statement/prospectus to influence a stockholder's decision regarding how to vote on any given proposal, but because the projections were provided to Hilltop and Sandler O'Neill.

Set forth below is a summary of the projections provided to Hilltop by SWS.

	Fiscal Year Ending June		
	2014	**2015**	**2016**
	(in thousands)		
Net Revenues	275,093	287,874	312,334
Non-Interest Expense	270,836	281,166	292,435
Gain/(Loss) on warrant	(91)		
Pre-tax Income	4,166	6,707	19,899

Set forth below is a summary of the projections used by Sandler O'Neill for purposes of its net present value analysis of SWS. These projections are the same as the projections provided to Hilltop except that Sandler O'Neill assumed, in consultation with SWS and with its consent, (i) an annualized growth rate in net revenues of approximately 8% for the remainder of 2016 and 5.6% in 2017, (ii) a reversal of the deferred tax assets valuation allowance on December 31, 2015 and (iii) that the current

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holders of SWS's outstanding warrants would exercise such warrants in 2016, with the proceeds of such exercise used to repay approximately $100 million of SWS's outstanding debt.

	Calendar Year Ending December 31			
	2014	2015	2016	2017
	(in thousands, except per share numbers)			
Net Revenues	279,472	300,273	324,645	342,828
Non-Interest Expense	274,285	287,593	270,083	299,315
Gain/(Loss) on warrant			24,288	
Pre-tax Income	5,187	12,680	54,562	43,513
Tax Provision		(24,395)	19,097	15,229
Net Income	5,187	37,075	35,465	28,284
Earnings per Share	$ 0.16	$ 0.85	$ 0.78	$ 0.56
Fully Converted Tangible Book Value per Share	$ 8.33	$ 9.14	$ 9.58	$ 10.15

Reconciliation of Non-GAAP to GAAP. The above projections used by Sandler O'Neill include the presentation of fully converted tangible book value per share. Fully converted tangible book value per share is a non-GAAP financial measure as defined by SEC rules. Fully converted tangible book value per share is stockholders' equity reduced by goodwill and other intangible assets, divided by total common shares outstanding and reflects the impact of the adjustments required if the warrants were fully exercised. This non-GAAP financial measure is useful in evaluating SWS, this information should be considered as supplemental in nature and not as a substitute for, or superior to, the related financial information prepared in accordance with GAAP. Pursuant to the applicable rules, regulations, interpretations and position of the SEC and its staff under the Exchange Act related to the presentation of non-GAAP financial information, the information in the following tables provides a reconciliation of fully converted tangible book value per share.

	Calendar Year Ending December 31			
	2014	2015	2016	2017
	(in thousands, except per share numbers)			
Book Value	318,651	355,726	491,191	519,474
Less: Goodwill and Other Intangibles	(7,552)	(7,552)	(7,552)	(7,552)
Tangible Book Value	311,099	348,174	483,639	511,922
Plus: Warrant Impact				
Exercise Price	100,000	100,000	NA(1)	NA(1)
After Tax Balance Sheet Adjustments(2)	9,000	12,869	NA(1)	NA(1)
Adjusted Tangible Book Value	420,099	461,043	483,639	511,922
Shares Outstanding	33,068,118	33,068,118	50,459,422	50,459,422
Warrant Shares	17,391,304	17,391,304	NA(1)	NA(1)
Full Converted Shares Outstanding	50,459,422	50,459,422	50,459,422	50,459,422
Tangible Book Value per Share	$ 9.41	$ 10.53	$ 9.58	$ 10.15
Fully Converted Tangible Book Value per Share	$ 8.33	$ 9.14	$ 9.58	$ 10.15

(1) Warrants assumed to be exercised concurrently with the maturity of the Hilltop and Oak Hill loan in July, 2016

(2) Includes after-tax impact of reversing warrant liability, debt discount and unamortized debt issuance costs

Public Trading Markets

Hilltop common stock trades on the New York Stock Exchange under the symbol "HTH". SWS common stock trades on the New York Stock Exchange under the symbol "SWS". The newly issued Hilltop common stock issuable pursuant to the merger agreement will be listed on the New York Stock Exchange under the symbol "HTH".

Appraisal / Dissenters' Rights

Holders of SWS common stock who do not vote for the adoption of the merger agreement and who are otherwise eligible and who otherwise comply with the applicable statutory procedures of Section 262 of the DGCL will have the right to obtain an appraisal of the value of their shares of SWS common stock in connection with the merger. This means that such stockholders are entitled to obtain a judicial determination of the fair value of their SWS shares (exclusive of any element of value arising from the accomplishment or expectation of the merger) determined by the Court of Chancery of the State of Delaware (the "Court of Chancery") and entitled to receive payment based upon that valuation, together with interest, if any, to be paid upon the amount determined to be a fair value, in lieu of any consideration to be received under the merger agreement.

The following is intended as a brief summary of the material provisions of the Delaware statutory procedures required to be followed by a stockholder in order to properly demand and perfect appraisal rights. This summary, however, is not a complete statement of law pertaining to appraisal rights under Delaware law and is qualified in its entirety by the full text of Section 262 of the DGCL, which is attached hereto as Annex C. The preservation and exercise of appraisal right requires strict and timely adherence to the applicable provisions of the DGCL. Failure to follow the requirements of Section 262 of the DGCL for demanding and perfecting appraisal rights may result in the loss of such rights. All references in this summary to a "stockholder" are to a record holder of SWS common stock on the record date for the special meeting unless otherwise indicated.

If you wish to consider exercising your appraisal rights, you should carefully review the text of Section 262 of the DGCL contained in Annex C hereto and should consult your legal advisor since failure to timely and properly comply with the requirements of Section 262 of the DGCL will result in the loss of your appraisal rights under the DGCL. All demands for appraisal must be received prior to the vote on the merger agreement and should be addressed to SWS, 1201 Elm Street, Suite 3500, Dallas, Texas 75270, Attention: Secretary, and should be executed by, or on behalf of, the record holder of the shares of SWS common stock. Holders of SWS common stock who desire to exercise their appraisal rights must not vote in favor of adoption of the merger agreement and must continuously hold their shares of SWS common stock through the effective date of the merger.

Under Section 262 of the DGCL, where a merger agreement relating to a proposed merger is to be submitted for adoption at a meeting of stockholders, as in the case of the special meeting, the corporation, not less than 20 days prior to such meeting, must notify each of its stockholders who was a stockholder on the record date for notice of such meeting with respect to shares for which appraisal rights are available, that appraisal rights are so available, and must include in each such notice a copy of Section 262 of the DGCL. This proxy statement/prospectus constitutes such notice to the holders of SWS common stock and Section 262 of the DGCL is attached to this proxy statement/prospectus as Annex C.

If you wish to exercise appraisal rights you must not vote for the adoption of the merger agreement and must deliver to SWS, before the vote on the proposal to adopt the merger agreement, a written demand for appraisal of your shares of SWS common stock. If you sign and return a proxy card that does not contain voting instructions or submit a proxy by telephone or through the Internet that does not contain voting instructions, you will effectively waive your appraisal rights because such shares represented by the proxy will, unless the proxy is revoked, be voted for the adoption of the merger agreement. Therefore, a stockholder who submits a proxy and who wishes to exercise appraisal rights must submit a proxy containing instructions to vote against the adoption of the merger agreement or abstain from voting on the adoption of the merger agreement. However, neither voting against the adoption of the merger agreement, nor abstaining from voting or failing to vote on the proposal to adopt the merger agreement, will in and of itself constitute a written demand for appraisal satisfying the requirements of Section 262 of the DGCL.

A demand for appraisal will be sufficient if it reasonably informs SWS of the identity of the stockholder and that such stockholder intends thereby to demand appraisal of such stockholder's shares of common stock. This written demand for appraisal must be separate from any proxy or vote abstaining from or voting against the adoption of the merger agreement. If you wish to exercise appraisal rights, you must be the record holder of such shares of SWS common stock on the date the written demand for appraisal is made and you must continue to hold such shares of record through the effective date of the merger. Accordingly, a stockholder who is the record holder of shares of common stock on the date the written demand for appraisal is made, but who thereafter transfers such shares prior to the effective date of the merger, will lose any right to appraisal in respect of such shares.

Only a holder of record of shares of SWS common stock on the record date for the special meeting is entitled to assert appraisal rights for such shares of common stock registered in that holder's name. To be effective, a demand for appraisal by a stockholder must be made by, or on behalf of, such stockholder of record. Beneficial owners who do not also hold their SWS shares of record may not directly make appraisal demands to SWS. The beneficial holder must, in such cases, have the owner of record, such as a broker, bank or other nominee, submit the required demand in respect of those shares of SWS common stock. If shares of SWS common stock are owned of record in a fiduciary capacity, such as by a trustee, guardian or custodian, execution of a demand for appraisal should be made by or for the fiduciary; and if the shares of SWS common stock are owned of record by more than one person, as in a joint tenancy or tenancy in common, the demand should be executed by or for all joint owners. An authorized agent, including an authorized agent for two or more joint owners, may execute the demand for appraisal for a stockholder of record; however, the agent must identify the record owner or owners and expressly disclose the fact that, in executing the demand, he or she is acting as agent for the record owner. A record owner, such as a broker, who holds shares of SWS common stock as a nominee for others, may exercise his or her right of appraisal with respect to the shares of SWS common stock held for one or more beneficial owners, while not exercising this right for other beneficial owners. In that case, the written demand should state the number of shares of SWS common stock as to which appraisal is sought. Where no number of shares of SWS common stock is expressly mentioned, the demand will be presumed to cover all shares of SWS common stock held in the name of the record owner.

If you hold your shares of SWS common stock in a brokerage account or in other nominee form and you wish to exercise appraisal rights, you should consult with your broker or the other nominee to determine the appropriate procedures for the making of a demand for appraisal by the nominee.

If any stockholder who demands appraisal under Delaware law fails to perfect or has effectively withdrawn or lost its right of appraisal, each share of SWS common stock held by such stockholder will be deemed to have been converted into and to have become, as of the effective time of the merger, the right to receive the merger consideration. A stockholder may withdraw his or her demand for appraisal and agree to accept the merger consideration by delivering to us a written withdrawal of his or her demand for appraisal and acceptance of the merger consideration within 60 days after the effective date of the merger (or thereafter with the consent of the surviving entity). Notwithstanding the foregoing, no appraisal proceeding in the Court of Chancery will be dismissed as to any stockholder without the approval of the Court of Chancery, and such approval may be conditioned upon such terms as the Court deems just; provided, however, that any stockholder who has not commenced an appraisal action or joined that proceeding as a named party may withdraw his or her demand for appraisal and agree to accept the merger consideration offered within 60 days after the effective date.

Within 10 days after the effective date of the merger, the surviving entity will notify each stockholder who properly asserted appraisal rights under Section 262 of the DGCL and has not voted for the adoption of the merger agreement of the effective date of the merger. Within 120 days after the effective date of the merger, but not thereafter, either the surviving entity, or any stockholder who has complied with the requirements of Section 262 of the DGCL and who is otherwise entitled to appraisal rights, may file a petition in the Court of Chancery demanding a determination of the fair value of the shares of SWS common stock held by all stockholders entitled to appraisal. A person who is the beneficial owner of shares of SWS common stock held in a voting trust or by a nominee on behalf of such person may, in such person's own name, file the petition described in the previous sentence. Upon the filing of the petition by a stockholder, service of a copy of such petition shall be made upon the surviving entity. The surviving entity of the merger does not have an obligation to file such a petition in the event there are dissenting stockholders. Accordingly, the failure of a stockholder to file such a petition within the period specified could nullify the stockholder's previously written demand for appraisal. Hilltop has no present intent to cause an appraisal petition to be filed, and stockholders seeking to exercise appraisal rights should not assume that the surviving entity will file such a petition or that it will initiate any negotiations with respect to the fair value of such shares of SWS common stock. Accordingly, stockholders who desire to have their shares of SWS common stock appraised should initiate any petitions necessary for the perfection of their appraisal rights within the time periods and in the manner prescribed in Section 262 of the DGCL.

The costs of the appraisal action may be determined by the Court of Chancery and made payable by the parties as the Court deems equitable in the circumstances. The Court also may order that all or a portion of the expenses incurred by any stockholder in connection with an appraisal, including, without limitation, reasonable attorneys' fees and the fees and expenses of experts utilized in the appraisal proceeding, be charged pro rata against the value of all of the shares entitled to appraisal.

If a petition for appraisal is duly filed by a stockholder and a copy of the petition is delivered to the surviving entity of the merger, such surviving entity will then be obligated, within 20 days after receiving service of a copy of the petition, to provide the Court of Chancery with a duly verified list containing the names and addresses of all stockholders who have demanded payment for their shares of SWS common stock and with whom agreements as to the value of their shares of SWS common stock have not been reached by the surviving entity. After notice to dissenting stockholders who demanded payment of their shares of SWS common stock, the Court of Chancery is empowered to conduct a hearing upon the petition, and to determine those stockholders who have complied with Section 262 of the DGCL and who have become entitled to the appraisal rights provided thereby. The Court of Chancery may require the stockholders who have demanded appraisal for their shares of SWS common stock to submit their stock certificates to the Register in Chancery for notation thereon of the pendency of the appraisal proceedings; and if any stockholder fails to comply with that direction, the Court of Chancery may dismiss the proceedings as to that stockholder.

Within 120 days after the effective date, any stockholder (including any beneficial owner of shares entitled to appraisal rights) that has complied with the requirements for exercise of appraisal rights will be entitled, upon written request, to receive from the surviving entity a statement setting forth the aggregate number of shares of SWS common stock not voted in favor of adoption of the merger agreement and with respect to which demands for appraisal have been received and the aggregate number of holders of those shares. These statements must be mailed to the stockholder within 10 days after a written request by such stockholder for the information has been received by the surviving entity, or within 10 days after expiration of the period for delivery of demands for appraisal under Section 262 of the DGCL, whichever is later.

After determination of the stockholders entitled to appraisal of their shares of SWS common stock (unless the Court of Chancery, in its discretion, proceeds to trial upon the appraisal prior to the final determination of the stockholders entitled to an appraisal), the Court of Chancery will appraise the shares of SWS common stock, determining their fair value exclusive of any element of value arising from the accomplishment or expectation of the merger, together with interest, if any. Unless the Court of Chancery in its discretion determines otherwise for good cause shown, interest from the effective date through the date of payment of the judgment shall be compounded quarterly and shall accrue at 5% over the Federal Reserve discount rate (including any surcharge) as established from time to time during the period between the effective date of the merger and the date of payment of the judgment. When the value is determined, the Court of Chancery will direct the payment of such value, with interest thereon, if any, to the stockholders entitled to receive the same, upon surrender by such stockholders of their certificates representing such shares or surrender of their book-entry shares, as applicable.

In determining the fair value of the shares of SWS common stock, the Court of Chancery is required to take into account all relevant factors. Accordingly, such determination could be based upon considerations other than, or in addition to, the market value of the shares of SWS common stock, including, among other things, asset values and earning capacity. In *Weinberger v. UOP, Inc.*, the Delaware Supreme Court stated, among other things, that "proof of value by any techniques or methods which are generally considered acceptable in the financial community and otherwise admissible in court" should be considered in an appraisal proceeding. The surviving entity of the merger may argue in an appraisal proceeding that, for purposes of such a proceeding, the fair value of the shares of SWS common stock is less than the merger consideration. Therefore, the value so determined in any appraisal proceeding could be the same as, or more or less than, the merger consideration.

Section 262 of the DGCL provides that fair value is to be "exclusive of any element of value arising from the accomplishment or expectation of the merger." In *Cede & Co. v. Technicolor, Inc.*, the Delaware Supreme Court stated that such exclusion is a "narrow exclusion [that] does not encompass known elements of value," but which rather applies only to the speculative elements of value arising from such accomplishment or expectation. In *Weinberger*, the Delaware Supreme Court construed Section 262 of the DGCL to mean that "elements of future value, including the nature of the enterprise, which are known or susceptible of proof as of the date of the merger and not the product of speculation, may be considered." In view of the complexity of Section 262 of the DGCL, stockholders who may wish to pursue appraisal rights should consult their legal advisors.

Any stockholder who has duly demanded and perfected an appraisal in compliance with Section 262 of the DGCL will not, after the effective date of the merger, be entitled to vote his or her shares for any purpose or be entitled to the payment of dividends or other distributions thereon, except dividends or other distributions payable to holders of record of shares of SWS common stock as of a date prior to the effective date of the merger.

If you desire to exercise your appraisal rights, you must not vote for the adoption of the merger agreement and you must strictly comply with the procedures set forth in Section 262 of the DGCL. Failure to take any required step in connection with the exercise of appraisal rights will result in the termination or waiver of such rights.

Regulatory Approvals Required for the Merger

Hilltop and SWS have agreed to use their reasonable best efforts to obtain all regulatory approvals required to complete the transactions contemplated by the merger agreement, including the merger and the bank merger. These approvals include approvals from the Federal Reserve Board and the Texas Department of Banking and, to the extent required, the expiration or termination of any applicable waiting period under the HSR Act. Hilltop and SWS have filed, or are in the process of filing, applications and notifications to obtain the required regulatory approvals.

Federal Reserve Board. The transactions contemplated by the merger agreement are subject to approval by the Federal Reserve Board pursuant to section 4 of the Bank Holding Company Act. The Federal Reserve Board takes into consideration a number of factors when acting on notices under section 4 of the BHC Act of 1956 (12 U.S.C. § 1843(j)) and Regulation Y (12 CFR 225.26). These factors include the financial and managerial resources (including consideration of the competence, experience, and integrity of the officers, directors, and principal shareholders, as well as the pro forma capital ratios) and future prospects of the combined organization. The Federal Reserve Board also considers whether the transaction can reasonably be expected to produce benefits to the public, such as greater convenience, increased competition, or gains in efficiency, that outweigh possible adverse effects, such as undue concentration of resources, decreased or unfair competition, conflicts of interest, or unsound banking practices. The Federal Reserve Board must also consider the extent to which the proposal would result in greater or more concentrated risks to the stability of the U.S. banking or financial system.

The merger of PlainsCapital Bank and Southwest Securities, FSB contemplated by the merger agreement is subject to approval by the Federal Reserve Board pursuant to the Bank Merger Act, 12 U.S.C. § 1828(c), and pursuant to Section 9 of the Federal Reserve Act. The Federal Reserve Board takes into consideration a number of factors when acting on applications under the Bank Merger Act. These factors include the financial and managerial resources (including consideration of the competence, experience, and integrity of the officers, directors, and principal shareholders) and future prospects of the combined organization. The Federal Reserve Board also considers the effectiveness of the applicant in combatting money laundering, the convenience and needs of the communities to be served, as well as the extent to which the proposal would result in greater or more concentrated risks to the stability of the U.S. banking or financial system. The Federal Reserve Board may not approve a proposal that would have significant adverse effects on competition or on the concentration of resources in any banking market.

In reviewing the convenience and needs of the communities to be serviced, the Federal Reserve Board will consider the records of performance of the relevant insured depository institutions under the CRA. In their most recent respective CRA examinations, both PlainsCapital Bank and Southwest Securities, FSB received an overall "satisfactory" regulatory rating.

Furthermore, the Bank Merger Act and applicable regulations require published notice of, and the opportunity for public comment on, these applications. The Federal Reserve Board will take into account the views of third party commenters, particularly on the subject of the merging parties' service to their respective communities, and any hearing, meeting or comments provided by third parties could prolong the period during which the application is under review by the Federal Reserve Board.

Transactions approved under the Bank Merger Act generally may not be completed until 30 days after the approval of the applicable federal agency is received, during which time the Department of Justice ("DOJ") may challenge the transaction on antitrust grounds. With the approval of the applicable federal agency and the concurrence of the DOJ, the waiting period may be reduced to no less than 15 days. The commencement of an antitrust action would stay the effectiveness of such an approval unless a court specifically ordered otherwise. In reviewing the merger, the DOJ could analyze the merger's effect on competition differently than the Federal Reserve Board, and thus it is possible that the DOJ could reach a different conclusion than the Federal Reserve Board regarding the transaction's effects on competition. A determination by the DOJ not to object to the merger may not prevent the filing of antitrust actions by private persons or state attorneys general.

Antitrust Considerations. The HSR Act, and the rules and regulations thereunder, provide that the transaction may not be completed until pre-merger notification filings have been made with the Federal Trade Commission (the "FTC") and the Antitrust Division of the DOJ (the "Antitrust Division") and any applicable waiting period has expired or is terminated. Even after the waiting period expires or is terminated, the Antitrust Division and the FTC retain the authority to challenge the transaction on

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antitrust grounds before or after the transaction is completed. Each of Hilltop and SWS filed a notification and report form for the transaction with the FTC and the Antitrust Division on May 14, 2014. On May 28, 2014, the parties received early termination of the waiting period under the HSR Act with respect to the transaction.

Additional Regulatory Approvals and Notices. A copy of the application submitted to the Federal Reserve Board in connection with the merger must be submitted to the Texas Department of Banking, which must approve the transaction, and Southwest Securities, FSB must submit a notification to the Office of the Comptroller of the Currency. Notifications and/or applications requesting approval may be submitted to various other federal and state regulatory authorities and self-regulatory organizations.

Timing. We cannot assure you that all of the regulatory approvals described above will be obtained and, if obtained, we cannot assure you as to the timing of any such approvals, our ability to obtain the approvals on satisfactory terms or the absence of any litigation challenging such approvals. We also cannot assure you that any third party will not attempt to challenge the merger on antitrust grounds, and, if such a challenge is made, we cannot assure you as to its result.

Hilltop and SWS believe that the merger does not raise substantial antitrust or other significant regulatory concerns and that we will be able to obtain all requisite regulatory approvals on a timely basis without the imposition of any condition that would have a material adverse effect on Hilltop or SWS. The parties' obligation to complete the merger is conditioned upon the receipt of all required regulatory approvals and Hilltop's obligation to complete the merger is conditioned upon there being no action taken or determination made, or any law enacted or deemed applicable to the transactions contemplated by the merger agreement by any governmental entity, in connection with the grant of any requisite regulatory approvals, which imposes or would result in the imposition of a restriction on Hilltop, SWS or the surviving company in connection therewith, that would reasonably be expected to have a material adverse effect (measured on a scale relative to SWS) on Hilltop or SWS.

We are not aware of any material governmental approvals or actions that are required for completion of the merger other than those described above. It is presently contemplated that if any such additional governmental approvals or actions are required, those approvals or actions will be sought. There can be no assurance, however, that any additional approvals or actions will be obtained.

Interests of SWS Directors and Executive Officers in the Merger

At the effective time of the merger, each share of SWS common stock held by SWS's directors and executive officers (other than certain restricted shares, as described below under "Equity Awards Restricted shares (post-merger agreement grants) Executive officers") will be converted into the right to receive the merger consideration (i.e., 0.2496 shares of Hilltop common stock and $1.94 in cash) on the same basis as SWS stockholders generally.

In addition, in considering the recommendation of the Board that you approve the merger agreement, you should be aware that SWS's directors and executive officers have interests in the merger that are different from, or in addition to, those of SWS stockholders generally. The members of the Board were aware of these interests and considered them, among other matters, in evaluating the merger agreement, in reaching their decision to adopt the merger agreement, and in recommending to SWS stockholders that the merger agreement be approved. These interests, which are described and quantified below, include the following:

Equity Awards. In connection with the merger, equity awards held by SWS's directors and executive officers will be treated as follows:

Restricted shares (pre-merger agreement grants). At the effective time of the merger, each restricted share of SWS common stock that was granted prior to the date of the merger agreement will vest in full, and the directors and executive officers will be entitled to receive the merger consideration for each such share on the same basis as SWS stockholders generally, less applicable withholding taxes (which will be withheld first from the cash portion of the merger consideration payable in respect of each such share).

Restricted shares (post-merger agreement grants). The merger agreement permits SWS to grant, prior to the effective time of the merger, restricted shares of SWS common stock to executive officers and non-employee directors of SWS on the following terms:

Executive officers. On August 20, 2014, the SWS compensation committee granted restricted shares of SWS common stock to certain executive officers and key employees of SWS, as specified in the merger agreement, in satisfaction of the fiscal 2014 annual bonuses that they earned based on achievement of the applicable pre-tax net income performance goal under the applicable SWS bonus plans, subject to certain adjustments and individual business line results. The aggregate grant date value of such restricted shares was $1,325,434 and the aggregate number of such restricted shares was 181,814. Such restricted shares will vest one-third on each of the first three anniversaries of the grant date, subject to the holder's continued employment through each applicable vesting date. The vesting of such restricted shares will not accelerate at the effective time of the merger and such restricted shares will not be converted into the merger consideration. Instead, the restricted shares will be converted into restricted shares of Hilltop common stock, with the number of Hilltop shares determined based on the value of the merger consideration. Following the effective time of the merger, Hilltop restricted shares will continue to vest in accordance with the original terms of the SWS restricted shares and will vest (i) as to all of such restricted shares on termination of employment by the employer without "cause" (see definition below under "*Golden Parachute Compensation Definition of 'Cause'"*) following the effective time of the merger, (ii) as to all of such restricted shares upon a change of control event (other than the merger) and (iii) as to a prorated portion of such restricted shares on termination of employment due to an employee's death or disability.

Directors. SWS may grant restricted shares of SWS common stock to non-employee directors of SWS in the ordinary course of business consistent with past practice with a grant date value not to exceed $35,000 per director.

Deferred shares. At the effective time of the merger, each deferred share of SWS common stock reflected in the accounts of executive officers under SWS's deferred compensation plans will be converted into 0.3328 of a deferred share of Hilltop common stock (i.e., the sum of the portion of the merger consideration paid in Hilltop common stock and a number of shares of Hilltop common stock with a value as of immediately prior to the date of the merger agreement that is equal to the portion of the merger consideration paid in cash). Following the effective time of the merger, any such deferred shares that are not vested will continue to vest in accordance with the original terms of the SWS deferred shares and will vest in full on termination of employment by the employer without "cause" (see definition below under "*Golden Parachute Compensation Definition of 'Cause'*"). Hilltop deferred shares will be distributed to the executive officers in accordance with the terms of the applicable plan and the participants' individual elections.

For an estimate of the amounts that would become payable to each of the SWS named executive officers and other executive officers on settlement of their unvested equity awards, see "*Golden Parachute Compensation*" below.

Severance and Retention Payments. Under the merger agreement, SWS's executive officers may be entitled to severance and retention payments on the following terms:

Severance practice. On termination of employment by the employer without "cause" (see definition below under "*Golden Parachute Compensation Definition of 'Cause'*") at any time on or prior to December 31, 2015, the executive officers (and other SWS employees) are entitled to cash severance in accordance with SWS's severance practice. The amount of such severance is equal to two weeks of base salary for each year of service, not to exceed 24 weeks of base salary. The severance is contingent on the executive's (or other employee's) execution and non-revocation of a release of claims. For an estimate of the value of the payments described above that would be payable under the SWS severance practice to each of the SWS named executive officers and other executive officers, see "*Golden Parachute Compensation*" below.

Retention agreements. As permitted under the terms of the merger agreement, SWS is permitted to enter into retention agreements with employees in an aggregate amount up to $5,000,000. As of the date of this proxy statement/prospectus, SWS has entered into retention agreements with certain executive officers (and other employees) that provide for cash retention payments in the aggregate amount of $4,418,800, of which $975,000 in the aggregate is payable under the agreements with certain executive officers. These retention amounts will be paid in a lump sum within 30 days of the six-month anniversary of the effective time of the merger, subject to the applicable executive officer's or other employee's continued employment with SWS through such six-month anniversary (except that, on a termination of employment by the employer without "cause" (see definition below under "*Golden Parachute Compensation Definition of 'Cause'*") after the effective time, the retention payment will be paid within 30 days of such termination date, contingent on the executive's (or other employee's) execution and non-revocation of a release of claims). Pursuant to the applicable retention agreement, the executive (or other employee) is subject to certain confidentiality obligations during employment with SWS and thereafter, as well as a restriction on soliciting employees and customers of SWS during employment and for 12 months thereafter.

Indemnification. Directors and executive officers of SWS have rights to indemnification, expense advancement and directors' and officers' liability insurance that will survive the effective time of the merger. See "*Indemnification of SWS Directors and Officers and Continuation of Directors' and Officers' Insurance*".

Messrs. Gerald J. Ford and J. Taylor Crandall are members of the SWS board of directors appointed by Hilltop and Oak Hill, respectively. Messrs. Ford and Crandall recused themselves from the vote of the SWS board of directors with respect to the approval and adoption of the merger agreement and the transactions contemplated thereby, including the merger. The decisions by the SWS Board that are described in this proxy statement/prospectus were all taken by unanimous vote of those directors who voted.

Golden Parachute Compensation

This section sets forth the information required by Item 402(t) of Regulation S-K regarding the compensation that may be paid or would be payable to SWS's "named executive officers" (as defined under SEC disclosure rules) that is based on or otherwise relates to the merger. The table below sets forth for each of SWS's six named executive officers estimates of the amounts of compensation that are based on or otherwise relate to the merger and that may be paid or would be payable to the executive either immediately after the effective time of the merger or on a subsequent termination of employment by the employer without "cause" (as defined below). SWS stockholders are being asked to approve, on a non-binding, advisory basis, such compensation for these named executive officers (see

"*Non-Binding Advisory Vote Approving Compensation (Proposal 2)*" beginning on page 67). Because the vote to approve such compensation is advisory only, it will not be binding on either SWS or Hilltop. Accordingly, if the merger agreement is approved by SWS stockholders and the merger is completed, the compensation will be paid (or payable) regardless of the outcome of the vote to approve such compensation, subject only to the conditions applicable thereto, which are described in the footnotes to the table below.

The table below also sets forth estimates of the amounts of such compensation for SWS's two executive officers who are not named executive officers. SWS stockholders are not being asked to approve such compensation for these executive officers.

The estimates in the table below assume that the merger had become effective on October 13, 2014 (the latest practicable date before the date of this proxy statement/prospectus) and that the employment of each of the executive officers was terminated without "cause" (as defined below) immediately thereafter. See the footnotes to the table for additional information.

Name	Cash ($)(1)	Equity ($)(2)	Pension/ NQDC ($)	Perquisites/ Benefits ($)	Tax Reimbursement ($)	Other ($)	Total ($)
Named Executive Officers							
James H. Ross, President and Chief Executive Officer	623,077	1,980,837	0	0	0	0	2,603,914
J. Michael Edge, Interim Chief Financial Officer and Treasurer	291,154	90,469	0	0	0	0	381,623
Stacy M. Hodges, Executive Vice President, Chief Financial Officer and Treasurer(3)							
Robert A. Chereck, Executive Chairman and President of Southwest Securities, FSB	126,923	13,427	0	0	0	0	140,350
Daniel R. Leland, Executive Vice President	103,846	387,425	0	0	0	0	491,271
Richard H. Litton, Executive Vice President	103,846	611,989	0	0	0	0	715,835
Other Executive Officers							
W. Norman Thompson, Executive Vice President and Chief Information Officer	253,846	254,009	0	0	0	0	507,855
Allen R. Tubb, Executive Vice President, General Counsel and Secretary	288,462	319,241	0	0	0	0	607,703

(1) The amounts in this column reflect the cash severance payment that each executive would be entitled to receive on termination of employment by the employer without "cause" (as defined below) on or prior to December 31, 2015 in accordance with SWS's severance practice (see above under "*Severance and Retention Payments Severance practice*"). For Messrs. Ross, Edge, Chereck, Thompson and Tubb, the amount in this column also reflects a cash retention payment that each executive is eligible to receive pursuant to his retention agreement with SWS (see above under "*Severance and Retention Payments Retention agreements*"). These retention payments will be paid in a lump sum within 30 days of the six-month anniversary of the effective time of the merger, subject to the applicable executive's continued employment with SWS through such six-month anniversary (except that, on a termination of employment by the employer without "cause" (see definition below under "*Definition of 'Cause'*") after the effective time, the retention payment will be paid within 30 days of such termination date, contingent on the executive's execution and non-revocation of a release of claims).

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The following table breaks down the amounts in this column by severance payment versus retention payment.

Name	Severance Payment ($)	Retention Payment ($)
James H. Ross	173,077	450,000
J. Michael Edge	166,154	125,000
Stacy M. Hodges		
Robert A. Chereck	26,923	100,000
Daniel R. Leland	103,846	
Richard H. Litton	103,846	
W. Norman Thompson	103,846	150,000
Allen R. Tubb	138,462	150,000

(2)

For all named executive officers and executive officers other than Mr. Edge, the amount in this column reflects the value of the accelerated vesting of the executives' outstanding unvested restricted shares of SWS common stock granted prior to the date of the merger agreement that would occur at the effective time of the merger (i.e., on a "single-trigger" basis). For Mr. Edge, the amount in this column reflects the value of the accelerated vesting of his deferred shares of SWS common stock, assuming Mr. Edge's employment was terminated by the employer without "cause" upon the effective time of the merger (i.e., on a "double-trigger" basis). At the effective time of the merger, each such restricted share will be converted into the merger consideration (i.e., 0.2496 shares of Hilltop common stock and $1.94 in cash) on the same basis as shares SWS stockholders generally and each such deferred share will be converted into 0.3328 of a deferred share of Hilltop common stock.

For all named executive officers and executive officers other than Mr. Chereck, the amount in this column also reflects the value of the accelerated vesting of the executives' restricted shares of SWS common stock granted after the date of the merger agreement in satisfaction of their fiscal 2014 annual bonuses that would occur on termination of employment by the employer without "cause" (i.e., on a "double-trigger" basis) (see above under "*Restricted shares (post-merger agreement grants) Executive officers*"), assuming each executive's employment was terminated without "cause" upon the effective time of the merger. At the effective time of the merger, such restricted shares will be converted into a number of restricted shares of Hilltop common stock, with the number of Hilltop shares determined based on the value of the merger consideration, which, for purposes of this column, has been estimated to equal 0.3439 of a restricted share of Hilltop common stock, based on the average of the high and low prices of a Hilltop share on the New York Stock Exchange from October 2, 2014 through October 8, 2014. The actual number of restricted shares of Hilltop common stock will be determined based on the average of the high and low sales prices of a Hilltop share on the New York Stock Exchange on each of the five consecutive trading days ending on the trading day that is two trading days prior to the closing date of the merger. Mr. Chereck was not granted any such restricted shares as his entire fiscal 2014 annual bonus was paid in cash.

For purposes of this column, each Hilltop share is assumed to have a value of $24.33 (which represents the average closing market price of Hilltop's securities over the first five business days following the first public announcement of the merger on April 1, 2014).

Under the SWS Group, Inc. Deferred Compensation Plan, participants who elect to defer amounts under the plan are eligible for allocations of employer matching contributions in the form of deferred shares of SWS common stock (see "*Equity Awards Deferred shares*" above). Mr. Edge is the only executive officer who elected to defer amounts under the plan for 2014, and so he is eligible for allocations of deferred shares to his account under the plan for 2014. The amounts in this column do not reflect any additional deferred shares that may be allocated after the date hereof to Mr. Edge's account under the plan. The vesting of any such additional deferred shares would accelerate on a termination of Mr. Edge's employment by SWS without "cause" following the effective time of the merger (i.e., on a "double-trigger" basis).

The following table breaks down the amounts in this column by awards of restricted versus deferred shares, and by whether the vesting of the restricted shares would accelerate on a "single-trigger" or "double-trigger" basis (the vesting of all of the deferred shares would accelerate on a "double-trigger" basis).

Name	"Single-Trigger" Restricted Shares ($)	"Double-Trigger" Restricted Shares ($)	"Double-Trigger" Deferred Shares ($)
James H. Ross	1,636,519	344,318	
J. Michael Edge		86,080	4,389
Stacy M. Hodges			
Robert A. Chereck	13,427		
Daniel R. Leland	249,693	137,732	
Richard H. Litton	168,988	443,001	
W. Norman Thompson	182,284	71,725	
Allen R. Tubb	233,161	86,080	

(3)
Ms. Hodges resigned from SWS as of September 30, 2013.

As discussed above, on termination of employment by the employer without "cause", the executive officers are entitled to severance payments in accordance with SWS's severance practice (if such termination occurs on or before December 31, 2015, and contingent on the executive's execution and non-revocation of a release of claims) and accelerated vesting of their deferred shares. In addition, the additional restricted shares of SWS common stock that were granted to the executive officers following the execution of the merger agreement will accelerate in full on termination of employment by the employer without "cause". For these purposes, "cause" means the executive's:

- plea of guilty or *nolo contendere* to a charge of commission of a felony or a crime requiring intent or involving moral turpitude;
- misappropriating or embezzling funds of SWS or any of its affiliates or of a client or customer of SWS or any of its affiliates that are under the control of SWS or any such affiliate;
- intentionally pursuing interests of, or for the benefit of, a competitor to the detriment of the financial interests of SWS or its affiliates;
- willful failure or refusal to perform employment duties assigned by SWS;
- gross negligence or willful misconduct in connection with the performance of his duties and services as a service provider of SWS or its affiliates;
- forfeiture or suspension of any license or certificate necessary for the performance of his duties;
- involvement in impermissible employment discrimination or failure to adhere to other material policies of SWS or its affiliates, including any code of conduct, as determined by SWS; or
- material breach of any obligations under a restrictive covenant agreement with SWS or its affiliates.

In each case (other than the first two events described above), SWS must provide the executive with written notice specifying the circumstances alleged to constitute "cause" and, to the extent subject to cure, the executive will have 30 days following receipt of such notice to cure such circumstances to SWS's reasonable satisfaction.

In addition, the cash retention amounts payable pursuant to the retention agreements entered into between SWS and Messrs. Ross, Chereck, Thompson, Tubb and Edge will accelerate on termination of employment by the employer without "cause". For this purpose, "cause" means the executive's:

- willful and repeated refusal to perform his duties with reasonable diligence, or to follow a lawful directive of the CEO or the Board commensurate with his position (other than a failure or refusal resulting from his incapacity);
- commission of an act involving a breach of trust, fraud, embezzlement, or theft against the property or personnel of SWS;
- engagement in conduct that SWS in good faith reasonably determines will be materially harmful to the reputation, business, assets, properties, results of operations or financial condition of SWS; or
- being identified as under investigation for a crime involving fraud, breach of trust or dishonesty (including any indictment).

In the case of the first and third events, SWS must first provide the executive with 15 days' prior written notice specifying the circumstances alleged to constitute "cause", and the executive will have a reasonable opportunity to cure such circumstances, if practicable, within such 15-day period, as determined by SWS in its sole discretion.

Indemnification of SWS Directors and Officers and Continuation of Directors' and Officers' Insurance

Each of Hilltop and Peruna LLC has agreed to indemnify and advance expenses to each present and former director and officer of SWS and its subsidiaries (when acting in such capacity) to the fullest extent permitted by law for any acts arising out of or pertaining to matters occurring at or existing prior to the closing. Additionally, Hilltop will provide director and officer liability insurance with respect to claims arising from facts or events occurring before the completion of the merger, which will contain at least the same coverage and amounts, and on no less advantageous terms to the indemnified party as that coverage currently provided by SWS, at an aggregate cost per annum not to exceed 300% of the annual aggregate premiums currently paid by SWS for such insurance, provided that if premiums for such insurance would exceed such cap, then Hilltop will maintain policies of insurance which provide the maximum coverage available at an annual premium equal to such cap. In lieu of the foregoing insurance, prior to the closing, SWS may purchase "tail" D&O insurance, at an aggregate cost not to exceed 300% of the annual aggregate premiums currently paid by it for such insurance.

Hilltop's Relationship with SWS

In March 2011, Hilltop, Oak Hill Capital Partners III, L.P. ("OHCP") and Oak Hill Capital Management Partners III, L.P. (collectively with OHCP, "Oak Hill") entered into a Funding Agreement (the "Funding Agreement") with SWS. On July 29, 2011, after receipt of regulatory and SWS stockholder approval, SWS completed the following transactions contemplated by the Funding Agreement:

- entered into a $100,000,000, five-year, unsecured loan comprised of equal commitments from each of Hilltop and Oak Hill under the terms of a credit agreement (the "Credit Agreement");
- issued warrants to each of Hilltop and Oak Hill for the purchase of up to 8,695,652 shares of SWS's common stock by each of Hilltop and Oak Hill exercisable for five years from the date of issuance at a fixed exercise price of $5.75 per share, subject to anti-dilution adjustments; and
- granted each of Hilltop and Oak Hill certain rights, including registration rights, preemptive rights, and the right for each to appoint one person to the board of directors of SWS for so long

as it owns 9.9% or more of all of the outstanding shares of SWS's common stock or securities convertible into at least 9.9% of SWS's outstanding common stock.

On October 2, 2014, Hilltop exercised its warrant in full, acquiring 8,695,652 shares of SWS common stock for the warrant exercise price of $5.75 per share. Pursuant to the terms of the warrant and Credit Agreement, the exercise price was paid by an automatic elimination of the $50,000,000 amount outstanding due to Hilltop under the Credit Agreement. Accordingly, as of the date of this proxy statement/prospectus, Hilltop (i) owns 10,171,039 shares of SWS common stock, representing approximately 21.0% of the outstanding shares of SWS common stock and (ii) is no longer a lender under the Credit Agreement. Mr. Gerald J. Ford, who is Chairman of Hilltop's board of directors, currently serves as Hilltop's designee on SWS's board of directors. Hilltop has agreed in the merger agreement to vote any shares of SWS that it owns as of the record date for the SWS special meeting in favor of approval and adoption of the merger agreement.

In connection with its acquisition of PlainsCapital Corporation in 2012, Hilltop provided certain passivity commitments to the Federal Reserve Board related to SWS. These passivity commitments provide that Hilltop cannot take certain actions, namely exercising any controlling influence over management or policies of SWS, without the prior approval of the Federal Reserve Bank.

The terms of the Credit Agreement include a covenant prohibiting SWS from undergoing a "Fundamental Change," which includes any merger, amalgamation or consolidation, and which SWS would breach by engaging in a merger, amalgamation or consolidation unless compliance were waived by each lender thereunder. During the parties' negotiations with respect to the merger, Hilltop indicated to SWS that it would not be willing to grant a waiver of this covenant to permit a third party transaction (see "The Merger Background of the Merger"). The Credit Agreement also prohibits SWS from prepaying the loan other than following a period during which the closing price for SWS common stock exceeds 150% of the exercise price of the warrants (or $8.625) for twenty out of any thirty consecutive trading days.

Oak Hill Letter Agreement

On September 26, 2014, Oak Hill partially exercised its warrants, acquiring a total of 6,521,739 shares of SWS common stock for the warrant exercise price of $5.75 per share. Pursuant to the terms of the warrant and Credit Agreement, the exercise price was paid by an automatic reduction by $37,499,999.25 of the $50,000,000 amount which had previously been due to Oak Hill under the Credit Agreement. Accordingly, as of the date of this proxy statement/prospectus, Oak Hill (i) owns and is entitled to vote 6,521,739 shares of SWS common stock, representing approximately 13.5% of the outstanding shares of SWS common stock, (ii) beneficially owns an additional 2,173,913 shares of SWS common stock pursuant to the unexercised portion of Oak Hill's warrants, equivalent to total beneficial ownership of approximately 17.2% if Oak Hill's warrants were fully exercised and (iii) remains a lender under the Credit Agreement with an outstanding loan balance of $12,500,000.75, which is the entire amount currently outstanding under the Credit Agreement. In addition, Oak Hill Capital Management, LLC and OHCM Management LLC, which are affiliates of Oak Hill, beneficially own an additional 19,925 shares of SWS common stock, equivalent to approximately 0.04% of the currently outstanding SWS common shares.

On March 31, 2014, concurrently with the entry by Hilltop and SWS into the merger agreement, SWS entered into a letter agreement with Oak Hill (the "Oak Hill Letter Agreement"). The Oak Hill Letter Agreement, among other things, provides:

(a) that Oak Hill (i) irrevocably and unconditionally waives compliance by SWS with the covenant in the Credit Agreement that prohibits SWS from undergoing a "Fundamental Change", with respect to the merger on the terms set forth in the merger agreement; (ii) irrevocably and unconditionally consents for all purposes under the Credit Agreement to the consummation of the merger on the terms set forth in the merger agreement, to the extent such consent is required for the consummation of the merger by SWS; (iii) irrevocably and unconditionally consents to the exchange of Oak Hill's outstanding warrants to acquire SWS common stock and Oak Hill's outstanding loans under the Credit Agreement for the following consideration: (a) the merger consideration that Oak Hill would have been entitled to receive upon consummation of the merger if its outstanding warrants had been exercised immediately prior to the effective time of the merger and (b) an amount equal to the Applicable Premium (as defined in the Credit Agreement, being a calculation of the present value of all required interest payments due on an outstanding loan through its maturity date on the date the loan is repaid) calculated as if the outstanding loans held by Oak Hill were prepaid in full as of the closing date of the merger; and (iv) covenants and agrees that Oak Hill shall not enter into any voting agreement or arrangement with Hilltop or any of its affiliates, grant any proxy to Hilltop or any of its affiliates or become party to any voting trust or other agreement, arrangement or understanding with Hilltop or any of its affiliates, in each case, with respect to the SWS common stock;

(b) that SWS will comply with its obligations under Section 1.7 of the merger agreement (which sets forth the treatment of Oak Hill's outstanding warrants and loans described in clause (a) above) on a timely basis and not amend Section 1.7 of the merger agreement in any manner or amend any other section of the merger agreement with the intent of amending Section 1.7; and

(c) that if SWS amends any other provision of the merger agreement in a manner that adversely affects Oak Hill (including without limitation any adverse change to the type or amount of merger consideration), without the prior written consent of Oak Hill, then Oak Hill will have the right to terminate the Oak Hill Letter Agreement.

The Oak Hill Letter Agreement does not preclude Oak Hill from granting a similar consent to any other transaction involving SWS that the Special Committee may recommend in the future. The Oak Hill Letter Agreement will terminate automatically if the merger agreement is terminated, if the merger is otherwise not consummated, or if the Special Committee withdraws or materially modifies its recommendation of the merger.

Litigation Relating to the Merger

Each of Hilltop, Peruna LLC, SWS and the individual members of the board of directors of SWS have been named as defendants in two purported shareholder class action lawsuits arising out of the merger. Both lawsuits were filed in Delaware Chancery Court (*Joseph Arceri v. SWS Group, Inc. et al* and *Chaile Steinberg v. SWS Group, Inc. et al* filed April 8, 2014 and April 11, 2014, respectively). On May 13, 2014, the Delaware Chancery Court consolidated the two actions for all purposes. On June 10, 2014, plaintiffs filed a consolidated amended complaint, a copy of which is attached to this proxy statement/prospectus as Annex D. The complaint generally alleges, among other things, that the SWS Board breached its fiduciary duties to stockholders by failing to take steps to maximize stockholder value or to engage in a fair sale process before approving the merger, that the SWS Board labored under conflicts of interest, that certain provisions of the merger agreement unduly restrict SWS's ability to negotiate with other potential bidders, and that the other defendants aided and abetted the SWS Board's breaches of fiduciary duty. The complaint further alleges, among other things, that the proxy statement/prospectus filed by Hilltop on May 29, 2014 omits or misstates certain material information. The complaints seek relief that includes, among other things, an injunction prohibiting the consummation of the merger, rescission to the extent the merger terms have already been implemented, damages for the alleged breaches of fiduciary duty, and the payment of plaintiffs' attorneys' fees and costs. On June 16, 2014, plaintiffs moved for a preliminary injunction prohibiting the consummation of the merger, and for expedited proceedings in connection therewith. Pursuant to negotiations between the parties to the lawsuit, plaintiffs subsequently withdrew those motions. Hilltop and SWS believe that the claims are without merit and each intends to vigorously defend against these actions.

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THE MERGER AGREEMENT

The following describes certain aspects of the merger, including certain material provisions of the merger agreement. The following description of the merger agreement is subject to, and qualified in its entirety by reference to, the merger agreement, which is attached to this proxy statement/prospectus as Annex A and is incorporated by reference into this proxy statement/prospectus. We urge you to read the merger agreement carefully and in its entirety, as it is the legal document governing the merger.

Structure of the Merger

The Merger

The merger agreement provides that SWS will merge into and with Peruna LLC, with Peruna LLC continuing as the surviving company and a wholly owned subsidiary of Hilltop. Subject to the terms of the merger agreement, each stockholder of SWS common stock issued and outstanding immediately prior to the completion of the merger will receive per share consideration consisting of $1.94 in cash and 0.2496 shares of Hilltop common stock, except for (i) certain shares of SWS common stock held by SWS or Hilltop and (ii) shares of SWS common stock held by stockholders properly asserting dissenters' rights at the completion of the merger.

The Bank Merger and the Broker-Dealer Merger

The merger agreement provides that immediately following the merger, Southwest Securities, FSB, a wholly-owned subsidiary of SWS, will merge with and into Hilltop's wholly-owned subsidiary PlainsCapital Bank, with PlainsCapital Bank continuing as the surviving bank (the "bank merger"). In addition, SWS has agreed to reasonably cooperate with Hilltop to obtain the necessary regulatory approvals to permit the merger of Hilltop's broker-dealer subsidiary First Southwest Company with Southwest Securities, Inc., a wholly-owned subsidiary of SWS, to be effected following the bank merger.

Fractional Shares

Hilltop will not issue any fractional shares of Hilltop common stock in the merger. Instead, an SWS stockholder who otherwise would have received a fraction of a share of Hilltop common stock will receive an equivalent amount in cash rounded to the nearest cent. The cash amount will be determined by multiplying (i) the average of the high and low sales prices of SWS common stock on the New York Stock Exchange, as reported on the New York Stock Exchange Composite Transaction Tape, on each of the five consecutive trading days ending on the trading day that is two trading days prior to the effective date of the merger, and (ii) the fraction of a share (after taking into account all shares of SWS common stock held by such stockholder at the effective date of the merger and rounded to the nearest thousandth when expressed in decimal form) of SWS common stock which such stockholder would otherwise be entitled to receive.

Surviving Company; Governing Documents; Directors and Officers

At the completion of the merger, the certificate of formation and limited liability company agreement of Peruna LLC in effect immediately prior to the effective time will be the certificate of formation and limited liability company agreement of the surviving company after completion of the merger until thereafter amended in accordance with their respective terms and applicable law.

At the completion of the merger, the directors of Peruna LLC immediately prior to the effective date shall become the initial directors of the surviving company and shall hold office until their respective successors are appointed.

Treatment of SWS Restricted Shares and Deferred Shares

Each restricted share of SWS common stock granted prior to the date of the merger agreement will vest in full at the effective time of the merger, and the holders of such restricted shares will be entitled to receive the merger consideration for each such share on the same basis as SWS stockholders generally, less applicable withholding taxes, which will be withheld first from the cash portion of the merger consideration payable in respect of each such share. As permitted under the terms of the merger agreement, on August 20, 2014, SWS granted additional restricted shares of SWS common stock to certain executive officers and key employees in satisfaction of their fiscal 2014 annual bonuses, which will be converted into restricted shares of Hilltop as of the effective time of the merger (with the number of Hilltop shares determined based on the value of the merger consideration), and will be subject to accelerated vesting (i) as to all of such restricted shares on termination of employment by the employer without "cause" (as defined in the merger agreement) following the effective time of the merger, (ii) as to all of such restricted shares upon a change of control event (other than the merger) and (iii) as to a prorated portion of such restricted shares on termination of employment due to an employee's death or disability. The merger agreement also permits SWS to grant, prior to the effective time of the merger, restricted shares of SWS common stock to non-employee directors of SWS in the ordinary course of business consistent with past practice with a grant date value not to exceed $35,000 per non-employee director.

As of the effective time of the merger, each deferred share of SWS common stock reflected in participant accounts under SWS deferred compensation plans will be converted into 0.3328 of a deferred share of Hilltop common stock (i.e., the sum of the portion of the merger consideration paid in Hilltop common stock and a number of shares of Hilltop common stock with a value as of immediately prior to the date of the merger agreement that is equal to the portion of the merger consideration paid in cash). Following the effective time of the merger, any such deferred shares that are not vested will continue to vest in accordance with the original terms of the SWS deferred shares and will vest in full on termination of employment by the employer without "cause" (as defined in the merger agreement) following the effective time of the merger. Hilltop deferred shares will be distributed in accordance with the terms of the applicable plan and the participants' individual elections.

For more information about these restricted and deferred shares, see "The Merger Interests of SWS Directors and Executive Officers in the Merger".

Treatment of Warrants

Concurrently with the execution of the merger agreement, Oak Hill and SWS entered into the Oak Hill Letter Agreement (see "The Merger Oak Hill Letter Agreement"). Pursuant to the Oak Hill Letter Agreement and the merger agreement, at the closing of the merger, Oak Hill will deliver to SWS the certificates evidencing its outstanding warrants and any loans of Oak Hill to SWS then outstanding under the Credit Agreement, and SWS will issue and deliver to Oak Hill, in exchange for its outstanding warrants and loans, the following consideration: (i) the merger consideration that Oak Hill would have been entitled to receive upon consummation of the merger if its outstanding warrants had been exercised immediately prior to the effective time of the merger and (ii) an amount equal to the Applicable Premium (as defined in the Credit Agreement, being a calculation of the present value of all required interest payments due on a loan through its maturity date on the date the loan is repaid) calculated as if the loans held by Oak Hill were prepaid in full as of the closing date of the merger.

Closing of the Merger

The merger shall become effective when the certificate of merger is accepted for filing by the Secretary of State of the State of Delaware in accordance with the DGCL. The completion of the merger will occur at 10:00 a.m. New York City time on a date no later than three business days after the satisfaction or waiver of the last of the conditions to the merger to be satisfied or waived, unless extended by mutual agreement of the parties. It is currently anticipated that the completion of the merger will occur by the end of 2014 subject to the receipt of SWS shareholder approval, regulatory approvals and other customary closing conditions, but neither Hilltop nor SWS can guarantee when or if the merger will be completed.

Hilltop Board of Directors Following Completion of the Merger

The Hilltop board of directors will not change pursuant to the merger agreement.

Conversion of Shares; Exchange of Certificates

The conversion of SWS common stock into the right to receive the merger consideration will occur automatically at the completion of the merger. Promptly after completion of the merger, the exchange agent (being a bank or trust company with certain responsibilities relating to distribution of the merger consideration) will exchange certificates or book-entry shares representing shares of SWS common stock for the merger consideration to be received pursuant to the terms of the merger agreement.

Letters of Transmittal

As soon as reasonably practicable after the completion of the merger, and in any event within five business days thereafter, the exchange agent will mail appropriate transmittal materials and instructions to those persons who were holders of SWS common stock immediately prior to the completion of the merger. These materials will contain instructions on how to surrender shares of SWS common stock, SWS common stock certificates and shares of SWS common stock held in book-entry form in exchange for the merger consideration such holders are entitled to receive under the merger agreement.

If a certificate for SWS common stock has been lost, stolen or destroyed, the exchange agent will issue the merger consideration upon receipt of (1) an affidavit of that fact by the claimant and (2) if reasonably required by Hilltop, such bond as Hilltop may determine is reasonably necessary as indemnity against any claim that may be made against Hilltop with respect to such lost, stolen or destroyed certificate.

After completion of the merger, there will be no further transfers on the stock transfer books of SWS other than to settle transfers of SWS common stock that occurred prior to the effective time of the merger.

Withholding

Hilltop and the exchange agent will be entitled to deduct and withhold from the consideration otherwise payable to any SWS stockholder the amounts Hilltop and the exchange agent are required to deduct and withhold under any applicable federal, state, local or foreign tax law. If any such amounts are withheld, these amounts will be treated for all purposes of the merger agreement as having been paid to the stockholders from whom they were withheld.

Dividends and Distributions

No dividends or other distributions declared with respect to Hilltop common stock will be paid to the holder of any unsurrendered certificates or book-entry shares of SWS common stock until the holder surrenders such certificate in accordance with the merger agreement. After the surrender of a certificate or book-entry share in accordance with the merger agreement, the record holder thereof will be entitled to receive (1) any such dividends or other distributions, without any interest, with a record date after the effective time and payable at that time with respect to the whole shares of Hilltop common stock represented by such certificate or book-entry share and paid prior to the date of surrender, or (2) at the appropriate payment date, the amount of dividends or other distributions payable with respect to shares of Hilltop common stock which the shares of SWS common stock represented by such certificate or book-entry share with a record date after the effective time of the merger but prior to the surrender date and with a payment date subsequent to the issuance of the Hilltop common stock issuable with respect to such SWS common stock.

Representations and Warranties

The representations, warranties and covenants described below and included in the merger agreement were made only for purposes of the merger agreement and as of specific dates, are solely for the benefit of Hilltop and SWS, may be subject to limitations, qualifications or exceptions agreed upon by the parties, including those included in confidential disclosures made for the purposes of, among other things, allocating contractual risk between Hilltop and SWS rather than establishing matters as facts, and may be subject to standards of materiality that differ from those standards relevant to investors. Investors should not rely on the representations, warranties, covenants or any description thereof as characterizations of the actual state of facts or condition of Hilltop, SWS or any of their respective subsidiaries or affiliates. Moreover, information concerning the subject matter of the representations, warranties and covenants may change after the date of the merger agreement, which subsequent information may or may not be fully reflected in public disclosures by Hilltop or SWS. The representations and warranties and other provisions of the merger agreement should not be read alone, but instead should be read only in conjunction with the information provided elsewhere in this proxy statement/prospectus and in the documents incorporated by reference into this proxy statement/prospectus.

The merger agreement contains customary representations and warranties of Hilltop and SWS relating to their respective businesses. The representations and warranties in the merger agreement do not survive the completion of the merger.

SWS has made representations and warranties regarding, among other things:

- corporate matters, including due organization and qualification of subsidiaries;
- capitalization;
- authority relative to execution and delivery of the merger agreement and the absence of conflicts with or violations of organizational documents or other obligations as a result of the merger;
- the accuracy of information supplied for inclusion in the proxy statement/prospectus and other similar documents;
- accurate regulatory reports and filings;
- financial statements and internal controls;
- real and personal property;
- tax matters;
- no material changes;

related-party matters;

litigation or legal proceedings;

- no undisclosed liabilities;
- compliance with applicable law;
- labor matters;
- employee benefits matters;
- risk management and derivatives matters;
- environmental matters;
- intellectual property matters;
- no undisclosed employment of brokers or finders;
- certain material contracts;
- compliance with applicable law and regulatory requirements relating to investment advisory services and broker-dealer services;
- loan matters;
- receipt of an opinion of its financial advisor;
- vote required;
- insurance matters;
- CRA Compliance; and
- title to investment securities.

Hilltop has made representations and warranties regarding, among other things:

- capitalization;

authority relative to execution and delivery of the merger agreement and the absence of conflicts with or violations of organizational documents or other obligations as a result of the merger;

accurate regulatory reports and filings;

the accuracy of information supplied for inclusion in this proxy statement/prospectus and other similar documents;

financial statements and internal controls;

tax matters;

the absence of certain changes or events;

litigation or legal proceedings;

no undisclosed liabilities;

compliance with applicable law;

no undisclosed employment of brokers or finders;

risk management and derivative matters;

no shareholder vote required;

absence of action, fact or circumstances that could reasonably be expected to prevent the merger from qualifying as a "reorganization" within the meaning of Section 368(a) of the Code;

- CRA Compliance;
- compliance with applicable law and regulatory requirements relating to investment advisory services and broker-dealer services; and
- sufficient financing for the completion of the merger.

Certain representations and warranties of Hilltop and SWS are qualified as to "materiality" or "material adverse effect." For purposes of the merger agreement, a "material adverse effect" means, with respect to either party, any occurrence, event, development, effect, change or condition that has had, or would reasonably be expected to have, individually or in the aggregate, a material adverse effect on the business, results of operations or financial condition of it and its subsidiaries, taken as a whole. However, the following shall not be considered when determining whether a material adverse effect has occurred:

- changes in (i) GAAP or interpretations thereof, (ii) laws, rules or regulations of general applicability to companies in any of the industries in which a party operates (including the adoption or repeal of any such laws, rules or regulations), (iii) global, national or regional political conditions or economic or market conditions generally (including changes in prevailing interest rates, credit availability and liquidity, currency exchange rates, and price levels or trading volumes in the United States or foreign securities markets) or (iv) the credit markets or adverse credit events resulting in deterioration in the credit markets generally and including changes to any previously correctly applied asset marks, except in the case of each of clauses (i)-(iv), to the extent that the effects of such change are materially disproportionately adverse to the financial condition, results of operations or business of a party as compared to other companies in the industries in which it operates;
- decline in the trading price of a party's common stock or a failure to meet earnings or projections in respect of revenues, earnings or other financial or operating metrics for any period, but not including the underlying causes thereof;
- execution and delivery of the merger agreement, the public announcement of the merger agreement or the merger, the taking of any action required by the merger agreement, or the identity of, or any facts or circumstances relating to any other party to the merger agreement, including the impact thereof on relationships with customers, providers, suppliers, partners, officers or employees (including departures of employees);
- acts of war, sabotage, terrorism or military actions, earthquakes, floods, hurricanes, tornadoes, natural disasters or other "acts of God" or any changes in conditions generally affecting any industry in which a party operates, except in each such event to the extent that the effects are materially disproportionately adverse to the financial condition, results of operations or business of a party as compared to other companies in the industries in which it operates;
- any litigation or legal proceedings arising from or allegations of a breach of fiduciary duty or violation of applicable law relating to the merger; or
- actions or omissions taken with the other party's prior written consent or expressly required by the merger agreement.

Covenants and Agreements

Conduct of Business Prior to the Completion of the Merger

SWS has agreed that, prior to the completion of the merger, it will, and will cause each of its subsidiaries to, conduct its business in the ordinary course consistent with past practice in all material respects and use commercially reasonable efforts to maintain and preserve intact its business

organization and advantageous business relationships. SWS and Hilltop agree to, and to cause each of their respective subsidiaries to, take no action that is intended to or would reasonably be expected to adversely affect or materially delay the ability of either SWS, Peruna LLC or Hilltop to obtain any necessary approvals of any regulatory agency or other governmental entity required for the transactions contemplated by the merger agreement or to perform their covenants and agreements under the merger agreement.

Additionally, SWS has agreed that prior to the completion of the merger, except as disclosed to Hilltop prior to the date of the merger agreement, and except as required by the merger agreement, required by applicable law or with the prior written consent of Hilltop, SWS will not, and will not permit any of its subsidiaries to, subject to certain exceptions, undertake certain actions, including the following:

- issue, sell, dispose of, authorize, pledge or encumber or pledge any shares of its capital stock or securities convertible into, or exchangeable for, additional shares of capital stock or other equity interests, except for issuances under dividend reinvestment plans in the ordinary course of business or automatic grants pursuant to existing SWS stock plans;

- adjust, split, combine or reclassify any capital stock or make, declare or pay any dividends or other distributions on any shares of its capital stock;

- amend the material terms of, knowingly and materially violate the terms of, waive any material rights under, or terminate any material contract, regulatory agreement or other binding obligation that is material to SWS and its subsidiaries, taken as a whole;

- sell, transfer, mortgage, encumber or otherwise dispose of any of its properties, deposits, businesses or assets other than in the ordinary course of business and in transactions that are not material to SWS and its subsidiaries, taken as a whole;

- acquire all or any portion of the assets, business, deposits or properties of any other entity, except in the ordinary course of business and in a transaction that is not material to SWS and its subsidiaries, taken as a whole, and would not reasonably be expected to present a material risk that the closing of the merger will be materially delayed or that any regulatory approval required to consummate the merger will be more difficult to obtain;

- amend the certificate of incorporation, bylaws or similar governing documents of SWS or any subsidiary of SWS;

- implement or adopt any change in its accounting principles, practices or methods, other than as may be required by GAAP or applicable regulatory accounting requirements;

- except as required under applicable law or the terms of any employee benefit plan in effect as of the date of the merger agreement, (i) increase the compensation, severance or benefits of any of the current or former directors, officers, employees or consultants of SWS or its subsidiaries, other than annual increases in base salary or benefits for employees who are not executive officers of SWS or its subsidiaries in the ordinary course of business consistent with past practice and subject to certain limits, (ii) pay or award, or commit to pay or award, any bonuses or incentive compensation subject to certain exceptions with respect to executive officer and employee bonuses for the 2014 and 2015 fiscal years, (iii) become a party to, establish, amend or terminate any material employee benefit plan, (iv) accelerate the vesting of or lapsing of restrictions with respect to any compensation, benefits, stock-based compensation, incentive compensation or the forgiveness of indebtedness of any loan, (v) fund any rabbi trust or similar arrangement or (vi) hire (other than to replace terminated employees) or terminate without cause the employment of any employee with base compensation of $150,000 or more;

subject to certain exceptions, permit or allow the securities inventory of taxable fixed income or municipal distribution to exceed or deviate from the parameters set forth in, and the terms of, policies;

incur or guarantee any indebtedness for borrowed money, other than in the ordinary course of business;

enter into any new line of business or materially change its lending, investment, underwriting, risk and asset liability management and other banking and operating policies, except as required by law or requested by a regulatory agency;

other than in consultation with Hilltop, make any material change to (i) its investment securities portfolio, derivatives portfolio or its interest rate exposure, through purchases, sales or otherwise, or (ii) the manner in which the portfolio is classified or reported, except as required by law or requested by a regulatory agency;

settle any action, suit, claim or proceeding against it or any of its subsidiaries, except for an action, suit, claim or proceeding that is settled in an amount and for consideration not in excess of $250,000 and that would not impose any material restriction on the business of it or its subsidiaries;

alter materially its interest rate or pricing fee or fee pricing policies with respect to stock lending and borrowing, margin loans, money market funds or bank insured depository accounts or waive any material fees with respect thereto;

make any material changes in its policies and practices with respect to (i) underwriting, pricing, originating, acquiring, selling, servicing, or buying or selling rights to service, loans, or (ii) its hedging practices and policies, in each case except as required by law or requested by a regulatory agency;

foreclose upon or take a deed or title to any real estate other than single-family residential properties without first conducting a Phase I environmental assessment of the property that satisfies the requirements of the all appropriate inquiries standard of CERCLA § 101(35), 42 U.S.C. § 9601(35) (except where such an assessment has been conducted in the preceding twelve months) or foreclose upon or take a deed or title to any such real estate if such environmental assessment indicates the presence of hazardous materials or other materials regulated under environmental laws in or at such real estate due to a release to the environment of such hazardous or regulated materials which presence is likely to lead to a material liability;

subject to certain exceptions, invest in any mortgage-backed or mortgage related securities that would be considered "high-risk" securities under applicable regulatory pronouncements;

subject to certain exceptions, (i) make or acquire any loan or issue a commitment for any loan, or amend or modify in any material respect any existing loan, that would result in total credit exposure to the applicable borrower in excess of $5,000,000, (ii) amend or modify in any material respect any existing special mention loan with total credit exposure to the applicable borrower and its affiliates in excess of $3,000,000, (iii) enter into agreements relating to, or consummate purchases or sales of, whole loans or pool loans in excess of $2,000,000 in principal amount or purchase price or (iv) sell or otherwise dispose of any loan or OREO that would have a loss in excess of $500,000;

make application for the opening, relocation or closing of any, or open, relocate or close any, branch office, loan production office or other material office or operations facility;

subject to certain exceptions, pay, loan or advance any amount to, or sell, transfer or lease any properties, rights or assets to, or enter into any arrangement or agreement with, any of its

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- officers or directors or any of their family members, or any affiliates or associates of any of its officers or directors, other than loans originated in the ordinary course of business and, in the case of any such arrangements or agreements relating to compensation, fringe benefits, severance or termination pay or related matters;

- make, change or revoke any material tax election, change or consent to any change in it or its subsidiaries' method of accounting for tax purposes (except as required by applicable tax law), take any material position on any material tax return filed on or after the date of the agreement, settle any material tax liability, claim or assessment, enter into any closing agreement, waive or extend any statute of limitations with respect to a material amount of taxes, surrender any right to claim a refund for a material amount of taxes or file any material amended tax return;

- take, or fail to take, any action that would prevent or impede, or could reasonably be expected to prevent or impede, the merger from qualifying as a "reorganization" within the meaning of Section 368(a) of the Code; or

- agree to take, make any commitment to take, or adopt any resolutions of its board of directors prohibited by the Company forbearances.

Hilltop has agreed that prior to the completion of the merger, except as disclosed to SWS prior to the date of the merger agreement, and except as expressly permitted by the merger agreement or with the prior consent of SWS, Hilltop will not, and will not permit any of its subsidiaries to, subject to certain exceptions, undertake the following actions:

- adopt or propose any amendments to its organizational documents;

- take, or fail to take, any action that would, or is reasonably likely to, prevent or impede the merger from qualifying as a "reorganization" within the meaning of Section 368(a) of the Code;

- adopt or propose to adopt a plan of complete or partial liquidation or dissolution of Purchaser;

- (i) make, declare, pay or set aside for payment any dividend payable in cash, capital stock or other property on or in respect of, or declare or make any distribution on any shares of its capital stock or (ii) directly or indirectly adjust, split, combine, redeem, reclassify, purchase or otherwise acquire, any shares of its capital stock; or

- agree to take, make any commitment to take, or adopt any resolutions of its board of directors in support of, any of the actions prohibited by the merger agreement.

Regulatory Matters

Hilltop and SWS have agreed to cooperate with each other and use their respective reasonable best efforts to promptly prepare and file all necessary documentation (including applications for approval from the Federal Reserve Board and the Texas Department of Banking and, if applicable, notification under the HSR Act), to effect all applications, notices, petitions and filings, and to consult with each other with respect to obtaining, and to obtain as promptly as practicable, all permits, consents, approvals and authorizations of all third parties and governmental entities that are necessary or advisable to consummate the merger, the bank merger and the other transactions contemplated by the merger agreement. Hilltop and SWS will use their respective reasonable best efforts to resolve any objections that may be asserted by any regulatory authority with respect to the merger agreement, the merger, the bank merger or the transactions contemplated by the merger agreement and will consult with the other party in advance of any meeting or conference with any governmental entity. Hilltop will not be required to take or commit to take any actions that would reasonably be expected to have a material adverse effect (measured on a scale relative to SWS) on Hilltop or SWS (referred to as a "materially burdensome regulatory condition"), and SWS shall not be required to take or commit to take any such action unless such actions are conditioned on the closing of the merger.

Employee Matters

The merger agreement provides that Hilltop will provide or cause to be provided to each employee who is employed by SWS or any of its subsidiaries on the closing date, during the period in which such employee is employed by Hilltop or any of its affiliates following the closing date, commencing on the closing date and ending on:

- the six-month anniversary of the closing date, a base salary that is not less than the base salary provided to such employee as of immediately prior to the closing date; and

- December 31, 2015, (i) bonus opportunities and employee benefits that, in the aggregate, are no less favorable than the bonus opportunities and employee benefits provided to similarly situated employees of Hilltop and its subsidiaries (other than SWS and its subsidiaries) and (ii) severance benefits that are no less favorable than those described in the merger agreement.

Director and Officer Indemnification and Insurance

Each of Hilltop and Peruna LLC has agreed to indemnify and advance expenses to each present and former director and officer of SWS and its subsidiaries (when acting in such capacity) to the fullest extent permitted by law for any acts arising out of or pertaining to matters occurring at or existing prior to the closing. Additionally, Hilltop will provide director and officer liability insurance with respect to claims arising from facts or events occurring before the completion of the merger, which will contain at least the same coverage and amounts, and on no less advantageous terms to the indemnified party as that coverage currently provided by SWS, at an aggregate cost per annum not to exceed 300% of the annual aggregate premiums currently paid by SWS for such insurance, provided that if premiums for such insurance would exceed such cap, then Hilltop will maintain policies of insurance which provide the maximum coverage available at an annual premium equal to such cap. In lieu of the foregoing insurance, prior to the closing, SWS may purchase "tail" D&O insurance, at an aggregate cost not to exceed 300% of the annual aggregate premiums currently paid by it for such insurance.

Voting of Shares Owned by Hilltop

Hilltop has agreed in the merger agreement to vote any shares of SWS that it owns as of the record date for the SWS special meeting (not including unissued shares that would be issuable upon the exercise of all or a portion of Hilltop's warrant) in favor of approval and adoption of the merger agreement.

Certain Additional Agreements

The merger agreement also contains additional covenants, including covenants relating to the filing of this proxy statement/prospectus, obtaining required consents, the listing of the shares of Hilltop common stock to be issued in the merger, access to information of the other company and public announcements with respect to the transactions contemplated by the merger agreement.

No Solicitation

SWS agreed in the merger agreement that it shall not, and shall cause its subsidiaries not to, and shall use its reasonable best efforts to cause its or their respective officers, directors, employees, representatives or agents not to (a) knowingly encourage, solicit, participate in, knowingly facilitate or initiate discussions, negotiations, inquiries, proposals or offers with or provide any non-public information to, any person relating to any third party acquisition (as defined below) or any inquiry, proposal or offer reasonably likely to lead to a third party acquisition or (b) waive, terminate, modify or fail to enforce any provision of any contractual "standstill" or similar obligation of any person other than Hilltop and Peruna LLC; provided, that prior to SWS stockholder approval of the merger, if SWS receives a bona fide unsolicited written proposal for a third party acquisition that the SWS board of directors determines in its good faith judgment is or could reasonably be expected to result in a superior proposal and was made after the date of the merger agreement, then the SWS board of directors may provide information to and enter into discussions with such third party, but only if (i) in the case of provision of information, prior to such provision of information such third party shall have entered into a confidentiality agreement with terms no less favorable to SWS than those contained in SWS's confidentiality agreement with Hilltop and any non-public information provided to such third party shall have been previously provided to Hilltop or shall be provided to Hilltop prior to or concurrently with being provided to such third party and (ii) the SWS board of directors determines in its good faith judgment, after consultation with and based upon the advice of outside legal counsel, that the failure to take such action would be reasonably likely to be inconsistent with its fiduciary duties under applicable law.

SWS has agreed to notify Hilltop within 24 hours of the receipt of a proposal for a third party acquisition. The notice must indicate the person making the proposal along with the material terms of the proposal and a copy of any written documentation. SWS will keep Hilltop fully informed, on a timely basis, of any material developments with respect to such proposal.

For purposes of the merger agreement:

"third party acquisition" means: (i) the acquisition, in one or a series of related transactions, of SWS or any of its subsidiaries representing more than 15% of the consolidated total assets of SWS taken as a whole, by merger, tender offer, exchange offer, consolidation, business combination or otherwise by any third party other than Hilltop or an affiliate of Hilltop (a "third party"), (ii) the acquisition by a third party in any one or a series of transactions of assets or businesses of SWS, including pursuant to a joint venture or partnership, representing more than 15% of the consolidated total assets of SWS or (iii) the acquisition by a third party in one or a series of related transactions in any manner of beneficial ownership of 15% or more of the outstanding shares of SWS common stock or any other class of capital stock or voting power of SWS.

"superior proposal" means any bona fide unsolicited written proposal for a third party acquisition (with the references to "15%" in the definition thereof replaced with references to "100%") that the SWS board of directors determines in its good faith judgment (after consulting its financial advisor) and taking into account all relevant factors, (i) is more favorable to the SWS stockholders (other than Hilltop) from a financial point of view than the transactions contemplated by the merger agreement (taking into account any adjustment to the terms and conditions proposed by Hilltop in a counteroffer and taking into account any break-up fees and expense reimbursement provisions) and (ii) is reasonably likely to be completed on the terms proposed.

Change in Recommendation

The board of directors of SWS has agreed to recommend in favor of the proposals related to the merger and the transactions contemplated by the merger agreement; provided if the SWS board of directors determines in its good faith judgment, after consultation with and based upon the advice of outside legal counsel, that, because of (i) the receipt of a written proposal for a third party acquisition that it determines in good faith constitutes a superior proposal or (ii) the occurrence of an intervening event (as defined below), the failure to take such action would be reasonably likely to be inconsistent with its fiduciary duties under applicable law (after taking into account all counteroffers proposed by Hilltop) the SWS board of directors may make a change in its recommendation in favor of the merger and, in the event of a superior proposal, recommend a superior proposal but only (i) after the fifth business day following Hilltop's receipt of written notice from SWS advising Hilltop that the SWS board of directors has received a superior proposal or that an intervening event has occurred, specifying, as applicable, (A) the terms and conditions of such superior proposal and identifying the person making it or (B) the nature of such intervening event in reasonable detail. During such five business day period, SWS must negotiate with Hilltop in good faith regarding adjustments to the merger agreement that would obviate the need for the SWS board of directors to change its recommendation in favor of the merger. Notwithstanding any change in its recommendation, SWS shall submit the merger agreement to the SWS shareholders at the SWS shareholder meeting and SWS may not enter into any alternative acquisition agreement until the SWS stockholder meeting has been held, the merger agreement has been terminated in accordance with its terms and any applicable termination fee has been paid to Hilltop.

If, on the date of the SWS shareholder meeting, Hilltop reasonably determines in good faith that SWS has not received sufficient proxies to obtain shareholder approval of the merger proposal, Hilltop may require SWS to adjourn the meeting until such date as shall be mutually agreed upon by SWS and Hilltop, which date shall be not less than five days nor more than ten days after the date of adjournment. SWS is only required to adjourn the SWS shareholder meeting one time.

An "intervening event" is any event, change, effect, development or occurrence occurring or arising after the date of the merger agreement that (i) was not known, or reasonably foreseeable, to the Board of Directors of SWS as of or prior to the date of the merger agreement and did not result from a breach of the merger agreement by SWS and (ii) does not relate to or involve a third party acquisition.

Conditions to Completion of the Merger

Hilltop and SWS's respective obligations to complete the merger are subject to the satisfaction or waiver of the following conditions:

- approval of the merger proposal by SWS stockholders;
- authorization for listing on the NYSE of the shares of Hilltop common stock to be issued in the merger;
- effectiveness of the registration statement of which this proxy/prospectus forms a part, and the absence of any stop order or proceedings seeking a stop order or initiation or threat of such proceedings by the SEC;
- the absence of any order, injunction or decree issued by any court or agency with competent jurisdiction, or other law, preventing the consummation of the merger or bank merger that has been issued and is in effect;
- receipt of necessary regulatory approvals from the Federal Reserve and the Texas Department of Banking and, if applicable, the expiration or termination of the waiting period under the HSR Act;
- subject to certain exceptions and materiality thresholds, accuracy of the other party's representations and warranties when made and at the effective time of the merger (except to the extent expressly made as of an earlier date, in which case as of such date) (and the receipt by each party of an officer's certificate from the other party to such effect);
- performance by the other party of its obligations under the merger agreement in all material respects (and the receipt by each party of an officer's certificate from the other party to such effect); and
- the receipt of a tax opinion from its legal counsel to the effect that the merger will qualify as a "reorganization" within the meaning of Section 368(a) of the Code.

Hilltop's obligation to complete the merger is further conditioned on:

- the fact that there shall not be any action taken or determination made, or any law enacted, entered, enforced or deemed applicable to the transactions contemplated by the merger or bank merger, by any governmental entity, in connection with the grant of a requisite regulatory approval, which imposes, contains or would result in the imposition of a materially burdensome regulatory condition.

Termination of the Merger Agreement

The merger agreement can be terminated at any time prior to the completion of the merger (i) by mutual consent, (ii) by Hilltop if (A) at any time prior to obtaining the SWS shareholder approval, the SWS board of directors has changed its recommendation in favor of the merger, (B) at any time prior to obtaining the SWS shareholder approval, SWS is in material breach of its non-solicitation obligations or its obligations regarding soliciting stockholder approval for the merger or (C) if any governmental entity that must grant a requisite regulatory approval imposes a materially burdensome regulatory condition and there is no meaningful possibility such condition can be revised prior to March 31, 2015 unless the failure to obtain such approval without a materially burdensome regulatory condition is due to any breach by Hilltop of the merger agreement or (iii) by either party in the following circumstances:

- a governmental entity that must grant a required regulatory approval has denied approval and such denial has become final or an injunction or legal prohibition against the transaction becomes final and nonappealable;

- the merger has not been consummated by March 31, 2015 unless the failure of the merger to be completed by such date is due to the failure of the party seeking to terminate the merger agreement to perform or observe its covenants and agreements under the merger agreement;

- the other party breaches any of its covenants or agreements under the merger agreement in a manner that would cause the closing conditions not to be satisfied and that is not within 30 days following written notice of the breach (provided that the terminating party is not also in material breach of any of its obligations under the merger agreement); or

- the special meeting of the SWS stockholders shall have concluded without the approval of the merger proposal.

Termination Fee

SWS is required to pay Hilltop a termination fee of $8 million if:

(i) a third party proposal has been publicly disclosed or made known to SWS management and not withdrawn, or any person has publicly announced or made known to SWS management and not withdrawn at least 10 business days' prior to the stockholder vote an intention to make a third party proposal, and thereafter the agreement is terminated:

  - by either Hilltop or SWS because the merger has not been consummated by March 31, 2015 (without SWS stockholder approval of the merger proposal having been obtained) or because the SWS stockholders failed to approve the merger proposal at a meeting called for such purpose; or

  - by Hilltop for SWS's willful breach of any of its covenants or agreements under the merger agreement, which breach would cause certain closing conditions not to be satisfied and which is not cured during the applicable cure period;

and, within 12 months of termination SWS consummates a third party acquisition or enters into an agreement in respect thereof (provided that the references to "15%" in the definition of third party acquisition shall be replaced with references to "50%" for this purpose); or

(ii) the merger agreement is terminated by Hilltop prior to the time SWS stockholders have approved the merger proposal because SWS or the board of directors of SWS changes its recommendation in favor of the merger, or SWS is in material breach of its non-solicitation obligations or its obligations regarding soliciting stockholder approval of the merger.

Effect of Termination

If the merger agreement is terminated, it will become void, and no directors or officers of Hilltop or SWS shall have any liability under the agreement, except that (i) each of Hilltop and SWS will remain liable for any willful breach of the merger agreement and (ii) designated provisions of the merger agreement will survive the termination, including those relating to payments of fees and expenses and the confidential treatment of information.

Expenses and Fees

All fees and expenses incurred in connection with the merger shall be paid by the party incurring such fees or expenses, whether or not the merger is consummated.

Amendment, Waiver and Extension of the Merger Agreement

Subject to applicable law, Hilltop and SWS may amend the merger agreement by action by their respective boards of directors (and, in the case of SWS, the Special Committee). However, after approval of the merger agreement by SWS stockholders, there may not be, without further approval of SWS stockholders, any amendment of the merger agreement that requires further approval under applicable law.

At any time prior to the completion of the merger, each party, to the extent legally allowed, may by action of its board of directors (and in the case of SWS, the Special Committee) extend the time for the performance of any of the obligations or other acts of the other party; waive any inaccuracies in the representations and warranties of the other party; and waive compliance by the other party with any of the agreements and conditions contained in the merger agreement except that after approval of the merger agreement by the SWS stockholders, there may not be, without further approval of such stockholders, any extension or waiver of the merger agreement or any portion thereof that reduces the amount or changes the form of the consideration to be delivered to the holders of SWS common stock or that otherwise requires further approval under applicable law.

ACCOUNTING TREATMENT OF THE MERGER

The merger will be accounted for as a "purchase," as that term is used under generally accepted accounting principles, for accounting and financial reporting purposes. Under purchase accounting, the assets (including identifiable intangible assets) and liabilities (including executory contracts and other commitments) of SWS as of the effective time of the merger will be recorded at their respective fair values and added to those of Hilltop. Any excess of purchase price over the aggregate of the fair values is recorded as goodwill. Consolidated financial statements of Hilltop issued after the merger would reflect these fair values and would not be restated retroactively to reflect the historical consolidated financial position or results of operations of SWS.

UNITED STATES FEDERAL INCOME TAX CONSEQUENCES OF THE MERGER

The following general discussion addresses the material United States federal income tax consequences of the merger to U.S. holders (as defined below) of SWS common stock that exchange their shares of SWS common stock for shares of Hilltop common stock and cash in the merger. This discussion does not address any tax consequences arising under the laws of any state, local or foreign jurisdiction, or under any United States federal laws other than those pertaining to income tax. This discussion is based upon the Code, the regulations promulgated under the Code and court and administrative rulings and decisions, all as in effect on the date of this proxy statement/prospectus. These laws may change, possibly retroactively, and any change could affect the accuracy of the statements and conclusions set forth in this discussion.

This discussion addresses only those holders of SWS common stock that hold their shares of SWS common stock as capital assets within the meaning of Section 1221 of the Code (generally, property held for investment). Further, this discussion does not address all aspects of United States federal income taxation that may be relevant to you in light of your particular circumstances or that may be applicable to you if you are subject to special treatment under the United States federal income tax laws, including if you are:

- a financial institution;
- a tax-exempt organization;
- an S corporation or other pass-through entity (or an investor in an S corporation or other pass-through entity);
- an insurance company;
- a mutual fund;
- a dealer or broker in stocks and securities, or currencies;
- a trader in securities that elects mark-to-market treatment;
- a holder of SWS common stock that received SWS common stock through the exercise of an employee stock option, through a tax qualified retirement plan or otherwise as compensation;
- a person that is not a U.S. holder (as defined below);
- a person that has a functional currency other than the U.S. dollar;
- a holder of SWS common stock that holds SWS common stock as part of a hedge, straddle, constructive sale, conversion or other integrated transaction; or
- a United States expatriate.

In addition, the discussion does not address any alternative minimum tax or any state, local or foreign tax consequences of the merger, nor does it address any tax consequences arising under the unearned income Medicare contribution tax pursuant to the Health Care and Education Reconciliation Act of 2010. Determining the actual tax consequences of the merger to you may be complex. They will depend on your specific situation and on factors that are not within the control of SWS or Hilltop. You should consult with your own tax advisor as to the tax consequences of the merger in your particular circumstances.

For purposes of this discussion, the term "U.S. holder" means a beneficial owner of SWS common stock that is for United States federal income tax purposes (i) an individual citizen or resident of the United States, (ii) a corporation, or entity treated as a corporation, organized in or under the laws of the United States or any state thereof or the District of Columbia, (iii) a trust if (a) a court within the United States is able to exercise primary supervision over the administration of the trust and one or more U.S. persons have the authority to control all substantial decisions of the trust or (b) such trust has made a valid election to be treated as a U.S. person for U.S. federal income tax purposes or (iv) an estate, the income of which is includible in gross income for U.S. federal income tax purposes regardless of its source.

The United States federal income tax consequences to a partner in an entity or arrangement that is treated as a partnership for United States federal income tax purposes and that holds SWS common stock generally will depend on the status of the partner and the activities of the partnership. Partners in a partnership holding SWS common stock should consult their own tax advisors.

Tax Consequences of the Merger Generally

The parties intend for the merger to qualify as a "reorganization" within the meaning of Section 368(a) of the Code. It is a condition to Hilltop's obligation to complete the merger that Hilltop receive an opinion from Wachtell, Lipton, Rosen & Katz ("Wachtell Lipton"), dated the closing date of the merger, to the effect that the merger will qualify as a "reorganization" within the meaning of Section 368(a) of the Code. It is a condition to SWS's obligation to complete the merger that SWS receive an opinion from Davis Polk & Wardwell LLP ("Davis Polk"), dated the closing date of the merger, to the effect that the merger will qualify as a "reorganization" within the meaning of Section 368(a) of the Code. These opinions will be based on representation letters provided by Hilltop and SWS and on customary factual assumptions. Neither of the opinions described above will be binding on the Internal Revenue Service. Hilltop and SWS have not sought and will not seek any ruling from the Internal Revenue Service regarding any matters relating to the merger, and as a result, there can be no assurance that the Internal Revenue Service will not assert, or that a court would not sustain, a position contrary to any of the conclusions set forth below.

In addition, in connection with the effectiveness of the registration statement of which this proxy statement/prospectus forms a part, each of Wachtell Lipton and Davis Polk has delivered its opinion to the effect that, on the basis of the facts, representations, assumptions and exclusions set forth in such opinion and certificates obtained from officers of Hilltop and SWS, (i) the merger will qualify as a "reorganization" within the meaning of Section 368(a) of the Code and (ii) the following discussion constitutes their opinion as to the material U.S. federal income tax consequences of the merger to holders of SWS common stock. Neither of these opinions is binding on the Internal Revenue Service or the courts, and neither Hilltop nor SWS intends to request a ruling from the Internal Revenue Service regarding the United States federal income tax consequences of the merger. Consequently, no assurance can be given that the Internal Revenue Service will not assert, or that a court would not sustain, a position contrary to any of those set forth below. In addition, if any of the representations or assumptions upon which such opinions are based are inconsistent with the actual facts, the United States federal income tax consequences of the merger could be adversely affected.

In general, the merger is intended to be tax-free to you, except to the extent of any cash that you receive in exchange for your shares of SWS common stock. Upon exchanging your SWS common stock for Hilltop common stock and cash (other than cash received in lieu of a fractional share), you generally will recognize gain (but not loss) in an amount equal to the lesser of (1) the amount of gain realized (i.e., the excess of the sum of the amount of cash and the fair market value of the Hilltop common stock received pursuant to the merger over your adjusted tax basis in your shares of SWS common stock surrendered) and (2) the amount of cash received pursuant to the merger (excluding any cash received in lieu of a fractional share). If you acquired different blocks of SWS common stock at different times or different prices, you should consult your tax advisor regarding the manner in which gain or loss should be determined. Any recognized gain generally will be long-term capital gain if, as of the effective date of the merger, your holding period with respect to the SWS common stock surrendered exceeds one year. If, however, the cash received has the effect of the distribution of a dividend as described below, the gain will be treated as a dividend to the extent of your ratable share of Hilltop's accumulated earnings and profits as calculated for United States federal income tax purposes. See " Possible Treatment of Cash as a Dividend" below.

The aggregate tax basis in the shares of Hilltop common stock that you receive in the merger, including any fractional share interests deemed received and sold as described below, will equal your aggregate adjusted tax basis in the SWS common stock you surrender, reduced by the amount of cash received (excluding any cash received in lieu of a fractional share) and increased by the amount of gain, if any, recognized by you (excluding any gain recognized with respect to cash received in lieu of a fractional share) on the exchange. Your holding period for the shares of Hilltop common stock that you receive in the merger (including a fractional share interest deemed received and sold as described below) will include your holding period for the shares of SWS common stock that you surrender in the exchange.

Possible Treatment of Cash as a Dividend

In general, the determination of whether the gain recognized in the exchange will be treated as capital gain or has the effect of a distribution of a dividend depends upon whether and to what extent the exchange reduces your deemed percentage stock ownership of Hilltop. For purposes of this determination, you are treated as if you first exchanged all of your shares of SWS common stock solely for Hilltop common stock and then Hilltop immediately redeemed, which we refer to in this document as the "deemed redemption," a portion of the Hilltop common stock in exchange for the cash you actually received. The gain recognized in the deemed redemption will be treated as capital gain if the deemed redemption is (1) "substantially disproportionate" with respect to you or (2) "not essentially equivalent to a dividend."

The deemed redemption will generally be "substantially disproportionate" with respect to you if the percentage described in (2) below is less than 80% of the percentage described in (1) below. Whether the deemed redemption is "not essentially equivalent to a dividend" with respect to you will depend upon your particular circumstances. At a minimum, however, in order for the deemed redemption to be "not essentially equivalent to a dividend," the deemed redemption must result in a "meaningful reduction" in your deemed percentage stock ownership of Hilltop. In general, that determination requires a comparison of (1) the percentage of the outstanding stock of Hilltop that you are deemed actually and constructively to have owned immediately before the deemed redemption and (2) the percentage of the outstanding stock of Hilltop that is actually and constructively owned by you immediately after the deemed redemption. In applying the above tests, you may, under the constructive ownership rules, be deemed to own stock that is owned by other persons or stock underlying any option you hold to purchase stock in addition to the stock actually owned by you.

The Internal Revenue Service has ruled that a stockholder in a publicly held corporation whose relative stock interest is minimal (e.g., less than 1%) and who exercises no control with respect to corporate affairs is generally considered to have a "meaningful reduction" if that stockholder has a relatively minor (e.g., approximately 3%) reduction in its percentage stock ownership under the above analysis; accordingly, the gain recognized in the exchange by such a stockholder would be treated as capital gain.

These rules are complex and dependent upon the specific factual circumstances particular to you. Consequently, you should consult your tax advisor as to the application of these rules to the particular facts relevant to you.

Cash Instead of a Fractional Share

If you receive cash instead of a fractional share of Hilltop common stock, you will be treated as having received the fractional share of Hilltop common stock pursuant to the merger and then as having sold that fractional share of Hilltop common stock for cash. As a result, you generally will

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recognize gain or loss equal to the difference between the amount of cash received and the basis allocable to your fractional share of Hilltop common stock. This gain or loss generally will be capital gain or loss, and will be long-term capital gain or loss if, as of the effective date of the merger, the holding period for the shares (including the holding period of SWS common stock surrendered therefor) is greater than one year. The deductibility of capital losses is subject to limitations.

Backup Withholding

If you are a non-corporate holder of SWS common stock you may be subject to information reporting and backup withholding (currently at a rate of 28%) on any cash payments you receive. You generally will not be subject to backup withholding, however, if you:

- furnish a correct taxpayer identification number, certify that you are not subject to backup withholding on the substitute Form W-9 or successor form included in the letter of transmittal you will receive and otherwise comply with all the applicable requirements of the backup withholding rules; or

- provide proof that you are otherwise exempt from backup withholding.

Any amounts withheld under the backup withholding rules will generally be allowed as a refund or credit against your United States federal income tax liability, provided you timely furnish the required information to the Internal Revenue Service.

This discussion of certain material United States federal income tax consequences is for general information only and is not tax advice. You are urged to consult your tax advisor with respect to the application of United States federal income tax laws to your particular situation as well as any tax consequences arising under the United States federal estate or gift tax rules, or under the laws of any state, local, foreign or other taxing jurisdiction.

DESCRIPTION OF HILLTOP CAPITAL STOCK

As a result of the merger, SWS stockholders who receive shares of Hilltop common stock in the merger will become shareholders of Hilltop. Your rights as shareholders of Hilltop will be governed by Maryland law and the charter and bylaws of Hilltop. The following briefly summarizes the material terms of Hilltop common stock and preferred stock. We urge you to read provisions of the Maryland General Corporate Law (which we refer to as the MGCL), Hilltop's charter and bylaws and federal law governing bank holding companies carefully in their entirety. Copies of Hilltop's governing documents have been filed with the SEC. To find out where copies of these documents can be obtained, see "Where You Can Find More Information".

Authorized Capital Stock

Hilltop's authorized capital stock consists of 125,000,000 shares of common stock, par value $0.01 per share, 10,000,000 shares of special voting stock, par value $0.01 per share, and 10,000,000 shares of preferred stock, par value $0.01 per share. As of October 13, 2014, there were 90,182,915 shares of Hilltop common stock outstanding, zero shares of special voting stock outstanding and 114,068 shares of Hilltop Series B preferred stock outstanding.

Common Stock

Preemptive Rights

Hilltop common stock has no preemptive rights.

Dividend Rights

Hilltop can pay dividends if, as and when declared by Hilltop's board of directors, subject to compliance with limitations imposed by law. The holders of Hilltop common stock are entitled to receive and share equally in these dividends as they may be declared by Hilltop's board of directors out of funds legally available for such purpose. The holders of such preferred stock may have a priority over the holders of the common stock with respect to dividends. For a description of the dividend rights of holders of Series B Preferred Stock, see "Series B Preferred Stock" below.

Voting Rights

Each holder of Hilltop common stock is entitled to one vote per share and does not have any right to cumulate votes in the election of directors. Directors are elected by a plurality of the shares actually voting on the matter. Holders of the preferred stock and special voting stock may also possess voting rights. For a description of the voting rights of holders of Series B Preferred Stock, see "Series B Preferred Stock" below.

Liquidation Rights

In the event of liquidation, dissolution or winding up of Hilltop, whether voluntary or involuntary, the holders of Hilltop common stock would be entitled to receive, after payment or provision for payment of all its debts and liabilities, all of the assets of Hilltop available for distribution. Holders thereof may have a priority over the holders of the common stock in the event of liquidation or dissolution. For a description of the rights of holders of Series B Preferred Stock in the event of liquidation or dissolution, see "Series B Preferred Stock" below.

Ownership Limitations

Hilltop's charter provides for certain limitations on the amount of Hilltop common stock that may be acquired by any person, until such time as the Hilltop board of directors determines that such limitations shall cease to be effective. The Hilltop board of directors made such a determination in connection with the 2012 PlainsCapital corporation merger, and such restrictions ceased to be effective at the effective time of that merger.

Preferred Stock

Relative Rights

The Hilltop board of directors is authorized to set and change, subject to certain limitations, the preferences, conversion or other rights, voting powers, restrictions, limitations as to dividends or other distributions, qualifications and terms and conditions of redemption for each class or series of Hilltop preferred stock. In general, the holders of Hilltop preferred stock may have, and the holders of the Series B Preferred Stock do have, preferences over holders of Hilltop common stock in the payment of dividends, upon liquidation of Hilltop, in respect of voting rights and in the redemption of the capital stock of Hilltop. For a description of the rights of holders of Series B Preferred Stock, see "Series B Preferred Stock" below.

Preemptive Rights

The Board of Directors may provide, when setting the terms of classified or reclassified shares of stock, that a class or series of Hilltop preferred stock carries preemptive rights.

Series B Preferred Stock

Dividend Rights

Holders of the Series B Preferred Stock are entitled to non-cumulative cash dividends at a fluctuating dividend rate based on Hilltop's level of qualified small business lending. Hilltop may generally declare and pay dividends on Hilltop common stock only if full dividends on all outstanding shares of Series B Preferred Stock for the most recently completed dividend period have been or are contemporaneously declared and paid.

Voting Rights

The Series B Preferred Stock is non-voting, except in limited circumstances. For instance, the holders of Series B Preferred Stock would have the right to vote in connection with the authorization of stock senior to the Series B Preferred Stock, amendments to the certificate of formation of the company adversely affecting the Series B Preferred Stock or certain fundamental transactions affecting the Series B Preferred Stock. In addition, in the event the company misses dividend payments for six consecutive quarters, whether or not consecutive, the holders of the Series B Preferred Stock have, in certain circumstances, the right to appoint representatives to the company's board of directors until the dividends have been paid timely for four consecutive periods.

Liquidation Rights

In the event of any liquidation, dissolution or winding up of the affairs of Hilltop, holders of Series B Preferred Stock are entitled to receive for each share of Series B Preferred Stock, out of the assets of Hilltop or proceeds thereof (whether capital or surplus) available for distribution to stockholders of Hilltop, subject to the rights of any creditors of Hilltop, before any distribution of such assets or proceeds is made to or set aside for the holders of Hilltop common stock, payment in full of the liquidation amount (being $1,000 per share of Series B Preferred Stock) plus the amount of any accrued and unpaid dividends on each such share.

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Redemption Rights

The Series B Preferred Stock may be redeemed at any time at Hilltop's option, at a redemption price of 100% of the liquidation amount plus accrued but unpaid dividends to the date of redemption for the current period, subject to the approval of its federal banking regulator.

Preemptive Rights

The Series B Preferred Stock has no preemptive rights.

Listing

Hilltop common stock is traded on the NYSE under the symbol "HTH."

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COMPARISON OF STOCKHOLDERS' RIGHTS

Hilltop is incorporated in Maryland and SWS is incorporated in Delaware. Your rights as a stockholder of SWS are governed by the DGCL, the SWS certificate of incorporation, as amended, and the SWS bylaws. Upon completion of the merger, as a Hilltop stockholder your rights will be governed by the Maryland General Corporation Law (the "MGCL"), the Hilltop charter, as amended, and the Hilltop bylaws.

The following is a summary of the material differences between the rights of holders of Hilltop common stock and the rights of holders of SWS common stock, but does not purport to be a complete description of those differences. These differences may be determined in full by reference to the MGCL, the DGCL, the Hilltop charter, the SWS certificate of incorporation, the Hilltop bylaws and the SWS bylaws, in each case as amended. The SWS certificate of incorporation, the Hilltop charter and each corporation's bylaws are subject to amendment in accordance with their terms. Although the MGCL and the DGCL are similar in most respects, there are a number of differences between the two statutes, many (but not all) of which are summarized below. In addition, there is a substantial body of case law in Delaware interpreting the corporation laws of that state. A comparable body of judicial interpretations does not exist in Maryland such that there may be less certainty as to the outcome of matters governed by Maryland corporation law than would be the case under Delaware corporation law. Copies of the governing corporate instruments are available, without charge, to any person, including any beneficial owner to whom this proxy statement/prospectus is delivered, by following the instructions listed under "Where You Can Find More Information" included elsewhere in this proxy statement/prospectus.

SWS	HILLTOP
AUTHORIZED CAPITAL STOCK	
Authorized Shares. SWS is authorized under the SWS certificate of incorporation to issue 60,000,000 of common stock, par value $0.10 per share, and 100,000 of preferred stock, par value $1.00 per share. The SWS certificate of incorporation authorizes the board of directors to classify and reclassify any unissued shares of Hilltop common stock and preferred stock into other classes or series of stock.	*Authorized Shares.* Hilltop is authorized under the Hilltop charter to issue 125,000,000 shares of common stock, par value $0.01 per share, 10,000,000 shares of Special Voting Stock, par value $0.01 per share and 10,000,000 shares of preferred stock, par value $0.01 per share. As permitted by the MGCL, the Hilltop charter authorizes the Hilltop board of directors to classify and reclassify any unissued shares of Hilltop common stock and preferred stock into other classes or series of stock. The Hilltop charter authorizes the Hilltop board of directors, without further stockholder action, to amend the Hilltop charter to increase or decrease the aggregate number of shares of stock or the number of shares of stock of any class or series that Hilltop has authority to issue.

SWS	HILLTOP
	Special Voting Stock. The Hilltop charter authorizes the board of directors, without further stockholder action, to issue up to 10,000,000 shares of special voting stock, none of which are currently issued and outstanding. A holder of special voting stock is not entitled to any regular or special dividend payments or other distributions, including any dividends or other distributions declared or paid with respect to shares of Hilltop's common stock or any other stock, and is not entitled to receive any distributions or other rights to receive property in the event of liquidation or dissolution. A holder of special voting stock has the right to one vote on all matters submitted to a vote of Hilltop's stockholders, and the holders of special voting stock vote collectively with the holders of Hilltop common stock as one class on all matters submitted to a vote of Hilltop's stockholders.
Preferred Stock. The SWS certificate of incorporation authorizes the board of directors, without further stockholder action, to issue up to 100,000 shares of preferred stock, in one or more series, and determine any designations, preferences, limitations or relative rights in each series. The rights of preferred stockholders may supersede the rights of common stockholders.	*Preferred Stock.* The Hilltop charter authorizes the board of directors, without further stockholder action, to issue up to 10,000,000 shares of preferred stock, in one or more series, and determine any preferences, conversion or other rights, voting powers, restrictions or limitations of additional series. The rights of preferred stockholders may supersede the rights of common stockholders.
PREEMPTIVE RIGHTS	
SWS stockholders do not have preemptive rights.	Hilltop's stockholders do not have preemptive rights.
VOTING RIGHTS IN AN EXTRAORDINARY TRANSACTION	
The DGCL generally requires that any merger, consolidation, or sale of substantially all the assets of a corporation be approved by a vote of a majority of all outstanding shares entitled to vote thereon. Although a Delaware corporation's certificate of incorporation may provide for a greater vote, the SWS certificate of incorporation does not.	Under the MGCL, a board of directors must generally declare a merger, consolidation, share exchange or transfer of all or substantially all of its assets advisable and direct that such transaction be submitted to the stockholders of the corporation for consideration. The transaction must be approved by the affirmative vote of stockholders entitled to cast at least two-thirds of all the votes entitled to be cast on the matter, unless the charter provides for a greater or lesser vote (which must be at least a majority of all votes entitled to be cast on the matter). Hilltop's charter provides that such transactions shall be effective and valid if taken or approved by the affirmative vote of holders of shares entitled to cast a majority of all the votes entitled to be cast on the matter.

SWS	HILLTOP
DIVIDENDS	
The SWS bylaws provide that the board of directors may declare dividends upon its capital stock at any regular meeting, and the dividend payments shall be made, pursuant to Delaware law, either (1) out of its surplus or (2) in case of no such surplus, out of its net profits for the fiscal year in which the dividend is declared and/or the preceding fiscal year.	Under Maryland law, Hilltop may make any distribution authorized by the board of directors unless, after the distribution (1) the corporation would not be able to pay its debts as they become due in the usual course of business or (2) generally, the corporation's total assets would be less than the sum of its total liabilities, plus the amount that would be needed if the corporation were dissolved at the time of the distribution to satisfy senior liquidation preferences. Hilltop is permitted to make a distribution so long as the distribution is made from (1) the net earnings of the corporation for the fiscal year in which the distribution is made, (2) its net earnings for the preceding fiscal year or (3) the sum of its net earnings for the preceding eight fiscal quarters.
AMENDMENT TO THE CHARTER/ARTICLES OF INCORPORATION	
Under § 242 of the DGCL and the SWS certificate of incorporation, the SWS certificate of incorporation may be amended, altered, changed or repealed by the SWS board of directors, the holders of a majority of the outstanding stock entitled to vote on the amendment and, in certain cases, the holders of a majority of each class of stock entitled to vote on the amendment as a class.	The Hilltop charter authorizes the Hilltop board of directors, without further stockholder action, to amend the Hilltop charter to increase or decrease the aggregate number of shares of stock or the number of shares of stock of any class or series that Hilltop has authority to issue. Subject to limited exceptions, Hilltop's charter may otherwise be amended only by the affirmative vote of the holders of not less than two-thirds of all the votes entitled to be cast on the matter.
AMENDMENT TO THE BYLAWS	
The SWS board of directors has the power to adopt, amend or repeal its bylaws. SWS stockholders require an affirmative vote of at least $66^2/_3\%$ in voting power of the issued and outstanding shares entitled to vote in order to alter, amend, repeal or adopt a provision inconsistent with the bylaws.	The Hilltop board of directors generally has the exclusive power to adopt, alter or appeal any provision of its bylaws and to make new bylaws.

SWS	HILLTOP

APPRAISAL/DISSENTERS' RIGHTS

SWS	HILLTOP
Under the DGCL, a stockholder of a Delaware corporation generally has appraisal rights in connection with certain mergers or consolidations in which the corporation is participating, subject to specified procedural requirements. The DGCL, however, does not confer appraisal rights for the shares of any class or series of stock that is (subject to certain exceptions) either (1) listed on a national securities exchange, or (2) held of record by more than 2,000 holders. There are no appraisal rights available for stockholders if the merger does not require the vote of stockholders for its approval. Even if a corporation's stock meets the foregoing requirements the DGCL provides that appraisal rights generally will be permitted if stockholders of the corporation are required to accept for their stock in certain mergers or consolidations anything other than (1) shares of stock of the corporation surviving or resulting from such merger or consolidation, or depository receipts in respect thereof; (2) shares of stock of any other corporation, or depository receipts in respect thereof, which shares of stock (or depository receipts in respect thereof) or depository receipts at the effective date of the merger or consolidation will be either listed on a national securities exchange or held of record by more than 2,000 holders; (3) cash in lieu of fractional shares or fractional depository receipts described in the foregoing; or (4) any combination of the foregoing.	Under Maryland law, a dissenting or objecting stockholder has the right to demand and receive payment of the fair value of the stockholders' stock from the successor if (1) the corporation consolidates or merges with another corporation; (2) the corporation's stock is to be acquired in a statutory share exchange; (3) the corporation transfers its assets in a manner requiring stockholder approval under section 3-105(e) of the MGCL; (4) the corporation amends its charter in a way which alters the contract rights, as expressly set forth in the charter, of any outstanding stock and substantially adversely affects the stockholder's rights, unless the right to do so is reserved in the charter of the corporation; or (5) the transaction is subject to certain provisions of the Maryland Business Combination Act, referred to as the MBCA. Maryland law provides that a stockholder may not demand the fair value of the stockholder's stock and is bound by the terms of the transaction if, among other things, (1) generally, the class or series of stock is listed on a national securities exchange on the record date for determining stockholders entitled to vote on the matter or, in certain mergers, the date notice is given or waived (except certain mergers where stock held by directors and executive officers is exchanged for merger consideration not available generally to stockholders); (2) the stock is that of the successor in the merger, unless either (A) the merger alters the contract rights of the stock as expressly set forth in the charter and the charter does not reserve the right to do so or (B) the stock is to be changed or converted in whole or in part in the merger into something other than either stock in the successor or cash, scrip or other rights or interests arising out of provisions for the treatment of fractional shares of stock in the successor; or (3) the charter provides that the holders of the stock are not entitled to exercise the rights of an objecting stockholder. Hilltop's common stock is listed on the NYSE and is expected to be listed on the NYSE on the record date for the Hilltop special meeting. Accordingly, holders of Hilltop common stock are not expected to be entitled to demand and receive payment of fair value in accordance with the MGCL (commonly referred to as appraisal or dissenters' rights) in connection with the merger.

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SWS	HILLTOP
SPECIAL MEETINGS OF STOCKHOLDERS	
The board of directors may call a special meeting of stockholders for any purpose or purposes at any time. Business transacted at the special meeting shall be limited to the purposes stated in the notice of meeting.	The chairman of the board, chief executive officer, president or board of directors may call a special meeting of the Hilltop stockholders. A special meeting must also be called by the secretary at the request of stockholders entitled to cast at least a majority of all the votes entitled to be cast on the matter to be considered at the meeting.
STOCKHOLDER PROPOSALS AND NOMINATIONS	
The SWS bylaws provide that with respect to an annual meeting of stockholders, nominations of individuals for election to the board of directors and the proposal of business to be considered by stockholders may be made only (i) pursuant to an SWS notice of meeting, (ii) by or at the direction of the board of directors or any committee thereof or (iii) by any stockholder of record entitled to vote at the meeting and who has complied with the notice provisions of the bylaws. With respect to special meetings of stockholders, only business specified in an SWS notice of meeting may be brought before the meeting. Nominations of individuals to the SWS board of directors at a special meeting may be made only pursuant to an SWS notice of meeting (i) by or at the direction of the board of directors or any committee thereof or (ii) provided that the board of directors has determined that directors will be elected at the meeting, by a stockholder who is entitled to vote at the meeting and who has complied with the notice provisions of the bylaws.	The Hilltop bylaws provide that with respect to an annual meeting of stockholders, nominations of individuals for election to the board of directors and the proposal of business to be considered by stockholders may be made only (i) pursuant to Hilltop's notice of the meeting, (ii) by or at the direction of the board of directors or (iii) by a stockholder who is entitled to vote at the meeting and who has complied with the advance notice procedures of the bylaws. With respect to special meetings of stockholders, only the business specified in Hilltop's notice of the meeting may be brought before the meeting. Nominations of individuals for election to the Hilltop board of directors at a special meeting may be made only (i) by or at the direction of the board of directors, or (ii) provided that the board of directors has duly called the special meeting for the purpose of electing directors, by a stockholder who is entitled to vote at the meeting and who has complied with the advance notice provisions of the bylaws.
BOARD OF DIRECTORS	
Number of Directors	
The SWS board of directors has ten (10) members. The SWS bylaws provide that the number of directors shall be determined by the board of directors. Directors are elected by a plurality of votes of the shares present in person or represented by a proxy and entitled to vote on the election of directors, at a meeting of stockholders duly called and at which a quorum is present.	The Hilltop board of directors has twenty-one (21) members. The Hilltop bylaws provide that the number of directors will be not less than one (the minimum required by the MGCL) or more than fifteen (15) and may be increased or decreased from time to time in the discretion of the board, except that no decrease in the number of directors may affect the term of any incumbent director. Notwithstanding the foregoing or any other provision of its charter or bylaws, pursuant to Section 3-804(b) of the MGCL, to which Hilltop has elected in its charter to be subject, the Hilltop board of directors has the ability to fix the number of directors constituting the Hilltop board of directors. Directors are elected by a plurality of all the votes cast at a meeting of stockholders duly called and at which a quorum is present.

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SWS	HILLTOP
Classification	
The SWS board of directors is not classified; all directors are subject to re-election on an annual basis.	The Hilltop board of directors is not classified; all directors are subject to re-election on an annual basis.
Removal	
Subject to applicable law, a director of SWS may be removed from office with or without cause by the holders of the majority of the shares then entitled to vote at an election of directors.	A director of Hilltop may be removed from office only for cause and then only by the affirmative vote of at least two-thirds of the votes entitled to be cast generally in the election of directors.
Vacancies	
Subject to applicable law, vacancies on the SWS board of directors may be filled by a vote of a majority of the remaining members of the board of directors.	Vacancies on the Hilltop board of directors may be filled by vote of a majority of the remaining members of the board of directors, even if less than a quorum.
Special Meetings of the Board	
Special meetings of the SWS board of directors may be called by the Chairman of the Board, Chief Executive Officer, the President, or the Secretary on 24 hours' notice to each director. Special meetings shall be called by the Chairman of the Board, Chief Executive Officer, the President, or the Secretary on the written request of any two directors. Notice of any such meeting need not be given to any director, however, if waived by him in writing or if he shall be present at such meeting.	Special meetings of the Hilltop board of directors may be called by or at the request of the chairman of the board, the chief executive officer, the president or a majority of the directors then in office. The person or persons authorized to call special meetings of the board may fix any place as the place for holding any special meeting of the board called by them. The board may provide, by resolution, the time and place for the holding of special meetings of the board without other notice than such resolution.

SWS	HILLTOP

Director Liability and Indemnification

The SWS certification of incorporation provides that (to the fullest extent permitted by Delaware statutory or decisional law) a director shall not be liable to SWS or its stockholders for any act or omission in its capacity as a director.

Under the Delaware law, a corporation may exculpate a director for breach of fiduciary duty as a director, except for liability (i) for a breach of a director's duty of loyalty to SWS or its stockholders, (ii) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law, (iii) under Section 174 of the DGCL or (iv) for any transaction from which a director derived an improper personal benefit.

The SWS bylaws also provide that SWS shall indemnify any person who is or was a director or officer who was or is made a party to or is threatened to be made a party to any threatened, pending or completed action, suit or proceeding by reason of the fact that he is or was a director or officer of SWS against certain expenses, (1) if he acted in good faith and in a manner he reasonably believed to be in or not opposed to the best interests of SWS; (2) to the extent that the action did not relate to service or performance of his duties as a director, officer, employee or agent of another enterprise; and (3) if, with respect to any criminal action, he had no reasonable cause to believe his conduct was unlawful. The determination of indemnification shall be made by (1) majority vote of the members of the board of directors who are not party to the action (even though it may be less than a quorum); (2) by a committee of such directors designated by majority vote of such directors (even though it may be less than a quorum); (3) if there are no such directors, or if such directors so direct, by independent legal counsel in written opinion; or (4) the stockholders.

The Hilltop bylaws provide for indemnification and advancement of expenses by Hilltop, to the fullest extent permitted by Maryland law, of Hilltop directors and officers who are made or threatened to be made a party to a proceeding by reason of his or her service in that capacity. The bylaws also permit Hilltop to provide such indemnification and advancement of expenses to any Hilltop employee or agent.

Under Maryland law, directors' and officers' liability to the corporation or its stockholders for money damages may be expanded or limited, except that liability of a director or officer may not be limited: (1) to the extent that it is proved that the person actually received an improper benefit or profit in money, property or services for the amount of the benefit or profit in money, property or services actually received; or (2) to the extent that a judgment or other final adjudication adverse to the person is entered in a proceeding based on a finding in the proceeding that the person's action, or failure to act, was the result of active and deliberate dishonesty and was material to the cause of action adjudicated in the proceeding.

Under Maryland law, a corporation may not indemnify a director or officer if it is established that: (1) the act or omission of the director or officer was material to the matter giving rise to the proceeding; and (A) was committed in bad faith or (B) was the result of active and deliberate dishonesty; or (2) the director or officer actually received an improper personal benefit in money, property or services; or (3) in the case of any criminal proceeding, the director or officer had reasonable cause to believe that the act or omission was unlawful.

SWS	HILLTOP
Under Delaware law, as stated in the bylaws, there is a mandatory right to indemnification where a present or former director or officer has been successful on the merits or otherwise in defense of any action, suit or proceedings in the bylaws. The indemnification covers expenses (including attorney's fees) actually and reasonably incurred by the director or officer in connection with the matter.	Under Maryland law, a corporation may not indemnify a director or officer who has been adjudged liable in a suit by or in the right of the corporation or in which the director or officer was adjudged liable to the corporation or on the basis that a personal benefit was improperly received. A court may order indemnification if it determines that the director is fairly and reasonably entitled to indemnification, even though the director may not have met the prescribed standard of conduct or may have been adjudged liable on the basis that personal benefit was improperly received; however, indemnification for an adverse judgment in a suit by or in the right of the corporation, or for a judgment of liability on the basis that personal benefit was improperly received, is limited to expenses. Except for a proceeding brought to enforce indemnification or where a resolution of the board of directors or an agreement approved by the board expressly provides otherwise, a corporation may not indemnify a director for a proceeding brought by the director against the corporation.
STOCKHOLDER RIGHTS PLAN	
SWS does not have a stockholder rights plan currently in effect.	Hilltop does not have a stockholder rights plan currently in effect.

SWS	HILLTOP
STATE ANTI-TAKEOVER STATUTES AND ARTICLE PROVISIONS	
Business Combinations	
Under the DGCL if a person acquires 15% or more of the stock of a Delaware corporation, thereby becoming an "interested stockholder" (for purposes of Section 203 of the DGCL), that person is generally prohibited from engaging in a business combinations for a period of three years after the date of the transaction in which the person became an interested stockholder, unless (1) the board of directors approved the transaction which resulted in the stockholder becoming an interested stockholder or the business combination transaction prior to the time that the person became an interested stockholder; (2) the person became an interested stockholder and 85% owner of the voting stock of the corporation in the same transaction, excluding (for the purpose of determining the stock outstanding) voting stock owned by directors who are also officers and certain employee stock plans; or (3) the business combination transaction is approved by the board of directors and by the affirmative vote of two-thirds of the outstanding voting stock which is not owned by the interested stockholder at an annual or special meeting. Under the DGCL, the term "business combination" is defined to include a wide variety of transactions, including mergers, consolidations, sales or other dispositions of 10% or more of a corporation's assets and various other transactions that may benefit an "interested stockholder."	Under Maryland law, "business combinations" between a Maryland corporation and an interested stockholder or an affiliate of an interested stockholder are prohibited for five years after the most recent date on which the interested stockholder becomes an interested stockholder. These business combinations include a merger, consolidation, share exchange, or, in circumstances specified in the statute, an asset transfer or issuance or reclassification of equity securities. An interested stockholder is defined as: any person who beneficially owns 10% or more of the voting power of the corporation's shares; or
A Delaware corporation may elect not to be governed by Section 203. SWS has not made such an election and accordingly is subject to Section 203.	an affiliate or associate of the corporation who, at any time within the two-year period prior to the date in question, was the beneficial owner of 10% or more of the voting power of the then outstanding voting stock of the corporation. A person is not an interested stockholder under the statute if the board of directors approved in advance the transaction by which he otherwise would have become an interested stockholder. However, in approving a transaction, the board of directors may provide that its approval is subject to compliance, at or after the time of approval, with any terms and conditions determined by the board. After the five-year prohibition, any business combination between the Maryland corporation and an interested stockholder generally must be recommended by the board of directors of the corporation and approved by the affirmative vote of at least: 80% of the votes entitled to be cast by holders of outstanding shares of voting stock of the corporation; and

two-thirds of the votes entitled to be cast by holders of voting stock of the corporation other than shares held by the interested stockholder with whom or with whose affiliate the business combination is to be effected or held by an affiliate or associate of the interested stockholder.

These super-majority vote requirements do not apply if the corporation's common stockholders receive a minimum price, as defined under Maryland law, for their shares in the form of cash or other consideration in the same form as previously paid by the interested stockholder for its shares.

SWS	HILLTOP
	The statute permits the board of directors to adopt a resolution opting out of the application of the statute, and the Hilltop board of directors has adopted such a resolution. In addition, the Hilltop charter contains a provision that requires Hilltop to obtain stockholder approval before it can opt back into the statute.

Control Share Acquisition

Delaware law does not contain a control share acquisition statute.	Maryland law provides that holders of control shares of a Maryland corporation acquired in a control share acquisition have no voting rights with respect to the control shares except to the extent approved by an affirmative vote of at least two-thirds of the votes entitled to be cast on the matter. Shares owned by the acquirer, by officers or by directors who are employees of the corporation are excluded from shares entitled to vote on the matter. Control shares are shares of stock which, if aggregated with all other shares of stock owned by the acquirer or in respect of which the acquirer is able to exercise or direct the exercise of voting power (except solely by virtue of a revocable proxy), would entitle the acquirer to exercise voting power in electing directors within one of the following ranges of voting power: one-tenth or more but less than one-third, one-third or more but less than a majority, or a majority or more of all voting power. Control shares do not include shares the acquiring person is then entitled to vote as a result of having previously obtained stockholder approval. A control share acquisition means the acquisition of control shares, or the power to direct the exercise of voting power with respect to such shares, subject to certain exceptions. A person who has made or proposes to make a control share acquisition may compel the board of directors of the corporation to call a special meeting of stockholders to be held within 50 days of demand to consider the voting rights of the shares. The right to compel the calling of a special meeting is subject to the satisfaction of certain conditions, including an undertaking to pay the expenses of the meeting. If no request for a meeting is made, the corporation may itself present the question at any stockholders meeting.

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SWS	HILLTOP
	If voting rights are not approved at the meeting or if the acquiring person does not deliver an acquiring person statement as required by the statute, then the corporation may redeem for fair value any or all of the control shares, except those for which voting rights have previously been approved. The right of the corporation to redeem control shares is subject to certain conditions and limitations. Fair value is determined, without regard to the absence of voting rights for the control shares, as of the date of the last control share acquisition by the acquirer or of any meeting of stockholders at which the voting rights of the shares are considered and not approved. If voting rights for control shares are approved at a stockholders meeting and the acquirer becomes entitled to vote a majority of the shares entitled to vote, or direct the exercise of a majority of all voting power, all other stockholders may exercise appraisal rights. The fair value of the shares as determined for purposes of appraisal rights may not be less than the highest price per share paid by the acquirer in the control share acquisition. The control share acquisition statute does not apply (i) to shares acquired in a merger, consolidation or share exchange if the corporation is a party to the transaction or (ii) to acquisitions approved or exempted by the charter or bylaws of the corporation. Hilltop's bylaws contain a provision exempting from the control share acquisition statute any and all acquisitions by any person of shares of Hilltop's stock. In addition, Hilltop's charter contains a provision that requires Hilltop to obtain the approval of its stockholders before it can opt back into the statute. The Hilltop charter provides for certain transfer restrictions that, subject to certain exceptions (including board approval), prohibit and void transactions which would create new 5% stockholders or increase the ownership percentage of existing 5% stockholders of Hilltop. The Hilltop board of directors has resolved that as of the effective time of the merger, such restrictions will no longer be in the best interests of Hilltop and its stockholders, and that such restrictions shall cease to be effective as of the effective time.

SWS	HILLTOP
DUTIES OF DIRECTORS	
Under Delaware law, the standards of conduct for directors have developed through written opinions of the Delaware courts. Generally, directors of a Delaware corporation are subject to a duty of loyalty, a duty of care and a duty of disclosure to the corporation's stockholders. The duty of care requires directors to exercise the care that a similarly situated person would exercise under similar circumstances, including informing themselves prior to making a business decision of all material information reasonably available to them. Directors should have sufficient information and should critically examine the information they have. The duty of loyalty requires directors to act in a manner that a director honestly believes to be in the best interest of the corporation and its stockholders, and refrain from self-dealing. The duty of disclosure requires directors to disclose fully and fairly all material information within the board's control when it seeks stockholder action.	Under the MGCL, the standard of conduct for directors is governed by statute. The MGCL requires that a director of a Maryland corporation perform his or her duties: (1) in good faith, (2) in a manner the director reasonably believes to be in the interests of the corporation and (3) with the care that an ordinarily prudent person in a like position would use under similar circumstances.

LEGAL MATTERS

The validity of the Hilltop common stock to be issued in connection with the merger will be passed upon for Hilltop by Wachtell, Lipton, Rosen & Katz. Certain U.S. federal income tax consequences relating to the merger will also be passed upon for Hilltop by Wachtell, Lipton, Rosen & Katz, and for SWS by Davis Polk & Wardwell LLP.

EXPERTS

The audited consolidated financial statements of Hilltop included in this proxy statement/prospectus, except as they relate to PrimeLending and First Southwest Company as of December 31, 2012 and for the period from December 1, 2012 through December 31, 2012, have been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm. Such financial statements, except as they relate to PrimeLending and First Southwest Company as of December 31, 2012 and for the period from December 1, 2012 through December 31, 2012, have been so included in reliance on the report of such independent registered public accounting firm given on the authority of said firm as experts in auditing and accounting.

The financial statements of PrimeLending and First Southwest Company as of December 31, 2012 and for the period from December 1, 2012 through December 31, 2012, not separately presented herein, but which are referred to and made a part of this proxy statement/prospectus and Registration Statement, have been audited by Ernst & Young LLP, an independent registered public accounting firm, as set forth in their reports appearing elsewhere herein. The audited financial statements of Hilltop, to the extent they relate to PrimeLending and First Southwest Company as of December 31, 2012 and for the period from December 1, 2012 through December 31, 2012, have been so included in reliance upon such reports given on the authority of such firm as experts in accounting and auditing.

The audited statement of assets acquired and liabilities assumed by PlainsCapital Bank, a wholly-owned subsidiary of Hilltop, included in this proxy statement/prospectus has been so included in reliance on the report of PricewaterhouseCoopers LLP, independent registered public accounting firm, given on the authority of said firm as experts in auditing and accounting.

The consolidated financial statements and management's assessment of the effectiveness of internal control over financial reporting of SWS (which is included in Management's Report on Internal Control Over Financial Reporting) incorporated in this proxy statement/prospectus by reference to SWS's Annual Report on Form 10-K for the year ended June 30, 2014 have been so incorporated in reliance on the reports of Grant Thornton LLP, an independent registered public accounting firm, upon the authority of said firm as experts in auditing and accounting.

OTHER MATTERS

According to the SWS bylaws, business to be conducted at a special meeting of stockholders may be brought before the meeting only pursuant to a notice of meeting. Accordingly, no matters other than the matters described in this proxy statement/prospectus will be presented for action at the special meeting or at any adjournment or postponement of the special meeting.

DEADLINE FOR SUBMITTING STOCKHOLDER PROPOSALS

SWS will hold an annual meeting for its 2014 fiscal year only if the merger has not already been completed.

Pursuant to rules of the SEC, a stockholder who intends to present a proposal at SWS's next annual meeting of stockholders and who wishes the proposal to be included in the proxy statement for that meeting must submit the proposal in writing to the attention of the Corporate Secretary of SWS at 1201 Elm Street, Suite 3500, Dallas, Texas 75270. The proposal must be received no later than June 5, 2014.

Stockholders wishing to submit proposals to be presented directly at SWS's next annual meeting of stockholders instead of by inclusion in next year's proxy statement must follow the submission criteria and deadlines set forth in SWS's bylaws concerning stockholder proposals. To be timely in connection with SWS's next annual meeting, a stockholder proposal concerning business other than director nominations must be received by SWS at its principal executive offices not later than the close of business on August 16, 2014, nor earlier than the close of business on July 17, 2014, unless the date of SWS's annual meeting is more than 30 days before or more than 70 days after November 14, 2014, in which case notice must be delivered not earlier than the close of business on the one hundred twentieth day prior to such annual meeting and not later than the close of business on the later of the ninetieth day prior to such annual meeting or the tenth day following the day on which public announcement of the date of such meeting is first made by SWS. In no event shall the public announcement of an adjournment or postponement of an annual meeting commence a new time period (or extend any time period) for the giving of a stockholder's notice as described above.

You may obtain a copy of SWS's bylaws by writing to the Corporate Secretary of SWS at the above address. The chairman of the meeting may refuse to bring before a meeting any business not brought in compliance with applicable law and SWS's bylaws.

STOCKHOLDERS SHARING AN ADDRESS

Only one copy of this proxy statement/prospectus is being delivered to multiple stockholders of SWS sharing an address unless SWS has previously received contrary instructions from one or more of such stockholders. On written or oral request to the Secretary of SWS at 1201 Elm Street, Suite 3500, Dallas, Texas 75270, (214) 859-1800, SWS will deliver promptly a separate copy of this proxy statement/prospectus to a stockholder at a shared address to which a single copy of the proxy statement/prospectus was delivered. Stockholders sharing an address who wish, in the future, to receive separate copies or a single copy of SWS's proxy statements and annual reports should provide written or oral notice to the Secretary of SWS at the address and telephone number set forth above.

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WHERE YOU CAN FIND MORE INFORMATION

Hilltop and SWS separately file annual, quarterly and current reports, proxy statements and other information with the SEC. You may read and copy any of this information filed with the SEC at the SEC's public reference room:

Public Reference Room
100 F Street NE
Room 1024
Washington, D.C. 20549

For information regarding the operation of the Public Reference Room, you may call the SEC at 1-800-SEC-0330. The SEC also maintains an internet website that contains reports, proxy statements and other information about issuers, like Hilltop and SWS, who file electronically with the SEC. The address of the site is www.sec.gov. Copies of the documents filed with the SEC by SWS are also available free of charge on SWS's internet website at www.swst.com or by contacting SWS's Investor Relations Department at (214) 859-1800. Copies of the documents filed with the SEC by Hilltop are also available free of charge on Hilltop's internet website at www.hilltop-holdings.com or by contacting Hilltop's Investor Relations Department at (214) 252-4029. We have included the web addresses of the SEC and Hilltop as inactive textual references only.

Hilltop is currently not eligible to incorporate in this proxy statement/prospectus by reference any documents that it filed, or may file in the future, with the SEC under Sections 13(a), 13(c), 14 and 15(d) of the Exchange Act.

The SEC allows SWS to incorporate by reference information in this proxy statement/prospectus. This means that SWS can disclose important information to you by referring you to another document filed separately with the SEC. The information incorporated by reference is considered to be a part of this proxy statement/prospectus, except for any information that is superseded by information that is included directly in this proxy statement/prospectus. Neither SWS nor Hilltop incorporates the contents of their websites into this proxy statement/prospectus.

This proxy statement/prospectus incorporates by reference the documents listed below, which contain important information about SWS and its financial condition. The following documents, which were filed by SWS with the SEC, are incorporated by reference into this proxy statement/prospectus:

SWS SEC Filings (SEC File No. 000-19483)	**Period or Date Filed**
Annual Report on Form 10-K and 10-K/A	Fiscal year ended June 30, 2014
Current Reports on Form 8-K	Filed on September 5, 2014, October 2, 2014 and October 6, 2014

To the extent that any information contained in any report on Form 8-K or any exhibit thereto, was furnished to, rather than filed with the SEC, such information or exhibit is specifically not incorporated by reference.

In addition, SWS incorporates by reference additional documents that it may file with the SEC pursuant to Sections 13(a), 13(c), 14, or 15(d) of the Exchange Act between the date of this proxy statement/prospectus and the date of the SWS special meeting. These documents include periodic reports, such as annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K, excluding any information furnished pursuant to Items 2.02 or 7.01 of any current report on Form 8-K, as well as proxy statements.

Except where the context otherwise indicates, SWS has supplied all information contained or incorporated by reference in this proxy statement/prospectus relating to SWS, and Hilltop has supplied all information contained in this proxy statement/prospectus relating to Hilltop as well as all pro forma financial information.

Documents incorporated by reference are available from SWS without charge, excluding any exhibits to those documents unless the exhibit is specifically incorporated by reference as an exhibit in this proxy statement/prospectus. You can obtain documents incorporated by reference in this proxy statement/prospectus by requesting them in writing or by telephone from SWS as follows:

SWS Group, Inc.
1201 Elm Street, Suite 3500
Dallas, Texas 75270
Attention: Investor Relations
Telephone: (214) 859-1800

IF YOU WOULD LIKE TO REQUEST DOCUMENTS FROM SWS, PLEASE CONTACT SWS NO LATER THAN NOVEMBER 14, 2014, IN ORDER TO RECEIVE THEM BEFORE THE SPECIAL MEETING. You will not be charged for any of these documents that you request. If you request any incorporated documents from SWS, SWS will mail them to you by first class mail, or another equally prompt means after it receives your request.

Neither Hilltop nor SWS has authorized anyone to give any information or make any representation about the merger or our companies that is different from, or in addition to, that contained in this proxy statement/prospectus or in any of the materials that have been incorporated in this proxy statement/prospectus. Therefore, if anyone does give you information of this sort, you should not rely on it. If you are in a jurisdiction where offers to exchange or sell, or solicitations of offers to exchange or purchase, the securities offered by this proxy statement/prospectus or the solicitation of proxies is unlawful, or if you are a person to whom it is unlawful to direct these types of activities, then the offer presented in this proxy statement/prospectus does not extend to you. The information contained in this proxy statement/prospectus speaks only as of the date of this proxy statement/prospectus unless the information specifically indicates that another date applies.

The representations, warranties and covenants described in this proxy statement/prospectus and included in the merger agreement were made only for purposes of the merger agreement and as of specific dates, are solely for the benefit of Hilltop and SWS, may be subject to limitations, qualifications or exceptions agreed upon by the parties, including those included in confidential disclosures made for the purposes of, among other things, allocating contractual risk between Hilltop and SWS rather than establishing matters as facts, and may be subject to standards of materiality that differ from those standards relevant to investors. You should not rely on the representations, warranties, or covenants or any description thereof as characterizations of the actual state of facts or condition of Hilltop, SWS or any of their respective subsidiaries or affiliates. Moreover, information concerning the subject matter of the representations, warranties, and covenants may change after the date of the merger agreement, which subsequent information may or may not be fully reflected in public disclosures by Hilltop or SWS. The representations and warranties and other provisions of the merger agreement should not be read alone, but instead should be read only in conjunction with the information provided elsewhere in this proxy statement/prospectus and in the documents incorporated by reference into this proxy statement/prospectus.

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Report of Independent Registered Public Accounting Firm

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

In our opinion, based on our audits and the report of other auditors, the accompanying consolidated balance sheets and the related consolidated statements of operations, of comprehensive income (loss), of stockholders' equity and of cash flows present fairly, in all material respects, the financial position of Hilltop Holdings Inc. and its subsidiaries (the "Company") at December 31, 2013 and 2012, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2013 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of PrimeLending and First Southwest Company as of December 31, 2012 and for the period from December 1, 2012 to December 31, 2012, both wholly owned subsidiaries of the Company, which statements reflect total assets of approximately $1.5 billion and $0.5 billion, respectively, of the related consolidated total as of December 31, 2012 and total net income before tax of approximately $5.7 million and $1.6 million, respectively, of the related consolidated total for the year ended December 31, 2012. Those statements were audited by other auditors whose report thereon has been furnished to us, and our opinion expressed herein, insofar as it relates to the amounts included for PrimeLending and First Southwest Company, is based solely on the reports of the other auditors. We conducted our audits of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits and the report of other auditors provide a reasonable basis for our opinion.

/s/ PricewaterhouseCoopers LLP

Dallas, Texas
March 3, 2014

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholder
PrimeLending, a PlainsCapital Company

We have audited the consolidated financial statements of PrimeLending, a PlainsCapital Company (the Company), which comprise the consolidated balance sheet as of December 31, 2012, and the related consolidated statement of income, stockholder's equity, and cash flows for the period from December 1, 2012 through December 31, 2012, and the related consolidated notes to the financial statements (not presented separately herein).

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in conformity with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free of material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States and in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of PrimeLending, a PlainsCapital Company at December 31, 2012, and the results of its operations and its cash flows for the period from December 1, 2012 through December 31, 2012 in conformity with U.S. generally accepted accounting principles.

/s/ Ernst & Young LLP

Dallas, Texas
March 15, 2013

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Report of Independent Registered Public Accounting Firm

Board of Directors
First Southwest Company

We have audited the financial statements of First Southwest Company (the Company), which comprise the statement of financial condition as of December 31, 2012, and the related statements of income, changes in stockholder's equity, and cash flows for the period from December 1, 2012 through December 31, 2012 that are filed pursuant to Rule 17a-5 under the Securities Exchange Act of 1934, and the related notes to the financial statements (not presented separately herein).

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in conformity with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States and in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Company's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of First Southwest Company as of December 31, 2012, and the results of its operations and its cash flows for the period from December 1, 2012 through December 31, 2012, in conformity with U.S. generally accepted accounting principles.

/s/ Ernst & Young LLP

Dallas, Texas
February 28, 2013

HILLTOP HOLDINGS INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share data)

	December 31, 2013	December 31, 2012
Assets		
Cash and due from banks	$ 713,099	$ 722,039
Federal funds sold and securities purchased under agreements to resell	32,924	4,421
Securities:		
Trading, at fair value	58,846	90,113
Available for sale, at fair value (amortized cost of $1,256,862 and $978,502, respectively)	1,203,143	990,953
	1,261,989	1,081,066
Loans held for sale	1,089,039	1,401,507
Non-covered loans, net of unearned income	3,514,646	3,152,396
Allowance for non-covered loan losses	(33,241)	(3,409)
Non-covered loans, net	3,481,405	3,148,987
Covered loans, net of allowance of $1,061	1,005,308	
Broker-dealer and clearing organization receivables	119,317	145,564
Insurance premiums receivable	25,597	24,615
Deferred policy acquisition costs	20,991	19,812
Premises and equipment, net	200,706	111,381
FDIC indemnification asset	188,291	
Covered other real estate owned	142,833	
Mortgage servicing rights	20,149	2,080
Other assets	279,745	293,885
Goodwill	251,808	253,770
Other intangible assets, net	70,921	77,738
Total assets	$ 8,904,122	$ 7,286,865

	2013	2012
Liabilities and Stockholders' Equity		
Deposits:		
Noninterest-bearing	$ 1,773,749	$ 1,349,584
Interest-bearing	4,949,169	3,350,877
Total deposits	6,722,918	4,700,461
Broker-dealer and clearing organization payables	129,678	187,990
Reserve for losses and loss adjustment expenses	27,468	34,012
Unearned insurance premiums	88,422	82,598
Short-term borrowings	342,087	728,250
Notes payable	56,327	141,539
Junior subordinated debentures	67,012	67,012

Other liabilities	158,288	198,453
Total liabilities	7,592,200	6,140,315
Commitments and contingencies (see Notes 18 and 19)		
Stockholders' equity:		
Hilltop stockholders' equity:		
Preferred stock, $0.01 par value, 10,000,000 shares authorized; Series B, liquidation value per share of $1,000; 114,068 shares issued and outstanding	114,068	114,068
Common stock, $0.01 par value, 100,000,000 shares authorized; 90,175,688 and 83,487,340 shares issued and outstanding, respectively	902	835
Additional paid-in capital	1,388,641	1,304,448
Accumulated other comprehensive income (loss)	(34,863)	8,094
Accumulated deficit	(157,607)	(282,949)
Total Hilltop stockholders' equity	1,311,141	1,144,496
Noncontrolling interest	781	2,054
Total stockholders' equity	1,311,922	1,146,550
Total liabilities and stockholders' equity	$ 8,904,122	$ 7,286,865

See accompanying notes.

HILLTOP HOLDINGS INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share data)

	Year Ended December 31,		
	2013	**2012**	**2011**
Interest income:			
Loans, including fees	$ 284,782	$ 23,900	$
Securities:			
Taxable	27,078	13,116	11,049
Tax-exempt	4,775	464	
Federal funds sold and securities purchased under agreements to resell	113	106	
Interest-bearing deposits with banks	1,848	801	
Other	10,479	651	
Total interest income	329,075	39,038	11,049
Interest expense:			
Deposits	14,877	1,013	
Short-term borrowings	1,814	215	
Notes payable	10,512	8,613	8,985
Junior subordinated debentures	2,409	212	
Other	3,262	143	
Total interest expense	32,874	10,196	8,985
Net interest income	296,201	28,842	2,064
Provision for loan losses	37,158	3,800	
Net interest income after provision for loan losses	259,043	25,042	2,064
Noninterest income:			
Net realized gains on securities	4,937	112	817
Net gains from sale of loans and other mortgage production income	457,531	50,384	
Mortgage loan origination fees	79,736	7,224	
Net insurance premiums earned	157,533	146,701	134,048
Investment and securities advisory fees and commissions	93,093	11,238	
Bargain purchase gain	12,585		
Other	44,670	8,573	6,785
Total noninterest income	850,085	224,232	141,650
Noninterest expense:			
Employees' compensation and benefits	480,496	60,972	7,743
Loss and loss adjustment expenses	110,755	109,159	96,734
Policy acquisition and other underwriting expenses	46,289	43,658	40,196
Occupancy and equipment, net	86,248	7,360	788
Other	187,947	34,368	9,793
Total noninterest expense	911,735	255,517	155,254

Income (loss) before income taxes	197,393	(6,243)	(11,540)
Income tax expense (benefit)	70,684	(1,145)	(5,009)
Net income (loss)	126,709	(5,098)	(6,531)
Less: Net income attributable to noncontrolling interest	1,367	494	
Income (loss) attributable to Hilltop	125,342	(5,592)	(6,531)
Dividends on preferred stock	4,327	259	
Income (loss) applicable to Hilltop common stockholders	$ 121,015	$ (5,851)	$ (6,531)
Earnings (loss) per common share:			
Basic	$ 1.43	$ (0.10)	$ (0.12)
Diluted	$ 1.40	$ (0.10)	$ (0.12)
Weighted average share information:			
Basic	84,382	58,754	56,499
Diluted	90,331	58,754	56,499

See accompanying notes.

HILLTOP HOLDINGS INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(in thousands)

	Year Ended December 31,		
	2013	**2012**	**2011**
Net income (loss)	$ 126,709	$ (5,098)	$ (6,531)
Other comprehensive income (loss):			
Unrealized gains (losses) on securities available for sale, net of tax of $(23,765), $(3,172) and $4,692, respectively	(43,039)	(5,889)	8,713
Other	82		
Comprehensive income (loss)	83,752	(10,987)	2,182
Less: comprehensive income attributable to noncontrolling interest	1,367	494	
Comprehensive income (loss) applicable to Hilltop	$ 82,385	$ (11,481)	$ 2,182

See accompanying notes.

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HILLTOP HOLDINGS INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(in thousands)

	Preferred Stock		Common Stock		Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss)	Accumulated Deficit	Total Hilltop Stockholders' Equity	Noncontrolling Interest	Total Stockholders' Equity
	Shares	Amount	Shares	Amount						
Balance, December 31, 2010		$	56,495	$ 565	$ 918,046	$ 5,270	$ (270,826)	$ 653,055	$	$ 653,055
Net loss							(6,531)	(6,531)		(6,531)
Other comprehensive income						8,713		8,713		8,713
Stock-based compensation expense					98			98		98
Common stock issued to board members			6		48			48		48
Balance, December 31, 2011		$	56,501	$ 565	$ 918,192	$ 13,983	$ (277,357)	$ 655,383	$	$ 655,383
Net loss							(5,592)	(5,592)	494	(5,098)
Other comprehensive income						(5,889)		(5,889)		(5,889)
Issuance of preferred stock	114	114,068						114,068		114,068
Issuance of common stock			27,123	271	387,312			387,583		387,583
Stock-based compensation expense					450			450		450
Common stock issued to board members			4		50			50		50
Repurchase and retirement of common stock			(141)	(1)	(1,297)			(1,298)		(1,298)
Dividends on preferred stock					(259)			(259)		(259)
Acquired noncontrolling interest									1,789	1,789
Cash distributions to noncontrolling interest									(229)	(229)
Balance, December 31, 2012	114	$ 114,068	83,487	$ 835	$ 1,304,448	$ 8,094	$ (282,949)	$ 1,144,496	$ 2,054	$ 1,146,550
Net income							125,342	125,342	1,367	126,709
Other comprehensive loss						(42,957)		(42,957)		(42,957)
Issuance of common stock			6,208	62	86,705			86,767		86,767
Stock-based compensation expense					1,671			1,671		1,671
			10		149			149		149

Common stock issued to board members										
Issuance of restricted common stock			471	5	(5)					
Dividends on preferred stock					(4,327)			(4,327)		(4,327)
Cash distributions to noncontrolling interest									(2,640)	(2,640)
Balance, December 31, 2013	114	$ 114,068	90,176	$ 902	$ 1,388,641	$ (34,863)	$ (157,607)	$ 1,311,141	$ 781	$ 1,311,922

See accompanying notes.

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HILLTOP HOLDINGS INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

	Year Ended December 31,		
	2013	**2012**	**2011**
Operating Activities			
Net income (loss)	$ 126,709	$ (5,098)	$ (6,531)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities			
Provision for loan losses	37,158	3,800	
Depreciation, amortization and accretion, net	(53,794)	(2,533)	1,714
Net realized gains on securities	(4,937)	(112)	(817)
Bargain purchase gain	(12,585)		
Deferred income taxes	15,829	(6,426)	(3,930)
Other, net	6,249	612	546
Net change in trading securities	31,267	12,900	
Net change in broker-dealer and clearing organization receivables	21,219	43,309	
Net change in other assets	7,465	(541)	12,237
Net change in broker-dealer and clearing organization payables	(55,247)	(46,509)	
Net change in loss and loss adjustment expense reserve	(6,544)	(10,823)	(14,047)
Net change in unearned insurance premiums	5,824	1,937	7,847
Net change in other liabilities	(34,540)	9,025	(341)
Net gains from sale of loans	(457,531)	(50,384)	
Loans originated for sale	(11,752,800)	(1,344,577)	
Proceeds from loans sold	12,522,963	1,510,639	
Net cash provided by (used in) operating activities	396,705	115,219	(3,322)
Investing Activities			
Proceeds from maturities and principal reductions of securities held to maturity			7,336
Proceeds from sales, maturities and principal reductions of securities available for sale	381,890	77,445	13,846
Purchases of securities available for sale	(372,998)	(224,893)	(81,583)
Net change in loans	(140,437)	10,673	
Purchases of premises and equipment and other assets	(33,066)	(17,412)	(296)
Proceeds from sales of premises and equipment and other real estate owned	21,233	1,377	
Net cash received for Federal Home Loan Bank and Federal Reserve Bank stock	4,600		
Net cash from FNB Transaction and PlainsCapital Merger	362,695	165,679	
Net cash provided by (used in) investing activities	223,917	12,869	(60,697)
Financing Activities			
Net change in deposits	(210,491)	207,997	
Net change in short-term borrowings	(386,163)	(185,812)	
Proceeds from notes payable	2,000		
Payments on notes payable	(3,262)	(766)	(6,900)
Payments to repurchase common stock		(1,298)	
Dividends paid on preferred stock	(2,985)		
Net cash distributed to noncontrolling interest	(2,640)	(229)	
Other, net	2,482	(40)	
Net cash provided by (used in) financing activities	(601,059)	19,852	(6,900)

Net change in cash and cash equivalents	19,563	147,940	(70,919)
Cash and cash equivalents, beginning of year	726,460	578,520	649,439
Cash and cash equivalents, end of year	$ 746,023	$ 726,460	$ 578,520
Supplemental Disclosures of Cash Flow Information			
Cash paid for interest	$ 31,805	$ 10,371	$ 8,780
Cash paid for income taxes, net of refunds	$ 73,802	$ (184)	$ (811)
Supplemental Schedule of Non-Cash Activities			
Redemption of senior exchangeable notes for common stock	$ 83,950	$	$
Conversion of loans to other real estate owned	$ 25,639	$	$
Preferred stock issued in acquisition	$	$ 114,068	$
Common stock issued in acquisition	$	$ 387,583	$

See accompanying notes.

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements

1. Summary of Significant Accounting and Reporting Policies

Nature of Operations

Hilltop Holdings Inc. ("Hilltop" and, collectively with its subsidiaries, the "Company") was organized in July 1998 as a Maryland corporation. Hilltop is a financial holding company registered under the Bank Holding Company Act of 1956, as amended by the Gramm-Leach-Bliley Act of 1999. On November 30, 2012, Hilltop acquired PlainsCapital Corporation pursuant through a plan of merger whereby PlainsCapital Corporation merged with and into a wholly owned subsidiary (the "PlainsCapital Merger"), which continued as the surviving entity under the name "PlainsCapital Corporation" ("PlainsCapital").

PlainsCapital is a financial holding company, headquartered in Dallas, Texas, that provides, through its subsidiaries, an array of financial products and services. In addition to traditional banking services, PlainsCapital provides residential mortgage lending, investment banking, public finance advisory, wealth and investment management, treasury management, capital equipment leasing, fixed income sales, asset management, and correspondent clearing services. The operating results of Hilltop for the year ended December 31, 2012 include the results from the operations acquired in the PlainsCapital Merger for the month ended December 31, 2012. Certain disclosures within the notes to consolidated financial statements are specific to financial products and services of PlainsCapital and its subsidiaries and therefore include information at December 31, 2013 and 2012 and relating to the post-acquisition year ended December 31, 2013 and one month period ended December 31, 2012.

Prior to the consummation of the PlainsCapital Merger, the Company's primary operations were limited to providing fire and homeowners insurance to low value dwellings and manufactured homes primarily in Texas and other areas of the southern United States through the Company's wholly owned property and casualty insurance holding company, National Lloyds Corporation ("NLC"), formerly known as NLASCO, Inc.

On September 13, 2013 (the "Bank Closing Date"), PlainsCapital Bank (the "Bank") assumed substantially all of the liabilities, including all of the deposits, and acquired substantially all of the assets of Edinburg, Texas-based First National Bank ("FNB") from the Federal Deposit Insurance Corporation (the "FDIC"), as receiver, and reopened former FNB branches acquired from the FDIC under the "PlainsCapital Bank" name (the "FNB Transaction"). Pursuant to the Purchase and Assumption Agreement (the "P&A Agreement"), the Bank and the FDIC entered into loss-share agreements whereby the FDIC agreed to share in the losses of certain covered loans and covered other real estate owned ("OREO") that the Bank acquired, as further described in Note 2 to the consolidated financial statements. Based on preliminary purchase date valuations, the fair value of the assets acquired was $2.2 billion, including $1.1 billion in covered loans, $286.2 million in securities, $135.2 million in covered OREO and $42.9 million in non-covered loans. The Bank also assumed $2.2 billion in liabilities, consisting primarily of deposits. FNB's expansive branch network allows the Bank to further develop its Texas footprint through expansion into the Rio Grande Valley, Houston, Corpus Christi, Laredo and El Paso markets, among others.

Basis of Presentation

The preparation of financial statements in conformity with accounting principles generally accepted in the United States ("GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

1. Summary of Significant Accounting and Reporting Policies (Continued)

reporting period. Actual results could differ from those estimates. Estimates regarding the allowance for loan losses, the fair values of financial instruments, the amounts receivable under the loss-share agreements with the FDIC ("FDIC Indemnification Asset"), reserves for losses and loss adjustment expenses, the mortgage loan indemnification liability, and the potential impairment of assets are particularly subject to change. The Company has applied its critical accounting policies and estimation methods consistently in all periods presented in these consolidated financial statements. As discussed in Note 2 to the consolidated financial statements, the purchase date valuations for certain identifiable assets acquired and liabilities assumed in the FNB Transaction are considered preliminary because management made significant estimates and exercised significant judgment in estimating fair values and accounting associated with the real estate appraisal validation exercise due to the short time period between the Bank Closing Date and December 31, 2013.

The presentation of the Company's historical consolidated financial statements has been modified and certain items in the prior period financial statements have been reclassified to conform to the current period presentation, which is more consistent with that of a financial institution that provides an array of financial products and services.

Certain reclassifications have been made to the prior period consolidated financial statements to conform with the current period presentation. In addition, the Company revised its historical consolidated balance sheets to correct the classification of certain noninterest-bearing deposits. The correction resulted in an increase in noninterest-bearing deposits and a decrease in interest-bearing deposits of $1.3 billion and $1.0 billion at December 31, 2013 and 2012, respectively, and the correction of the deposits note to the consolidated financial statements. Management has evaluated the impact of the correction as immaterial to previously issued financial statements; however, management has elected to revise such amounts in the accompanying consolidated financial statements. The Company will similarly revise the consolidated balance sheets and deposits note to the quarterly and annual consolidated financial statements in its future filings.

Hilltop owns 100% of the outstanding stock of PlainsCapital. PlainsCapital owns 100% of the outstanding stock of the Bank and 100% of the membership interest in PlainsCapital Equity, LLC. The Bank owns 100% of the outstanding stock of PrimeLending, a PlainsCapital Company ("PrimeLending") and PCB-ARC, Inc. The Bank has a 100% membership interest in First Southwest Holdings, LLC ("First Southwest") and PlainsCapital Securities, LLC, as well as a 51% voting interest in PlainsCapital Insurance Services, LLC.

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

PrimeLending owns a 100% membership interest in PrimeLending Ventures Management, LLC, the controlling and sole managing member of PrimeLending Ventures, LLC ("Ventures").

The principal subsidiaries of First Southwest are First Southwest Company ("FSC"), a broker-dealer registered with the Securities and Exchange Commission (the "SEC") and the Financial Industry Regulatory Authority, and First Southwest Asset Management, Inc., a registered investment advisor under the Investment Advisors Act of 1940.

The consolidated financial statements include the accounts of the above-named entities. All significant intercompany transactions and balances have been eliminated. Noncontrolling interests have been recorded for minority ownership in entities that are not wholly owned and are presented in

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

1. Summary of Significant Accounting and Reporting Policies (Continued)

compliance with the provisions of Noncontrolling Interest in Subsidiary Subsections of the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC").

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

Accounting Change

Effective October 1, 2013, the Company changed its method of applying ASC Topic 350 such that the annual goodwill impairment testing date was changed from December 31st to October 1st for its insurance reporting unit. This new testing date is preferable under the circumstances in order to combine evaluation efforts to provide for a more consistent, efficient and effective entity-wide impairment testing process and it allows the Company more time to accurately complete its impairment testing process in order to incorporate the results in the annual consolidated financial statements. The Company has prospectively applied the change in the annual goodwill impairment testing date from October 1, 2013.

Acquisition Accounting

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

Securities Purchased Under Agreements to Resell

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

Securities

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

Securities held but not intended to be held to maturity or on a long-term basis are classified as available for sale. Securities included in this category are those that management intends to use as part of its asset/liability management strategy and that may be sold in response to changes in interest rates, resultant prepayment risk, and other factors related to interest rate and resultant prepayment risk changes. Securities available for sale are carried at fair value. Unrealized holding gains and losses on

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

1. Summary of Significant Accounting and Reporting Policies (Continued)

securities available for sale, net of taxes, are reported in other comprehensive income (loss) until realized. Premiums and discounts are recognized in interest income using the effective interest method and consider any optionality that may be embedded in the security.

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

Loans Held for Sale

Loans held for sale consist primarily of single-family residential mortgages funded through PrimeLending. These loans are generally on the consolidated balance sheet for no more than 30 days. Substantially all mortgage loans originated by PrimeLending are sold in the secondary market, the majority with servicing released. Mortgage loans held for sale are carried at fair value under the provisions of the Fair Value Option Subsections of the ASC ("Fair Value Option"). Changes in the fair value of the loans held for sale are recognized in earnings and fees and costs associated with origination are recognized as incurred. The specific identification method is used to determine realized gains and losses on sales of loans, which are reported as net gains (losses) in noninterest income. Loans sold are subject to certain indemnification provisions with investors, including the repurchase of loans sold and repayment of certain sales proceeds to investors under certain conditions.

Loans

Originated Loans

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

Impaired loans include non-accrual loans, troubled debt restructurings and partially charged-off loans. The accrual of interest on impaired loans is discontinued when, in management's opinion, there is a clear indication that the borrower's cash flow may not be sufficient to meet principal and interest payments as they become due according to the terms of the loan agreement, which is generally when a loan is 90 days past due unless the loan is both well secured and in the process of collection. When a loan is placed on non-accrual status, all previously accrued and unpaid interest is charged against income. If the ultimate collectability of principal, wholly or partially, is in doubt, any payment received

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

1. Summary of Significant Accounting and Reporting Policies (Continued)

on a loan on which the accrual of interest has been suspended is applied to reduce principal to the extent necessary to eliminate such doubt. Once the collection of the remaining recorded loan balance is fully expected, interest income is recognized on a cash basis.

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

Acquired Loans

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

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

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

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

1. Summary of Significant Accounting and Reporting Policies (Continued)

continued use of key assumptions and estimates, similar to those used in the initial estimate of fair value.

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

Allowance for Loan Losses

Originated Loans

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

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

Acquired Loans

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

For PCI loans, cash flows expected to be collected are recast at each reporting date for each loan or pool. These evaluations require the continued use and updating of key assumptions and estimates such as default rates, loss severity given default and prepayment speed assumptions, similar to those used for the initial fair value estimate. Management judgment must be applied in developing these assumptions. If expected cash flows for a loan or pool decreases, an increase in the allowance for loan losses is made through a charge to the provision for loan losses. If expected cash flows for a loan

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

1. Summary of Significant Accounting and Reporting Policies (Continued)

increase, any previously established allowance for loan losses is reversed and any remaining difference increases the accretable yield which will be taken into income over the remaining life of the loan or pool.

Assets Segregated for Regulatory Purposes

Under certain conditions, FSC may be required to segregate cash and securities in a special reserve account for the benefit of customers under Rule 15c3-3 promulgated under the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Assets segregated under the provisions of the Exchange Act are not available for general corporate purposes. At December 31, 2013, FSC was not required to segregate cash and securities. FSC was required to segregate an aggregate of $19.0 million in cash and securities at December 31, 2012, which is included in other assets within the consolidated balance sheets.

FSC was not required to segregate cash or securities in a special reserve account for the benefit of proprietary accounts of introducing broker-dealers at December 31, 2013 and 2012.

Broker-Dealer and Clearing Organization Transactions

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

Insurance Premiums Receivable

Insurance premiums receivable include premiums written and not yet collected. NLC routinely evaluates the receivable balance to determine if an allowance for uncollectible amounts is necessary. At December 31, 2013 and 2012, NLC determined that no valuation allowance was necessary.

Deferred Policy Acquisition Costs

Costs of acquiring insurance vary with and are primarily related to the successful acquisition of new and renewal business, primarily consisting of commissions, premium taxes and underwriting expenses, and are deferred and amortized over the terms of the policies or reinsurance treaties to which they relate. Proceeds from reinsurance transactions that represent recovery of acquisition costs reduce applicable unamortized acquisition costs in such a manner that net acquisition costs are capitalized and charged to expense in proportion to net revenue recognized. Future investment income is considered in determining the recoverability of deferred policy acquisition costs. NLC regularly reviews the categories of acquisition costs that are deferred and assesses the recoverability of this asset. A premium deficiency and a corresponding charge to income is recognized if the sum of the expected loss and loss adjustment expenses, unamortized policy acquisition costs, and maintenance costs exceed

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

1. Summary of Significant Accounting and Reporting Policies (Continued)

related unearned insurance premiums and anticipated investment income. At December 31, 2013 and 2012, there was no premium deficiency.

Reinsurance

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

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

Premises and Equipment

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

FDIC Indemnification Asset

The Company has elected to account for the FDIC Indemnification Asset in accordance with FASB ASC 805. The FDIC Indemnification Asset is initially recorded at fair value, based on the discounted value of expected future cash flows under the loss-share agreements. The difference between the present value and the undiscounted cash flows the Company expects to collect from the FDIC will be accreted into noninterest income within the consolidated statements of operations over the life of the FDIC Indemnification Asset. The FDIC Indemnification Asset is reviewed quarterly and adjusted for any changes in expected cash flows based on recent performance and expectations for future performance of the covered portfolio. These adjustments are measured on the same basis as the related covered loans and covered OREO. Any increases in cash flow of the covered assets over those expected will reduce the FDIC Indemnification Asset and any decreases in cash flow of the covered assets under those expected will increase the FDIC Indemnification Asset. Any amortization of changes in value is limited to the contractual term of the loss-share agreements. Increases and decreases to the FDIC Indemnification Asset are recorded as adjustments to noninterest income within the consolidated statements of operations over the life of the loss-share agreements.

Covered Other Real Estate Owned

Acquired OREO subject to FDIC loss-share agreements is referred to as "covered OREO" and reported separately in the consolidated balance sheets. Covered OREO is reported exclusive of expected reimbursement cash flows from the FDIC. Foreclosed covered loan collateral is transferred

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

1. Summary of Significant Accounting and Reporting Policies (Continued)

into covered OREO at the collateral's fair value, less selling costs. Covered OREO was initially recorded at its estimated fair value based on similar market comparable valuations, less estimated selling costs. Subsequently, loan collateral transferred to OREO is recorded at its net realizable value. Any subsequent valuation adjustments due to declines in fair value of the covered OREO will be charged to noninterest expense, and will be partially offset by noninterest income representing the corresponding increase to the FDIC Indemnification Asset for loss reimbursements. Any recoveries of previous valuation decreases will be credited to noninterest expense with a corresponding charge to noninterest income for the portion of the recovery that is due to the FDIC.

Other Real Estate Owned

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

Debt Issuance Costs

The Company capitalizes debt issuance costs associated with financing of debt. These costs are amortized on a straight-line basis, which approximates the effective interest method, over the repayment term of the loans. Debt issuance costs of $2.3 million, $0.2 million and $0.4 million in 2013, 2012 and 2011 were amortized and included in interest expense within the consolidated statements of operations. In November 2013, the total remaining unamortized balance of $2.1 million was expensed as a result of the redemption of all outstanding 7.5% Senior Exchangeable Notes due 2025 ("the Notes"), as further described in Note 13 to the consolidated financial statements. In 2011, an additional $0.2 million of the unamortized balance was written down as a result of NLC purchasing $6.9 million of the Notes in the open market.

Goodwill

Goodwill, which represents the excess of cost over the fair value of the net assets acquired, is allocated to reporting units and tested for impairment annually, or whenever events or changes in circumstances indicate that the carrying amount should be assessed. The Company performs required annual impairment tests of its goodwill and other intangible assets as of October 1st for each of its reporting units. Prior to testing goodwill for impairment, the Company has the option to assess on a qualitative basis whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If determined, based on its assessment of qualitative factors that it is more likely than not that fair value of a reporting unit is less than its carrying amount, the Company will proceed to test goodwill for impairment as a part of a two-step process. First, the Company determines the fair value of a reporting unit and compares it to its carrying amount. Second, if the carrying amount of a reporting unit exceeds its fair value, an impairment loss is recognized for any excess of the carrying amount of the reporting unit's goodwill over the implied fair value of that goodwill. The implied fair value of goodwill is determined by allocating the fair value of the reporting unit in a manner similar to

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

1. Summary of Significant Accounting and Reporting Policies (Continued)

a purchase price allocation. The residual fair value after this allocation is the implied fair value of the reporting unit goodwill.

Intangibles and Other Long-Lived Assets

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

Mortgage Servicing Rights

The Company determines its classes of residential mortgage servicing assets based on the asset type being serviced along with the methods used to manage the risk inherent in the servicing assets, which includes the market inputs used to value the servicing assets. The Company measures its servicing assets at fair value and reports changes in fair value through earnings. Fair value adjustments that encompass market-driven valuation changes and the runoff in value that occurs from the passage of time are each separately reported.

Retained mortgage servicing rights ("MSR") are measured at fair value as of the date of sale of the related mortgage loan. Subsequent fair value measurements are determined using a discounted cash flow model. In order to determine the fair value of the MSR, the present value of expected future cash flows is estimated. Assumptions used include market discount rates, anticipated prepayment speeds, delinquency and foreclosure rates, and ancillary fee income.

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

Derivative Financial Instruments

The Company's hedging policies permit the use of various derivative financial instruments, including interest rate lock commitments ("IRLCs"), forward commitments and interest rate swaps, to manage interest rate risk or to hedge specified assets and liabilities. The IRLCs and forward

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

1. Summary of Significant Accounting and Reporting Policies (Continued)

commitments meet the definition of a derivative under the provisions of the Derivatives and Hedging Topic of the ASC.

Derivatives are recorded at fair value in the consolidated balance sheets. To qualify for hedge accounting, derivatives must be highly effective at reducing the risk associated with the exposure being hedged and must be designated as a hedge at the inception of the derivative contract. If derivative instruments are designated as hedges of fair values, the change in the fair value of both the derivative instrument and the hedged item are included in current earnings. Changes in the fair value of derivatives designated as hedges of cash flows are recorded in other comprehensive income (loss). Actual cash receipts and/or payments and related accruals on derivatives related to hedges are recorded as adjustments to the line item where the hedged item's effect on earnings is recorded.

Reserve for Losses and Loss Adjustment Expenses

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

Loss Contingencies

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

Stock-Based Compensation

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

Advertising

Advertising costs are expensed as incurred. Advertising expense totaled $5.3 million, $0.4 million and $34 thousand during 2013, 2012 and 2011, respectively.

Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recorded for the estimated future tax effects of the temporary difference between the tax basis and book basis of assets and liabilities reported in the accompanying consolidated balance sheets. The provision for income tax expense or benefit differs from the amounts of income taxes currently payable because certain items of income and expense included in the consolidated financial statements

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

1. Summary of Significant Accounting and Reporting Policies (Continued)

are recognized in different time periods by taxing authorities. Interest and penalties incurred related to tax matters are charged to other interest expense or other noninterest expense, respectively.

Benefits from uncertain tax positions are recognized in the consolidated financial statements only when it is more likely than not that the tax position will be sustained upon examination by the appropriate taxing authority having full knowledge of all relevant information. A tax position that meets the more-likely-than-not recognition threshold is measured at the largest amount of cumulative benefit that is greater than fifty percent likely of being realized upon ultimate settlement. Tax positions that previously failed to meet the more-likely-than-not recognition threshold are recognized in the reporting period in which that threshold is met. Previously recognized tax positions that no longer meet the more-likely-than-not recognition threshold are derecognized in the reporting period in which that threshold is no longer met. The Company has not recorded any significant liabilities for uncertain tax positions.

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

Cash Flow Reporting

For the purpose of presentation in the consolidated statements of cash flows, cash and cash equivalents are defined as the amount included in the consolidated balance sheets caption "Cash and due from banks" and the portion of the amount in the caption "Federal funds sold and securities purchased under agreements to resell" that represents federal funds sold. Cash equivalents have original maturities of three months or less.

Basic and Diluted Net Income (Loss) Per Share

Nonvested share-based payment awards that contain nonforfeitable rights to dividends or dividend equivalents are participating securities and are included in the computation of earnings per share pursuant to the two-class method prescribed by the Earnings Per Share Topic of the ASC. The two-class method is an earnings allocation formula that determines earnings per share for each class of common stock and participating security according to dividends declared (or accumulated) and participation rights in undistributed earnings. In May 2013, as discussed in Note 20 to the consolidated financial statements, Hilltop issued restricted stock awards which qualify as participating securities.

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

Diluted earnings per common share is computed in a similar manner, except that first the denominator is increased to include the number of additional common shares that would have been outstanding if potentially dilutive common shares, excluding the participating securities, were issued using the treasury stock method. For all periods presented, stock options and redemption of the Notes are the only potentially dilutive non-participating instruments issued by Hilltop. Next, we determine and include in the diluted earnings per common share calculation the more dilutive effect of the

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

1. Summary of Significant Accounting and Reporting Policies (Continued)

participating securities using the treasury stock method or the two-class method. Undistributed losses are not allocated to the nonvested share-based payment awards (the participating securities) under the two-class method as the holders are not contractually obligated to share in the losses of the Company.

2. Acquisitions

FNB Transaction

On the Bank Closing Date, the Bank assumed substantially all of the liabilities, including all of the deposits, and acquired substantially all of the assets of FNB from the FDIC in an FDIC-assisted transaction. As part of the P&A Agreement, the Bank and the FDIC entered into loss-share agreements covering future losses incurred on certain acquired loans and OREO. The Company refers to acquired commercial and single family residential loan portfolios and OREO that are subject to the loss-share agreements as "covered loans" and "covered OREO", respectively, and these assets are presented as separate line items in the Company's consolidated balance sheet. Collectively, covered loans and covered OREO are referred to as "covered assets". Pursuant to the loss-share agreements, the FDIC has agreed to reimburse the Bank the following amounts with respect to the covered assets pursuant to the loss-share agreements: (i) 80% of losses on the first $240.4 million of losses incurred; (ii) 0% of losses in excess of $240.4 million up to and including $365.7 million of losses incurred; and (iii) 80% of losses in excess of $365.7 million of losses incurred. The loss-share agreements for commercial and single family residential loans are in effect for 5 years and 10 years, respectively, from the Bank Closing Date and the loss recovery provisions to the FDIC are in effect for 8 years and 10 years, respectively, from the Bank Closing Date.

In accordance with the loss-share agreements, the Bank may be required to make a "true-up" payment to the FDIC approximately ten years following the Bank Closing Date if the FDIC's initial estimate of losses on covered assets is greater than the actual realized losses. The "true-up" payment is calculated using a defined formula set forth in the P&A Agreement.

The operations of FNB are included in the Company's operating results beginning September 14, 2013. For the period from September 14, 2013 through December 31, 2013, FNB's operations include net interest income of $32.0 million, other revenues of $20.4 million and net income of $18.5 million. Such operating results include a preliminary bargain purchase gain of $12.6 million, before taxes of $4.5 million, and are not necessarily indicative of future operating results. FNB's results of operations prior to the Bank Closing Date are not included in the Company's consolidated operating results.

Transaction-related expenses of $0.1 million associated with the FNB Transaction are included in noninterest expense within the consolidated statement of operations for the year ended December 31, 2013. Such expenses were for professional services and other incremental costs associated with the integration of FNB's operations.

The FNB Transaction was accounted for using the purchase method of accounting and, accordingly, purchased assets, including identifiable intangible assets and assumed liabilities, were recorded at their respective Bank Closing Date fair values using significant estimates and assumptions to value certain identifiable assets acquired and liabilities assumed. During the quarter ended December 31, 2013, the estimated fair values of certain identifiable assets acquired and liabilities assumed as of the Bank Closing Date were adjusted as a result of additional information obtained primarily related to the fair values of loans, covered OREO, FDIC Indemnification Asset, premises and

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

2. Acquisitions (Continued)

equipment and other intangible assets. Due to the short time period between the Bank Closing Date and December 31, 2013, the real estate appraisal validation exercise remains outstanding and the Bank Closing Date valuations related to covered OREO and FDIC Indemnification Asset are considered preliminary and could differ significantly when finalized. The amounts are also subject to adjustments based upon final settlement with the FDIC. The terms of the P&A Agreement provide for the FDIC to indemnify the Bank against claims with respect to liabilities and assets of FNB or any of its affiliates not assumed or otherwise purchased by the Bank and with respect to certain other claims by third parties.

A summary of the net assets received from the FDIC in the FNB Transaction and the estimated fair value adjustments resulting in the bargain purchase gain are presented below (in thousands).

Cost basis net assets on September 13, 2013	$ 215,000
Cash payment received from the FDIC	45,000
Fair value adjustments:	
Securities	(3,341)
Loans	(343,068)
Premises and equipment	3,565
Other real estate owned	(79,273)
FDIC indemnification asset	185,680
Other intangible assets	4,270
Deposits	(8,282)
Other	(6,966)
Bargain purchase gain	$ 12,585

In FDIC-assisted transactions, only certain assets and liabilities are transferred to the acquirer and, depending on the nature and amount of the acquirer's bid, the FDIC may be required to make a cash payment to the acquirer or the acquirer may be required to make a payment to the FDIC. In the FNB Transaction, cost basis net assets of $215.0 million and an initial cash payment received from the FDIC of $45.0 million were transferred to the Bank. This initial cash payment from the FDIC is subject to adjustment and settlement. The bargain purchase gain represents the excess of the estimated fair value of the assets acquired over the estimated fair value of the liabilities assumed.

The FDIC bid form provided a list of properties (branches and support facilities) owned by FNB for sale at fixed prices. The Bank purchased 44 properties owned by FNB in connection with its bid for an aggregate purchase price of $59.5 million. For those properties owned by FNB that the Bank declined to purchase in its bid, the Bank had exclusive options to purchase those properties following the Bank Closing Date. In connection with those options, the Bank purchased an additional seven properties owned by FNB, for an aggregate purchase price of $4.9 million. The Bank also had an option to assume the leases of properties leased by FNB. The Bank was required to purchase all data management equipment and, other certain special assets, furniture, fixtures and equipment, in each case at an appraised value at any properties purchased or leased by the Bank. The Bank paid $10.3 million to the FDIC for furniture, fixtures and data management equipment. The Bank is required to pay rent to the FDIC on properties owned or leased by FNB and furniture and equipment at such properties until it surrenders such properties to the FDIC.

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

2. Acquisitions (Continued)

The resulting fair values of the identifiable assets acquired, and liabilities assumed, of FNB at September 13, 2013 are summarized in the following table (in thousands).

Cash and due from banks	$	362,695
Securities		286,214
Non-covered loans		42,884
Covered loans		1,116,583
Premises and equipment		78,399
FDIC indemnification asset		185,680
Covered other real estate owned		135,187
Other assets		26,300
Other intangible assets		4,270
Total identifiable assets acquired		2,238,212
Deposits		(2,211,740)
Other liabilities		(13,887)
Total liabilities assumed		(2,225,627)
Net identifiable assets acquired/bargain purchase gain	$	12,585

The Bank acquired loans both with and without evidence of credit quality deterioration since origination. Based on purchase date valuations, the Bank's portfolio of acquired loans had a fair value of $1.2 billion as of the Bank Closing Date, with no carryover of any allowance for loan losses. Acquired loans were segregated between those considered to be PCI loans and those without credit impairment at acquisition. The following table presents details on acquired loans at the Bank Closing Date (in thousands).

	Loans, excluding PCI Loans	PCI Loans	Total Loans
Commercial and industrial	$ 47,874	$ 47,751	$ 95,625
Real estate	242,998	611,219	854,217
Construction and land development	26,669	158,247	184,916
Consumer	19,095	5,614	24,709
Total	$ 336,636	$ 822,831	$ 1,159,467

The following table presents information about the acquired PCI loans at the Bank Closing Date (in thousands).

Contractually required principal and interest payments	$	1,533,667
Nonaccretable difference		542,241
Cash flows expected to be collected		991,426
Accretable difference		168,595
Fair value of loans acquired with a deterioration of credit quality	$	822,831

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

2. Acquisitions (Continued)

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

Contractually required principal and interest payments	$ 466,754
Contractual cash flows not expected to be collected	43,783
Fair value at acquisition	336,636

PlainsCapital Merger

After the close of business on November 30, 2012, Hilltop acquired PlainsCapital Corporation in a stock and cash transaction. PlainsCapital Corporation merged with and into a wholly owned subsidiary, which continued as the surviving entity under the name "PlainsCapital Corporation". Based on Hilltop's closing stock price on November 30, 2012, the total purchase price was $813.5 million, consisting of 27.1 million shares of common stock, $311.8 million in cash and the issuance of 114,068 shares of Hilltop Non-Cumulative Perpetual Preferred Stock, Series B (the "Hilltop Series B Preferred Stock") in exchange on a one-for-one basis for the outstanding shares of PlainsCapital Non-Cumulative Perpetual Preferred Stock, Series C, all of which were held by the United States Department of the Treasury (the "U.S. Treasury"). The fair value of assets acquired, excluding goodwill, totaled $6.5 billion, including $3.2 billion of loans, $730.8 million of investment securities and $70.7 million of identifiable intangibles. The fair value of the liabilities assumed was $5.9 billion, including $4.5 billion of deposits.

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

Fair value of consideration paid:	
Common stock issued	$ 387,584
Preferred stock issued	114,068
Cash	311,805
Total consideration paid	$ 813,457

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

2. Acquisitions (Continued)

The resulting fair values of the identifiable assets acquired, and liabilities assumed, of PlainsCapital at December 1, 2012 are summarized in the following table (in thousands).

Cash and due from banks	$	393,132
Federal funds sold and securities purchased agreements to resell		84,352
Securities		730,779
Loans held for sale		1,520,833
Loans, net		3,195,309
Broker-dealer and clearing organization receivables		149,457
Premises and equipment		96,886
Other intangible assets		70,650
Other assets		241,876
Total identifiable assets acquired		6,483,274
Deposits		4,463,069
Broker-dealer and clearing organization payables		263,894
Short-term borrowings		914,062
Notes payable		10,855
Junior subordinated debentures		67,012
Other liabilities		180,998
Total liabilities assumed		5,899,890
Net identifiable assets acquired		583,384
Goodwill resulting from the acquisition		230,073
Net assets acquired	$	813,457

For further information regarding goodwill recorded in connection with the PlainsCapital Merger, refer to Note 9, Goodwill and Other Intangible Assets.

Expenses of $6.6 million associated with the PlainsCapital Merger are included in noninterest expense within the consolidated statement of operations for 2012. Such expenses were for professional services and other incremental costs associated with the integration of PlainsCapital's operations.

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

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

2. Acquisitions (Continued)

those considered to be PCI loans and those without credit impairment at acquisition. The following table presents details on acquired loans at the acquisition date (in thousands).

	Loans, excluding PCI Loans	PCI Loans	Total Loans
Commercial and industrial	$ 1,684,706	$ 74,911	$ 1,759,617
Real estate	1,077,295	63,866	1,141,161
Construction and land development	232,313	34,008	266,321
Consumer	28,131	79	28,210
Total	$ 3,022,445	$ 172,864	$ 3,195,309

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

Contractually required principal and interest payments	$ 252,818
Nonaccretable difference	61,527
Cash flows expected to be collected	191,291
Accretable difference	18,427
Fair value of loans acquired with a deterioration of credit quality	$ 172,864

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

Contractually required principal and interest payments	$ 3,498,554
Contractual cash flows not expected to be collected	92,526
Fair value at acquisition	3,022,445

Pro Forma Results of Operations

The purchase of assets and assumption of certain liabilities of FNB from the FDIC, as receiver, was significant at a level to require disclosure of historical financial statements and related pro forma financial disclosure. An essential part of the transaction is the federal financial assistance governed by the P&A Agreement with the FDIC, which is not reflective of the previous operations of FNB. The nature and magnitude of the FNB Transaction, coupled with the federal assistance, substantially reduces the relevance of historical financial information of FNB when considering the assessment of the historical financial information relative to future operations. Because the Company believes that the continuity of FNB's historical operations is substantially lacking after the FNB Transaction and pro forma information is not reasonably available, the Company has omitted certain historical financial information and the related pro forma financial information of FNB pursuant to the guidance provided in Staff Accounting Bulletin Topic 1.K, Financial Statements of Acquired Troubled Financial Institutions ("SAB 1:K"), and a request for relief granted by the SEC. SAB 1:K provides relief from the requirements of Rule 3-05 of Regulation S-X in certain instances, such as the FNB Transaction, where a registrant engages in an acquisition of a significant amount of assets of a troubled financial institution that involves pervasive federal assistance and audited financial statements of the troubled

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

2. Acquisitions (Continued)

financial institution are not reasonably available. Therefore, no additional historical pro forma information regarding FNB is provided below.

The results of operations acquired in the PlainsCapital Merger have been included in the Company's consolidated financial results since December 1, 2012. The following table discloses the impact of PlainsCapital (excluding the impact of acquisition-related merger and restructuring charges discussed below) since the acquisition date through December 31, 2012.

The table also presents pro forma results had the PlainsCapital Merger taken place on January 1, 2011 (in thousands), and includes the estimated impact of purchase accounting adjustments. The purchase accounting adjustments reflect the impact of recording the acquired loans at fair value, including the estimated accretion of the purchase discount on the loan portfolio. Accretion estimates were based on the acquisition date purchase discount on the loan portfolio, as it was not practicable to determine the amount of discount that would have been recorded based on economic conditions that existed on January 1, 2011. The pro forma results do not include any potential operating cost savings as a result of the PlainsCapital Merger. Further, certain costs associated with any restructuring or integration activities are also not reflected in the pro forma results. Pro forma results include any acquisition-related merger and restructuring charges incurred during the period. The pro forma results are not indicative of what would have occurred had the PlainsCapital Merger taken place on the indicated date.

	PlainsCapital Acquisition Date through December 31,	Pro Forma Combined Twelve Months Ended December 31,	
	2012	**2012**	**2011**
Net interest income	$ 24,029	$ 221,635	$ 225,436
Other revenues	70,085	901,347	616,582
Net income	8,361	75,138	63,067

3. Fair Value Measurements

Fair Value Measurements and Disclosures

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

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

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

3. Fair Value Measurements (Continued)

Level 1 Inputs: Unadjusted quoted prices in active markets for identical assets or liabilities that the Company can access at the measurement date.

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

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

Fair Value Option

The Company has elected to measure substantially all of PrimeLending's mortgage loans held for sale at fair value and MSR, and certain time deposits at the Bank under the provisions of the Fair Value Option. The Company elected to apply the provisions of the Fair Value Option to these items so that it would have the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. The Company determines the fair value of the financial instruments accounted for under the provisions of the Fair Value Option in compliance with the provisions of the Fair Value Topic of the ASC discussed above.

At December 31, 2013, the aggregate fair value of PrimeLending's mortgage loans held for sale accounted for under the Fair Value Option was $1.09 billion, and the unpaid principal balance of those loans was $1.07 billion. At December 31, 2012, the aggregate fair value of PrimeLending's mortgage loans held for sale accounted for under the Fair Value Option was $1.40 billion, and the unpaid principal balance of those loans was $1.36 billion. The interest component of fair value is reported as interest income on loans in the accompanying consolidated statements of operations.

The Company holds a number of financial instruments that are measured at fair value on a recurring basis, either by the application of the Fair Value Option or other authoritative pronouncements. The fair values of those instruments are determined primarily using Level 2 inputs, as further described below. Those inputs include quotes from mortgage loan investors and derivatives dealers, data from independent pricing services and rates paid in the brokered certificate of deposit market.

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

Available For Sale Securities Most securities available for sale are reported at fair value using Level 2 inputs. The Company obtains fair value measurements from independent pricing services. As the Company is responsible for the determination of fair value, control processes are designed to ensure that the fair values received from independent pricing services are reasonable and the valuation techniques and assumptions used appear reasonable and consistent with prevailing market conditions. The fair value measurements consider observable data that may include dealer quotes, market spreads,

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

3. Fair Value Measurements (Continued)

cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the financial instruments' terms and conditions, among other things. For public common and preferred equity stocks, the determination of fair value uses Level 1 inputs based on observable market transactions. Regarding the note receivable and warrants, the determination of fair value uses Level 3 inputs such as internal or external fund manager valuations based on unobservable inputs including recent filings, operating results, balance sheet stability, growth and other business and market sector fundamentals.

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

Loans Held for Sale Mortgage loans held for sale are reported at fair value, as discussed above, using Level 2 inputs that consist of commitments on hand from investors or prevailing market prices. These instruments are held for relatively short periods, typically no more than 30 days. As a result, changes in instrument-specific credit risk are not a significant component of the change in fair value. Mortgage loans that are non-performing, including monitored loans, are reported at fair value using Level 3 inputs. These loans were previously valued using Level 2 inputs. However, refinements made during 2013 to the fair value inputs for these loans resulted in the use of significant unobservable inputs.

Deposits As discussed previously, certain time deposits are reported at fair value by virtue of an election under the provisions of Fair Value Option. Fair values are determined using Level 2 inputs that consist of observable rates paid on instruments of the same tenor in the brokered certificate of deposit market.

Derivatives Derivatives are reported at fair value using either Level 2 or Level 3 inputs. PlainsCapital uses dealer quotes to determine the fair value of interest rate swaps used to hedge time deposits. PrimeLending and FSC use dealer quotes to value forward purchase commitments and forward sale commitments, respectively, executed for both hedging and non-hedging purposes. PrimeLending also issues IRLCs to its customers and FSC issues forward purchase commitments to its clients that are valued based on the change in the fair value of the underlying mortgage loan from inception of the IRLC or purchase commitment to the balance sheet date, adjusted for projected loan closing rates. PrimeLending determines the value of the underlying mortgage loan as discussed in "Loans Held for Sale", above. FSC determines the value of the underlying mortgage loan from prices of comparable securities used to value forward sale commitments. Additionally, First Southwest entered into a derivative option agreement ("Fee Award Option").

Mortgage servicing asset The mortgage servicing asset is reported at fair value using Level 3 inputs. Fair value is determined by projecting net servicing cash flows, which are then discounted to estimate the fair value. The fair value of the mortgage servicing asset is impacted by a variety of factors, including prepayment assumptions, discount rates, delinquency rates, contractually specified servicing fees, servicing costs and underlying portfolio characteristics.

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

3. Fair Value Measurements (Continued)

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

December 31, 2013	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
Cash and cash equivalents	$ 746,023	$	$	$ 746,023
Trading securities	33	58,813		58,846
Available for sale securities	22,079	1,121,011	60,053	1,203,143
Loans held for sale		1,061,310	27,729	1,089,039
Derivative assets		23,564		23,564
Mortgage servicing asset			20,149	20,149
Trading liabilities		46		46
Derivative liabilities		139	5,600	5,739

December 31, 2012	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
Cash and cash equivalents	$ 726,460	$	$	726,460
Trading securities		90,113		90,113
Available for sale securities	20,428	914,248	56,277	990,953
Loans held for sale		1,400,737		1,400,737
Derivative assets		15,697		15,697
Mortgage servicing asset			2,080	2,080
Time deposits		1,073		1,073
Trading liabilities		3,164		3,164
Derivative liabilities		1,080	4,490	5,570

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

3. Fair Value Measurements (Continued)

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

	Balance at Beginning of Period	Purchases	Sales	Transfers into Level 3	Total Gains or Losses (Realized or Unrealized) Included in Net Income (Loss)	Included in Other Comprehensive Income (Loss)	Balance at End of Period
Year ended December 31, 2013							
Available for sale securities	$ 56,277	$	$	$	$ 2,166	$ 1,610	$ 60,053
Loans held for sale				27,729			27,729
Mortgage servicing asset	2,080	13,886			4,183		20,149
Derivative liabilities	(4,490)				(1,110)		(5,600)
Total	$ 53,867	$ 13,886	$	$ 27,729	$ 5,239	$ 1,610	$ 102,331
Year ended December 31, 2012							
Available for sale securities	$ 60,377	$	$	$	$ 1,867	$ (5,967)	$ 56,277
Mortgage servicing asset		1,890			190		2,080
Derivative liabilities		(4,455)			(35)		(4,490)
Total	$ 60,377	$ (2,565)	$	$	$ 2,022	$ (5,967)	$ 53,867
Year ended December 31, 2011							
Available for sale securities	$	$ 50,000	$	$	$ 709	$ 9,668	$ 60,377
Total	$	$ 50,000	$	$	$ 709	$ 9,668	$ 60,377

All net unrealized gains (losses) in the table above are reflected in the accompanying consolidated financial statements. The unrealized gains (losses) relate to financial instruments still held at December 31, 2013. The available for sale securities noted in the table above reflect

Hilltop's note receivable and warrant to purchase common stock of SWS Group, Inc. ("SWS") as discussed in Note 4 to the consolidated financial statements.

Hilltop's note receivable is valued using a cash flow model that estimates yield based on comparable securities in the market. The interest rate used to discount cash flows is the most significant unobservable input. An increase or decrease in the discount rate would result in a corresponding decrease or increase, respectively, in the fair value measurement of the note receivable.

The warrant is valued utilizing a binomial model. The underlying SWS common stock price and its related volatility, an unobservable input, are the most significant inputs into the model, and, therefore, decreases or increases to the SWS common stock price would result in a significant change in the fair value measurement of the warrant.

Loans held for sale, including monitored mortgage loans, are valued using commitments on hand from investors or prevailing market prices.

The mortgage servicing asset is valued by projecting net servicing cash flows, which are then discounted to estimate the fair value. The fair value of the mortgage servicing asset is impacted by a

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

3. Fair Value Measurements (Continued)

variety of factors, including prepayment assumptions, discount rates, delinquency rates, contractually specified servicing fees, servicing costs and underlying portfolio characteristics.

Derivative liabilities in the tables above include a Fee Award Option valued using discounted cash flows and probability of exercise.

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

The following table presents the changes in fair value for instruments that are reported at fair value under the Fair Value Option (in thousands).

Changes in Fair Value for Assets and Liabilities Reported at Fair Value under Fair Value Option

	Year Ended December 31, 2013			Year Ended December 31, 2012		
	Net Gains (Losses) from Sale of Loans	Other Noninterest Income	Total Changes in Fair Value	Net Gains (Losses) from Sale of Loans	Other Noninterest Income	Total Changes in Fair Value
Loans held for sale	$ (19,353)	$	$ (19,353)	$ (3,297)	$	$ (3,297)
Mortgage servicing asset	18,069		18,069	190		190
Time deposits		12	12		7	7

The Company also determines the fair value of certain assets and liabilities on a non-recurring basis. In particular, the fair value of all of the assets and liabilities purchased in the PlainsCapital Merger was determined at the acquisition date, while fair value of all assets acquired and liabilities assumed in the FNB Transaction was determined at the Bank Closing Date. In addition, facts and circumstances may dictate a fair value measurement when there is evidence of impairment. Assets and liabilities measured on a non-recurring basis include the items discussed below.

Impaired Loans The Company reports impaired loans based on the underlying fair value of the collateral through specific allowances within the allowance for loan losses. The Company acquired PCI loans with a fair value of $172.9 million and $822.8 million upon completion of the PlainsCapital Merger and the FNB Transaction, respectively. Substantially all PCI loans acquired in the FNB Transaction are covered by FDIC loss-share agreements. The fair value of PCI loans was determined using Level 3 inputs, including estimates of expected cash flows that incorporated assumptions regarding default rates, loss severity rates assuming default, prepayment speeds and estimated collateral values. At December 31, 2013, non-covered PCI loans with a carrying amount of $100.4 million had been reduced by specific allowances within the allowance for non-covered loan losses of $3.1 million, resulting in a reported value of $97.3 million that approximates fair value. At December 31, 2013, covered PCI loans with a carrying amount of $729.2 million had been reduced by specific allowances within the allowance for covered loan losses of $0.9 million, resulting in a reported value of $728.3 million.

Other Real Estate Owned The Company reports OREO at fair value less estimated cost to sell. Any excess of recorded investment over fair value, less cost to sell, is charged against the allowance for loan losses when property is initially transferred to OREO. Subsequent to the initial transfer to OREO, downward valuation adjustments are charged against earnings. The Company determines fair value primarily using independent appraisals of OREO properties. The resulting fair value measurements are classified as Level 2 or Level 3 inputs, depending upon the extent to which unobservable inputs determine the fair value measurement. The Company considers a number of factors in determining the

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

3. Fair Value Measurements (Continued)

extent to which specific fair value measurements utilize unobservable inputs, including, but not limited to, the inherent subjectivity in appraisals, the length of time elapsed since the receipt of independent market price or appraised value, and current market conditions. In the FNB Transaction, the Bank acquired OREO of $135.2 million, all of which is covered by an FDIC loss-share agreement. At December 31, 2013, the estimated fair value of covered OREO was $142.8 million, and the underlying fair value measurements utilize Level 3 inputs. The fair value of non-covered OREO at December 31, 2013 and 2012 was $4.8 million and $11.1 million, respectively, and is included in other assets within the consolidated balance sheets. During the reported periods, all fair value measurements for non-covered OREO utilized Level 2 inputs.

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

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

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

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

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

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

3. Fair Value Measurements (Continued)

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

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

Short-Term Borrowings The carrying amounts of federal funds purchased, borrowings under repurchase agreements and other short-term borrowings approximate their fair values.

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

The following table presents the carrying values and estimated fair values of financial instruments (in thousands).

		Estimated Fair Value			
December 31, 2013	**Carrying Amount**	**Level 1 Inputs**	**Level 2 Inputs**	**Level 3 Inputs**	**Total**
Financial assets:					
Non-covered loans, net	$ 3,481,405	$	$ 281,712	$ 3,119,319	$ 3,401,031
Covered loans, net	1,005,308			997,371	997,371
Broker-dealer and clearing organization receivables	119,317		119,317		119,317
FDIC indemnification asset	188,291			188,291	188,291
Other assets	66,055		43,946	22,109	66,055
Financial liabilities:					
Deposits	6,722,019		6,722,909		6,722,909
Broker-dealer and clearing organization payables	129,678		129,678		129,678
Short-term borrowings	342,087		342,087		342,087
Debt	123,339		114,671		114,671
Other liabilities	3,362		3,362		3,362

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

3. Fair Value Measurements (Continued)

		Estimated Fair Value			
December 31, 2012	**Carrying Amount**	**Level 1 Inputs**	**Level 2 Inputs**	**Level 3 Inputs**	**Total**
Financial assets:					
Non-covered loans, net	$ 3,148,987	$	$	$ 3,148,987	$ 3,148,987
Broker-dealer and clearing organization receivables	145,564		145,564		145,564
Other assets	59,094		59,094		59,094
Financial liabilities:					
Deposits	4,700,461		4,698,848		4,698,848
Broker-dealer and clearing organization payables	187,990		187,990		187,990
Short-term borrowings	728,250		728,250		728,250
Debt	208,551		217,092		217,092
Other liabilities	4,400		4,400		4,400

The deferred income amounts arising from unrecognized financial instruments are not significant. These financial instruments also have contractual interest rates at or above current market rates. Therefore, no fair value disclosure is provided for these items.

4. Securities

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

December 31, 2013	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**
U.S. Treasury securities	$ 43,684	$ 82	$ (238)	$ 43,528
U.S. government agencies:				
Bonds	717,909	550	(55,727)	662,732
Residential mortgage-backed securities	59,936	735	(584)	60,087
Collateralized mortgage obligations	124,502	349	(4,390)	120,461
Corporate debt securities	72,376	4,610	(378)	76,608
States and political subdivisions	162,955	388	(6,508)	156,835
Commercial mortgage-backed securities	691	69		760
Equity securities	20,067	2,012		22,079
Note receivable	42,674	5,235		47,909
Warrant	12,068	76		12,144
Totals	$ 1,256,862	$ 14,106	$ (67,825)	$ 1,203,143

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

4. Securities (Continued)

December 31, 2012	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury securities	$ 7,046	$ 141	$ (2)	$ 7,185
U.S. government agencies:				
Bonds	524,888	1,663	(314)	526,237
Residential mortgage-backed securities	18,473	490	(70)	18,893
Collateralized mortgage obligations	97,812	191	(79)	97,924
Corporate debt securities	79,716	7,461		87,177
States and political subdivisions	177,701	196	(2,138)	175,759
Commercial mortgage-backed securities	1,001	72		1,073
Equity securities	19,289	1,139		20,428
Note receivable	40,508	3,652		44,160
Warrant	12,068	49		12,117
Totals	$ 978,502	$ 15,054	$ (2,603)	$ 990,953

Available for sale equity securities includes 1,475,387 shares of SWS common stock, a $50.0 million aggregate principal amount note issued by SWS and a warrant to purchase 8,695,652 shares of SWS common stock. SWS issued the note in July 2011 under a credit agreement pursuant to a senior unsecured loan from Hilltop. The note bears interest at a rate of 8.0% per annum, is prepayable by SWS subject to certain conditions after three years, and has a maturity of five years. The warrant provides for the purchase of 8,695,652 shares of SWS common stock at an exercise price of $5.75 per share, subject to anti-dilution adjustments. If the warrant was fully exercised, Hilltop would beneficially own 24.4% of SWS.

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

4. Securities (Continued)

Information regarding available for sale securities that were in an unrealized loss position is shown in the following table (dollars in thousands).

	December 31, 2013			December 31, 2012		
	Number of Securities	Fair Value	Unrealized Losses	Number of Securities	Fair Value	Unrealized Losses
U.S. treasury securities:						
Unrealized loss for less than twelve months	6	$ 12,748	$ 238	2	$ 2,427	$ 2
Unrealized loss for twelve months or longer						
	6	12,748	238	2	2,427	2
U.S. government agencies:						
Bonds:						
Unrealized loss for less than twelve months	35	526,817	45,274	14	236,305	314
Unrealized loss for twelve months or longer	5	90,931	10,453			
	40	617,748	55,727	14	236,305	314
Residential mortgage-backed securities:						
Unrealized loss for less than twelve months	2	2,194	54	7	12,279	70
Unrealized loss for twelve months or longer	3	9,309	530			
	5	11,503	584	7	12,279	70
Collateralized mortgage obligations:						
Unrealized loss for less than twelve months	7	84,054	4,320	8	38,887	79
Unrealized loss for twelve months or longer	2	4,995	70			
	9	89,049	4,390	8	38,887	79
Corporate debt securities:						
Unrealized loss for less than twelve months	7	10,754	378			
Unrealized loss for twelve months or longer						
	7	10,754	378			
States and political subdivisions:						
Unrealized loss for less than twelve months	46	30,245	669	225	156,664	2,138
Unrealized loss for twelve months or longer	150	96,882	5,839			

	196		127,127		6,508	225		156,664		2,138
Total available for sale:										
Unrealized loss for less than twelve months	103		666,812		50,933	256		446,562		2,603
Unrealized loss for twelve months or longer	160		202,117		16,892					
	263	$	868,929	$	67,825	256	$	446,562	$	2,603

During 2013, 2012 and 2011, the Company did not record any other-than-temporary impairments. While all of the investments are monitored for potential other-than-temporary impairment, the Company's analysis and experience indicate that these available for sale investments generally do not present a great risk of other-than-temporary-impairment, as fair value should recover over time. Factors considered in the Company's analysis include the reasons for the unrealized loss position, the severity and duration of the unrealized loss position, credit worthiness, and forecasted performance of the investee. While some of the securities held in the investment portfolio have decreased in value since the date of acquisition, the severity of loss and the duration of the loss position are not believed to be significant enough to warrant other-than-temporary impairment of the securities. The Company does not intend, nor is it likely that the Company will be required, to sell these securities before the recovery of the cost basis. Therefore, management does not believe any other-than-temporary impairments exist at December 31, 2013.

Expected maturities may differ from contractual maturities because certain borrowers may have the right to call or prepay obligations with or without penalties. The amortized cost and fair value of

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

4. Securities (Continued)

securities, excluding trading and available for sale equity securities and the available for sale warrant, at December 31, 2013 are shown by contractual maturity below (in thousands).

	Amortized Cost	Fair Value
Due in one year or less	$ 125,804	$ 125,881
Due after one year through five years	115,950	125,245
Due after five years through ten years	70,173	70,280
Due after ten years	727,671	666,206
	1,039,598	987,612
Residential mortgage-backed securities	59,936	60,087
Collateralized mortgage obligations	124,502	120,461
Commercial mortgage-backed securities	691	760
	$ 1,224,727	$ 1,168,920

The Company realized net losses from its trading securities portfolio of $2.8 million and $0.7 million during the year ended December 31, 2013 and the month of December 31, 2012, respectively, which are recorded as a component of other noninterest income within the consolidated statements of operations.

Securities with a carrying amount of $1.0 billion and $635.2 million (with a fair value of $938.1 million and $633.4 million) at December 31, 2013 and 2012, respectively, were pledged to secure public and trust deposits, federal funds purchased and securities sold under agreements to repurchase, and for other purposes as required or permitted by law.

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

At December 31, 2013 and 2012, NLC had investments on deposit in custody for various state insurance departments with carrying values of $9.4 million and $9.3 million, respectively.

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

Non-covered loans refer to loans not covered by the FDIC loss-share agreements. The non-covered loan portfolio at December 31, 2013 includes loans acquired as a part of the FNB Transaction totaling $53.4 million, of which $7.2 million are categorized as non-covered PCI loans. Covered loans are

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

5. Non-Covered Loans and Allowance for Non-Covered Loan Losses (Continued)

discussed in Note 6 to the consolidated financial statements. Non-covered loans summarized by portfolio segment are as follows (in thousands).

	December 31, 2013	December 31, 2012
Commercial and industrial	$ 1,637,266	$ 1,660,293
Real estate	1,457,253	1,184,914
Construction and land development	364,551	280,483
Consumer	55,576	26,706
	3,514,646	3,152,396
Allowance for non-covered loan losses	(33,241)	(3,409)
Total non-covered loans, net of allowance	$ 3,481,405	$ 3,148,987

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

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

The Bank maintains a loan review department that reviews credit risk in response to both external and internal factors that potentially impact the performance of either individual loans or the overall loan portfolio. The loan review process reviews the creditworthiness of borrowers and determines compliance with the loan policy. The loan review process complements and reinforces the risk identification and assessment decisions made by lenders and credit personnel. Results of these reviews are presented to management and the Bank's Board of Directors.

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

5. Non-Covered Loans and Allowance for Non-Covered Loan Losses (Continued)

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

	December 31,	
	2013	2012
Carrying amount	$ 100,392	$ 166,780
Outstanding balance	141,983	222,674

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

	Year Ended December 31, 2013	Month Ended December 31, 2012
Balance, beginning of period	$ 17,553	$ 18,427
Additions	622	
Increases in expected cash flows	18,793	
Disposals of loans	(3,692)	(22)
Accretion	(15,675)	(852)
Balance, end of period	$ 17,601	$ 17,553

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

Non-covered PCI loans are summarized by class in the following tables (in thousands). In addition to the non-covered PCI loans, there were $4.1 million of additional non-covered impaired loans at December 31, 2013. There were no impaired loans at December 31, 2012 other than PCI loans.

December 31, 2013	Unpaid Contractual Principal Balance	Recorded Investment with No Allowance	Recorded Investment with Allowance	Total Recorded Investment	Related Allowance
Commercial and industrial:					
Secured	$ 60,309	$ 19,280	$ 16,092	$ 35,372	$ 2,705
Unsecured	11,772	240	1,204	1,444	15
Real estate:					
Secured by commercial properties	49,306	20,185	16,070	36,255	339
Secured by residential properties	5,013	1,347	1,648	2,995	39
Construction and land development:					
Residential construction loans	33				
Commercial construction loans and land development	48,515	15,225	4,592	19,817	39
Consumer	7,946	4,509		4,509	

	$ 182,894	$ 60,786	$ 39,606	$ 100,392	$ 3,137

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

5. Non-Covered Loans and Allowance for Non-Covered Loan Losses (Continued)

December 31, 2012	**Unpaid Contractual Principal Balance**	**Recorded Investment with No Allowance**	**Recorded Investment with Allowance**	**Total Recorded Investment**
Commercial and industrial:				
Secured	$ 102,642	$ 67,967	$	$ 67,967
Unsecured	17,133	3,419		3,419
Real estate:				
Secured by commercial properties	70,284	55,519		55,519
Secured by residential properties	10,164	6,728		6,728
Construction and land development:				
Residential construction loans	1,137	708		708
Commercial construction loans and land development	60,425	32,362		32,362
Consumer	92	77		77
	$ 261,877	$ 166,780	$	$ 166,780

Average investment in non-covered PCI loans for the year ended December 31, 2013 is summarized by class in the following table (in thousands).

Commercial and industrial:	
Secured	$ 51,670
Unsecured	2,432
Real estate:	
Secured by commercial properties	45,887
Secured by residential properties	4,862
Construction and land development:	
Residential construction loans	354
Commercial construction loans and land development	26,090
Consumer	2,293
	$ 133,588

Non-covered non-accrual loans at December 31, 2013, excluding those classified as held for sale, are summarized by class in the following table (in thousands).

Commercial and industrial:	
Secured	$ 15,430
Unsecured	1,300

Real estate:	
Secured by commercial properties	2,638
Secured by residential properties	398
Construction and land development:	
Residential construction loans	
Commercial construction loans and land development	112
Consumer	
	$ 19,878

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

5. Non-Covered Loans and Allowance for Non-Covered Loan Losses (Continued)

At December 31, 2013, non-covered non-accrual loans included non-covered PCI loans of $15.8 million for which discount accretion has been suspended because the extent and timing of cash flows from these non-covered PCI loans can no longer be reasonably estimated. All non-covered PCI loans at December 31, 2012 were considered to be performing due to the application of the accretion method. In addition to the non-covered non-accrual loans in the table above, $3.5 million and $1.8 million of real estate loans secured by residential properties and classified as held for sale were in non-accrual status at December 31, 2013 and 2012, respectively.

Interest income recorded on accruing impaired loans was $17.7 million and $0.9 million for the year ended December 31, 2013 and the month ended December 31, 2012, respectively. Interest income recorded on non-accrual loans in 2013 and 2012 was nominal.

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

Information regarding TDRs granted is shown in the following table (in thousands). All TDRs granted relate to non-covered PCI loans. There were no TDRs granted during the month ended December 31, 2012. At December 31, 2013, the Bank had $0.5 million in unadvanced commitments to borrowers whose loans have been restructured in TDRs.

	Recorded Investment in Loans Modified by			
Year ended December 31, 2013	**A/B Note**	**Interest Rate Adjustment**	**Payment Term Extension**	**Total Modification**
Commercial and industrial:				
Secured	$	$	$ 10,390	$ 10,390
Unsecured				
Real estate:				
Secured by commercial properties			279	279
Secured by residential properties			777	777
Construction and land development:				
Residential construction loans				
Commercial construction loans and land development				
Consumer				
	$	$	$ 11,446	$ 11,446

Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

5. Non-Covered Loans and Allowance for Non-Covered Loan Losses (Continued)

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

December 31, 2013	Loans Past Due 30 - 59 Days	Loans Past Due 60 - 89 Days	Loans Past Due 90 Days or More	Total Past Due Loans	Current Loans	PCI Loans	Total Loans	Accruing Loans Past Due 90 Days or More
Commercial and industrial:								
Secured	$ 2,171	$ 277	$ 1,354	$ 3,802	$ 1,492,793	$ 35,372	$ 1,531,967	$ 272
Unsecured	333	9	60	402	103,453	1,444	105,299	59
Real estate:								
Secured by commercial properties	192		132	324	1,044,437	36,255	1,081,016	
Secured by residential properties	1,045	36	203	1,284	371,958	2,995	376,237	203
Construction and land development:								
Residential construction loans	415			415	64,664		65,079	
Commercial construction loans and land development	41	881	112	1,034	278,621	19,817	299,472	
Consumer	201	60		261	50,806	4,509	55,576	
	$ 4,398	$ 1,263	$ 1,861	$ 7,522	$ 3,406,732	$ 100,392	$ 3,514,646	$ 534

December 31, 2012	Loans Past Due 30 - 59 Days	Loans Past Due 60 - 89 Days	Loans Past Due 90 Days or More	Total Past Due Loans	Current Loans	PCI Loans	Total Loans	Accruing Loans Past Due 90 Days or More
Commercial and industrial:								