

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
WASHINGTON, DC 20549

**FORM 10-K**

☒ **ANNUAL REPORT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2023

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_.

**Commission File Number: 001-38910**

**TECTONIC FINANCIAL, INC.**

(Exact name of registrant as specified in its charter)

Texas  
State or other jurisdiction of incorporation or organization

82-0764846  
(I.R.S. Employer Identification Number)

16200 Dallas Parkway, Suite 190, Dallas, Texas 75248  
(Address of principal executive offices)

75248  
(ZIP Code)

Registrant's telephone number, including area code: (972) 720-9000

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Series B preferred stock, \$0.01 par value per share	TECTP	The Nasdaq Stock Market, LLC

Securities registered pursuant to Section 12(g) of the Act: **None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☐ No ☒

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ☐ No ☒

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

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

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

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

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

Indicate by check mark whether the registrant has filed a report on and attestation to its management’s assessment of the effectiveness of its internal control over financial reporting under Section 404(b) of the Sarbanes-Oxley Act (15 U.S.C. 7262(b)) by the registered public accounting firm that prepared or issued its audit report. ☐

If securities are registered pursuant to Section 12(b) of the Act, indicate by check mark whether the financial statements of the registrant included in the filing reflect the correction of an error to previously issued financial statements. ☐

Indicate by check mark whether any of those error corrections are restatements that required a recovery analysis of incentive-based compensation received by any of the registrant’s executive officers during the relevant recovery period pursuant to §240.10D-1(b). ☐

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

The shares of registrant’s common stock are not listed or quoted on an exchange, and as a result, there is no public market price to calculate the aggregate market value.

The number of shares outstanding of the registrant’s common stock as of March 27, 2024 was 7,102,680 shares.

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## PART I

### CAUTIONARY STATEMENT REGARDING FORWARD LOOKING STATEMENTS

This Annual Report on Form 10-K for the year ended December 31, 2023 (this “Form 10-K”) contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the “Securities Act”) and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). When used in this Form 10-K, words such as “anticipate,” “believe,” “estimate,” “expect,” “intend,” “predict,” “project,” and similar expressions, as they relate to us or our management, identify forward-looking statements. These forward-looking statements are not historical facts and are based on information currently available to our management. Accordingly, we caution you that any such forward-looking statements are not guarantees of future performance and are subject to risks, assumptions, estimates and uncertainties that are difficult to predict. Although we believe that the expectations reflected in these forward-looking statements are reasonable as of the date made, actual results could differ materially from those contemplated by the forward-looking statements as a result of certain factors, including but not limited, to those listed in “Item 1A-Risk Factors” of this Form 10-K and the following:

- potential recession in the United States and our market areas;
- the impacts related to or resulting from bank failures and any continuation of the recent uncertainty in the banking industry, including the associated impact to the Company and other financial institutions of any regulatory changes or other mitigation efforts taken by governmental agencies in response thereto;
- liquidity risks, including those related to having enough liquid assets to meet depositor demands;
- risks associated with generating deposits from retail sources without a branch network so that we can fund our loan portfolio and growth;
- our ability to maintain a strong core deposit base or other low-cost funding sources;
- risks associated with higher cost deposits relative to our peer group, which has an impact on our net interest margin and profits;
- increased competition for deposits and related changes in deposit customer behavior;
- risks associated with the persistent inflationary environment in the United States and our market areas, and its impact on market interest rates, the economy and credit quality;
- the adequacy of the allowance for credit losses;
- changes in market interest rates, including the significant increases in market interest rates experienced since March 2022, which could negatively impact bond market values and result in a lower net book value;
- fluctuation in the value of our investment securities;
- changes in the economy generally and the regulatory response thereto;
- changes in the economy of the State of Texas, our primary market;
- increases in unemployment rates in the United States and our market areas;
- risks associated with implementing aspects of our expansion strategy, whether through additional services and products or acquisitions;
- the need to hold more capital in order to comply with consolidated capital ratios;
- our ability to raise additional capital, particularly during times of stress;
- competition from other banks, financial institutions and wealth and investment management firms and our ability to retain our clients;
- risks associated with having one referral source, Cain Watters & Associates, LLC (“Cain Watters”), comprise a substantial part of our business;
- our reliance on key personnel and the ability to attract and retain the personnel necessary to implement our business plan;
- risks specific to commercial loans and borrowers (particularly dental and U.S. Small Business Administration (“SBA”) loans), including the risk of declines in commercial real estate prices or deterioration in value of the general business assets that secure such loans;
- our ability to continue to originate loans (including SBA loans);
- impairment of our goodwill or other intangible assets;
- claims and litigation pertaining to our fiduciary responsibilities;
- generating investment returns for our wealth management, brokerage and other customers that are satisfactory to them;
- our ability to manage our credit risk;
- regulatory scrutiny related to our loan portfolio, including commercial real estate;
- the earnings capacity of our borrowers;
- our inability to identify and address potential conflicts of interest;
- our ability to maintain effective internal control over financial reporting;
- the accuracy of estimates and assumptions;
- the development of an active, liquid market for the Series B preferred stock;



- the soundness of other counterparty financial institutions and certain securities brokerage firms;
- technological change in the banking, investment, brokerage and insurance industry;
- our ability to protect against and manage fraudulent activity and cybersecurity risk, including cyber incidents or other failures, disruptions or breaches of our information security systems or infrastructure, or those of our third-party vendors or other service providers, and identify theft;
- our reliance on communications, information, operating and financial control systems technology and related services from third-party service providers;
- natural disasters and epidemics and pandemics;
- the effects of terrorism and acts of war or threat thereof;
- environmental liabilities;
- legislative changes or the adoption of tax reform policies;
- uncertainty regarding United States fiscal debt and budget matters;
- political instability and changes in tariffs and trade barriers;
- compliance with laws and regulations of the financial services industry, supervisory actions, capital requirements, the Bank Secrecy Act, anti-money laundering laws, consumer laws, and other statutes and regulations;
- regulation of broker-dealers and investment advisors;
- the enactment of regulations relating to privacy, information security and data protection;
- legal and regulatory examinations, proceedings, investigations and inquiries, fines and sanctions;
- future issuances of preferred stock or debt securities and its impact on the Series B preferred stock;
- our ability to manage our existing and future preferred stock and indebtedness;
- our ability to pay dividends;
- the continuation of securities analysts coverage of the company;
- our management and board of directors have significant control over our business;
- risks related to being a “controlled company” under NASDAQ rules;
- the costs and expenses of being a public company; and
- changes in the laws, rules, regulations, interpretations or policies relating to financial institutions, accounting, tax, trade, current and future governmental monetary and fiscal policies, including the uncertain impacts of quantitative tightening and current and future policies of the Board of Governors of the Federal Reserve System (“Federal Reserve”) and as a result of initiatives of the Biden administration.

Such statements reflect the current views of our management with respect to future events and are subject to these and other risks, uncertainties and assumptions relating to our operations, results of operations, growth strategy and liquidity. All subsequent written and oral forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by this paragraph. We undertake no obligation to publicly update or otherwise revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law.

**Item 1. Business.**

**Our Company**

Tectonic Financial, Inc. (the “Company,” “we,” “us,” or “our”) is a financial holding company headquartered in Dallas, Texas offering banking, trust, investment advisory, third-party administration and recordkeeping, securities brokerage, underwriting, and insurance services to high net worth individuals, small businesses and institutions across the United States. The Company was formed in late 2016 for the purpose of acquiring T Bancshares, Inc. (“T Bancshares”), and its wholly owned subsidiary, T Bank, National Association (the “Bank”). T Bancshares was incorporated under the laws of the State of Texas on December 23, 2002 to serve as the bank holding company for the Bank. On May 13, 2019, we completed a merger with Tectonic Holdings, LLC (“Tectonic Holdings”), a company with whom we had common ownership (the “Tectonic Merger”). Through the Tectonic Merger, we acquired Tectonic Advisors, LLC (“Tectonic Advisors”) and Sanders Morris LLC (“Sanders Morris”), as well as its subsidiary, HWG Insurance Agency LLC (“HWG”), which expanded our financial services to include investment advisory, securities brokerage, investment banking, and insurance services.

As of December 31, 2023, we had, on a consolidated basis, \$677.3 million in assets, \$494.8 million in total loans held for investment, \$26.6 million in loans held for sale, \$526.9 million in deposits and \$106.9 million in shareholders’ equity. Net income for the year ended December 31, 2023 was \$15.2 million. The Company’s Series B preferred stock is traded through the NASDAQ Capital Market under the symbol “TECTP”.

**Operating Segments**

**Overview**

We operate through three business segments: Banking, Other Financial Services, and HoldCo operations.

- Our Banking segment operates through the Bank, a full-service, nationally chartered commercial bank headquartered in Dallas, Texas providing traditional community banking services, as well as factoring services through the Bank’s Integra Factoring Division. The Bank’s Trust Division is within our Other Financial Services segment below.
- Our Other Financial Services segment includes Tectonic Advisors, Sanders Morris, HWG and the Bank’s Trust Division, which includes a third-party administrator (“TPA”) services unit:
  - o Tectonic Advisors is a registered investment advisor providing investment advisory services to individuals, institutions (including affiliates) and families. It advises on portfolios of assets for an asset-based fee. As of December 31, 2023, Tectonic Advisors had approximately \$3.6 billion in client assets under management (“AUM”) (which includes \$1.8 billion of AUM held by the Bank as a fiduciary).
  - o Sanders Morris is a registered broker-dealer with Financial Industry Regulatory Authority (“FINRA”), and registered investment advisor with the Securities and Exchange Commission (the “SEC”). Through Sanders Morris, we serve clients on their investment portfolios as an advisor or broker (often with limited powers of attorney). We also execute trades for institutions and households, and provide investment banking services to corporate entities. As of December 31, 2023, Sanders Morris had approximately \$1.2 billion in client advisory assets under management, and client brokerage assets of \$2.0 billion, bringing total client assets to \$3.2 billion at Sanders Morris.
  - o HWG is an insurance agency registered with the Texas Department of Insurance (“TDI”), and is focused on offering life and disability coverages.
  - o The Bank’s Trust Division provides private trust services, and also includes a TPA services unit providing retirement plan design and administrative services.
- Our Holdco segment, HoldCo, includes the Bank’s immediate parent and related subordinated debt, as well as operations of Tectonic Financial, Inc., the financial holding company that serves as parent for the group overall. Its principal source of revenue is dividends from our subsidiaries.

## Banking

**General.** The Bank is a full-service commercial bank offering a broad range of commercial and consumer banking services to small- to medium-sized businesses, single-family residential and commercial contractors and consumers. The Bank strives to generate an attractive risk-adjusted return on assets and capital by providing niche lending services and generating significant non-interest income through its factoring and trust services. Lending services include commercial loans to small- to medium-sized businesses and professional concerns as well as consumers. The Bank offers a wide range of deposit services including demand deposits, regular savings accounts, money market accounts, individual retirement accounts, and certificates of deposit with fixed rates and a range of maturity options. The Bank also offers trust services. These services are provided through a variety of delivery systems including automated teller machines, mobile banking and internet banking.

**Lending Services.** From its single location, the Bank operates three lending verticals where it has established expertise: SBA and U.S. Department of Agriculture (“USDA”), dental and other professionals and traditional community banking. We believe our lending products provide an important diversity of risk and opportunity, which differentiates us from most community banks our size. The Bank also offers factoring services through its Integra Division. See the discussion of “Factored Receivables” below.

**SBA and USDA.** The Bank originates and services commercial and real estate loans under programs guaranteed by the SBA and the USDA representing approximately 54.1% of the Bank’s total lending services as of December 31, 2023. Generally 75% to 80% of the principal balance of these loans is guaranteed by these agencies. The CARES Act increased the SBA 7(a) guaranty on 7(a) loans to 90% for loans originated from February 1, 2020 through September 30, 2021. These loans generally offer borrowers more flexible terms and conditions than available through conventional commercial loans. Examples of more flexible terms include longer amortization periods, lower required down payments, and less borrower operating history. These loans are generally secured by equipment, real estate, and other tangible collateral. Loan-to-value ratios may, in some instances, be higher than conventional loans. Loans secured by business assets that do not include real estate have terms that are generally not more than 10 years and are fully amortizing. Loans secured by real estate as the principal collateral are generally 25 years or less and are also generally fully amortizing. Loans can be adjustable rate loans, but may also be fixed for the term of the loan. Repayment of the loans is based on an analysis of the borrower’s ability to generate sufficient income from operations. This analysis may rely more heavily on projected future earnings than on conventional loans. The Bank also analyzes the industry sector to determine the feasibility of the projected income.

There is generally an active secondary market for the guaranteed portion of these loans. Because the guaranteed portion carries the full faith and credit guarantee of an agency of the U.S. government, the guaranteed portion of the loan can generally be sold for a premium at the time of the sale. We may sell the guaranteed portion or retain the guaranteed portion on our balance sheet based on, among other things, our view of the premiums being paid for such guaranteed portions, our desire to generate additional capital for the Bank and/or the funding costs and sources to fund such loans. As the guaranteed portion of the SBA/USDA loans age, the premium that such portions can generate typically declines. Therefore, we typically make the determination about whether to sell the guaranteed portion of such loans shortly after such loans are certified as guaranteed by either the SBA or USDA, as applicable.

**Dental and Other Professionals.** The Bank offers loans to the dental industry and other small-to-medium sized businesses. The principal referral source of the dental loans is Cain Watters. Most of the partners of Cain Watters are stockholders in the Company, and four partners serve on our board of directors. Cain Watters has been highly successful in providing a variety of consulting services to dentists and dental companies for over 30 years with a national client base. Cain Watters refers loans to a variety of lenders (including the Bank), who compete on price, terms and service. We view the dental lending vertical as highly competitive.

**Traditional Community Banking.** The Bank offers traditional lending services, including commercial and industrial, commercial real estate, construction and, on a very limited basis, consumer loans (each as further described below). The majority of these loans are to commercial enterprises in the Dallas, Texas area.

**Commercial and Industrial Loans.** Loans for commercial purposes in various lines of businesses are a major component of the Bank's loan portfolio. The targets in the commercial loan markets are retail establishments, professional service providers, in particular dentists, and small- to medium-sized businesses. See "—Dental and Other Professionals" above. Commercial lending generally involves greater credit risk than residential mortgage or consumer lending and involves risks that are different from those associated with commercial real estate lending. The terms of these loans vary by purpose and by type of underlying collateral, if any. The commercial loans are primarily underwritten on the basis of the borrower's ability to service the loan from income and their creditworthiness. Although commercial loans may be collateralized by equipment or other business assets, the liquidation of collateral in the event of a borrower default may represent an insufficient source of repayment because equipment and other business assets may, among other things, be obsolete or of limited use. Accordingly, the repayment of a commercial loan depends primarily on the creditworthiness and projected cash flow of the borrower (and any guarantors), while liquidation of collateral is considered a secondary source of repayment. On some of these loans, the Bank takes a security interest in real estate as a prudent practice and measure and not as the principal collateral for the loan.

The Bank will typically make equipment loans for a fixed term of generally not more than 10 years at fixed or variable rates, with the loan fully amortized over the term. Loans to support working capital will typically have terms not exceeding one year and will usually be secured by accounts receivable, inventory or personal guarantees of the principals of the business. For loans secured by accounts receivable or inventory, principal will typically be repaid or reduced with cash generated as the accounts receivable and/or inventory is converted into cash, and for loans secured with other types of collateral, principal will typically be repaid over the term of the loan or due at maturity.

**Real Estate Loans.** The Bank makes owner occupied and non-owner occupied commercial real estate loans, residential and commercial construction and development loans, and residential real estate loans. The Bank often uses appraisals to assess the collateral value of such real estate. However, the Company's use of appraisals in deciding whether to make a loan on or secured by real property does not ensure the value of the real property collateral if it must ultimately be foreclosed upon and sold.

**Commercial Real Estate.** Commercial real estate loan terms generally are limited to 25 years or less. Interest rates may be fixed or adjustable, although rates typically are not fixed for loans with maturity dates exceeding 10 years. The Bank generally requires personal guarantees from the principal owners of the property supported by a review by the Bank's management of the principal owners' personal financial statements. Risks associated with commercial real estate loans include fluctuations in the value of real estate, tenant vacancy rates and the quality of the borrower's management.

**Residential Real Estate.** The Bank's residential real estate loans consist of loans to acquire and renovate existing homes for subsequent re-sale, residential new construction loans, residential loans purchased in the secondary market, residential rental properties, and on a limited basis, traditional mortgage lending for one-to-four family owner occupied property. Loans are generally made in accordance with the Bank's appraisal and loan policy with the ratio of the loan principal to the value of collateral (typically established by independent appraisal).

**Consumer Installment Loans.** On a limited basis, the Bank makes loans to individuals for personal, family and household purposes, including secured and unsecured installment and term loans. These loans are typically to the principals and employees of our business customers. Repayment of consumer loans depends upon the borrower's financial stability and is more likely to be adversely affected by divorce, job loss, illness and personal hardships than repayment of other loans. Because many consumer loans are secured by depreciable assets such as boats, cars and trailers, the loan should be amortized over the useful life of the asset. The loan officer will review the borrower's past credit history, past income level, debt history and, when applicable, cash flow and determine the impact of all these factors on the ability of the borrower to make future payments as agreed. The principal competitors for consumer loans are the established banks and finance companies in our market.

**Lending Policy.** The Bank's delegations of authority, which are approved by its board of directors, provide for various levels of officer lending authority. The Bank has an independent third-party review that evaluates the quality of loans on a periodic basis and determines if loans are originated in accordance with the guidelines established by its board of directors. Additionally, our board of directors has formed a directors' loan committee with members named by board resolution to provide the following oversight:

- ensure compliance with loan policy, procedures and guidelines as well as appropriate regulatory requirements;
- approve loans with net Bank exposure over \$2 million;
- monitor delinquent, non-accrual loans and classified loans;
- monitor loan portfolio concentrations and quality through a variety of metrics;
- monitor our loan servicing and review systems; and
- review the adequacy of the credit loss reserve.

We believe we follow a relatively conservative lending policy, but one that we believe permits prudent risks to assist businesses and consumers in our lending market. Interest rates vary depending on our cost of funds, the loan maturity, the degree of risk and other loan terms. The Bank does not make any loans to any of its directors, executive officers or their affiliates.

**Lending Limits.** The Bank's lending activities are subject to a variety of lending limits. Differing limits apply based on the type of loan or the nature of the borrower, including the borrower's relationship to the Bank. In general, however, the Bank is able to loan to any one borrower a maximum amount equal to either:

- 15% of the Bank's capital and surplus and allowance for credit losses;
- 25% of its capital and surplus and allowance for credit losses if the amount that exceeds 15% is secured by cash or readily marketable collateral, as determined by reliable and continuously available price quotations; or
- any amount when the loan is fully secured by a segregated deposit at the Bank and the Bank has perfected its security interest in the deposit.

These legal limits will increase or decrease as the Bank's capital increases or decreases as a result of its earnings or losses, among other reasons.

**Credit Risks.** The principal economic risk associated with each category of loans that the Bank makes is the creditworthiness of the borrower. Borrower creditworthiness is affected by general economic conditions and the strength of the relevant business market segment. General economic factors affecting a borrower's ability to repay include interest, inflation and employment rates, as well as other factors affecting a borrower's customers, suppliers and employees. The well-established financial institutions in our primary service area currently make proportionately more loans to medium- to large-sized businesses than the Bank. Many of the Bank's anticipated commercial loans will likely be made to small- to medium-sized businesses that may be less able to withstand competitive, economic and financial pressures than larger borrowers.

**Factored Receivables.** The Bank offers financing to smaller transportation companies across the United States primarily through factoring of accounts receivables through its Integra Division. We directly purchase the receivables generated by our clients, primarily transportation companies, at a discount to their face value. The transactions are structured to provide the clients with immediate working capital when there is a mismatch between trade payable payments to the client for services rendered and the required payment of operating costs, such as fuel and insurance costs, incurred to provide such good or service. The receivables are typically collected 30 to 60 days after delivery.

**Investments.** The Bank invests a portion of its assets in available for sale securities, which include U.S. Treasuries, U.S. government agencies, mortgage-backed securities, direct obligations of quasi government agencies including Fannie Mae, Freddie Mac, and the Federal Home Loan Bank. In addition, the Bank may make investments in held to maturity assets, including certain municipal or state obligations or securities that it believes have a similar risk profile thereto. These investments include, among other things, securities issued pursuant to Property Assessed Clean Energy programs ("PACE") and Public Improvement District/Tax Increment Reinvestment Zone ("PID/TIRZ") investments. These investment contracts or bonds originate under a contractual obligation between the property owners, the local county or city administration, and a third-party administrator and sponsor. Generally, as a property assessment, the total assessment is repaid in installments over a period of 5 to 32 years by the then current property owner(s). Investments in instruments other than U.S. Treasuries carry a degree of risk, including risk of default, market fluctuations and lack of liquidity.

**Deposit Services.** To fund its loan and securities portfolio, the Bank offers a wide range of deposit services including demand deposits, regular savings accounts, money market accounts, individual retirement accounts, and certificates of deposit with fixed rates and a range of maturity options. In addition, the Bank can access uninvested cash from customers of its trust department by moving portions of it into money market deposits. As of December 31, 2023, the Bank deposits included \$31.3 million available from the funds of trust clients.

In addition to traditional lobby banking services, the Bank offers robust e-banking services, via on-line and mobile devices, to both consumers and businesses. These services include remote check deposits, bill payment, electronic transfer of funds between financial institutions, person-to-person payments, positive pay, as well as traditional internet services such as balance inquiries and internal funds transfers. The Bank provides a courier and mobile banking concierge service throughout the Dallas MSA and offers its customers free usage of any automated teller machine in the world through its debit card. We also offer an on-line only option to open transaction, savings, and certificate deposits that is marketed via the internet to attract consumer deposits.

As of December 31, 2023, the Bank had total deposits of approximately \$531.4 million which includes \$4.5 million of intercompany deposits of the parent company and other subsidiaries, for a net balance of \$526.9 million. Time deposits of \$250 thousand and over totaled \$109.6 million as of December 31, 2023. The Bank had \$50.0 million of brokered deposits through an Insured Cash Sweep One-Way Buy Agreement as of December 31, 2023.

***Borrowings.*** In addition to deposits, we utilize advances from the Federal Home Loan Bank of Dallas (the “FHLB”), and other borrowings, such as a line of credit with the Federal Reserve Bank of Dallas (the “FRB”) and borrowings under the Bank Term Funding Program (“BTFP”), along with long-term subordinated notes as supplementary funding sources to finance our operations. At December 31, 2023, the Company had no borrowings with the FHLB or the FRB under the lines of credit. The Bank had \$21.0 million, or 3.7% of total liabilities, borrowed under the BTFP, and the debt at T Bancshares, net of debt issuance costs, totaled \$12.0 million, or 2.1% of total liabilities.

## **Other Financial Services**

***General.*** We provide a variety of investment and insurance services to our clients through one or more subsidiaries, including investment advisory, asset management, stock and bond investments, institutional trading, private investments and access to public offerings and other investments. By providing our clients with a broad array of investment products and services, we believe that we can attract clients seeking differentiated investment solutions and retain them over a longer period of time. These services include:

***Trust Services.*** The Company provides trust services to individuals and defined contribution and benefit plans established by small businesses for their owners and employees. We have approximately 1,800 trust accounts in 48 states. The Bank has established common pooled funds to comingle our clients’ capital to invest in stocks, bonds, exchange-traded funds or other investments and thereby provide a smaller investor with broader diversification and access to professional investment advisors. The Bank has approximately \$1.9 billion in market value of trust assets as of December 31, 2023.

We currently have six common pooled funds for qualified plans and another three for personal trust (individual) investors. Each common pooled fund is established for a particular asset class or investment strategy, and each invests in stocks, bonds and/or exchange traded funds (depending on the fund’s strategy), often selected by a registered investment sub-advisor(s) retained by the Bank to serve the particular common pooled fund. The suite of common pooled funds provides an investor with the ability to diversify across asset classes (e.g., equities, fixed income or real assets) and managers. We also have common pooled funds that invest in ETFs (as selected by Tectonic Advisors), which provide our investors with the ability to invest in passive portfolios. We believe that the benefit of a common pooled fund is that it provides investors with access to managers that might not be accessible to individual or smaller investors, sometimes with a lower cost than in a mutual fund format.

The Bank has retained Tectonic Advisors under a long-term contract to provide investment advisory services in selecting managers and certain investments and constructing the allocations of the common pooled funds. The Bank generates fees by providing administrative services to the common pooled funds and providing trust services to the plans and the individual investors.

Cain Watters has referred substantially all of the clients of the Bank’s Trust Division. Cain Watters specializes in providing financial planning, accounting, tax and advisory services to small businesses, principally dental practices. Cain Watters refers certain of its clients to the Trust Division to provide custodial and fiduciary services for their defined benefit and contribution plans and also their personal assets. Cain Watters is not obligated to make such referrals and refers its clients to other service providers that are competitive with the Bank. The Bank competes on the basis of service and investment performance. However, the Bank and Cain Watters are parties to an agreement which, among other provisions, obligates each party to preserve the other’s business relationship with their mutual clients. This agreement was renewed on December 1, 2022 under an automatic extension clause, and was subsequently amended effective January 31, 2023 to provide for termination upon the dissolution of either party or upon a mutually agreeable date in the event of the sale of the Company. The partners of Cain Watters own approximately 29.3% of the Company, and four partners of Cain Watters serve on the board of directors of the Company.

***Third Party Administration.*** The Nolan Company (“Nolan”), a TPA based in Overland Park, Kansas, operates as a department within the Bank doing business under the name of The Nolan Company. Founded in 1979, Nolan provides clients with retirement plan design and administrative services, specializing in ministerial recordkeeping, administration, actuarial and design services for retirement plans of small businesses and professional practices. We believe that offering TPA services allows us to serve our clients more fully and to attract new clients to our trust platform.

**Investment Advisory.** Tectonic Advisors and Sanders Morris are registered investment advisors regulated by the SEC. They provide investment advisory and due diligence services to their respective clients for an asset-based or a performance-based fee.

Tectonic Advisors provides investment advice to the board of director's trust committee in the management of its \$1.9 billion of common pooled funds under a long-term agreement that has been in effect since 2006, the current form of which renewed in December 2022 under an automatic extension clause within the agreement, and was subsequently extended effective January 31, 2023 to a duration that terminates upon the dissolution of either party or upon a mutually agreeable date in the event of a sale of the Company. Pursuant to this agreement, Tectonic Advisors provides investment advice, asset allocation advice and third party manager research for the construction of portfolios. Tectonic Advisors provides advice on six common pooled funds, which are combined in various manners to develop different portfolios for investors (ranging from a conservative allocation to an aggressive allocation). Tectonic Advisors works with the Bank's Trust Division, and the board of director's trust committee, in the management of these common pooled funds and portfolios and meets with the Trust Division and trust committee on a quarterly basis. In addition to services provided to the Bank, Tectonic Advisors provides investment advisory research and due diligence services to Cain Watters under a continuing agreement.

In providing investment advisory services to individuals and families, Tectonic Advisors' and Sanders Morris' investment advisor representatives first determine the risk profile of the investor, which considers the age, investment time horizon, tolerance for risk and investment objectives. Once determined, the advisor makes a recommendation on asset allocation and populates each asset class (e.g., domestic equity, international equity, fixed income, etc.) among mutual funds, exchange traded funds, common stocks and/or bonds, and alternative investments to provide exposure to each such asset class. The asset allocation and investments populating each asset class are revisited periodically based on interaction with the client, his or her changing risk profile, investment performance, changing market conditions and/or other factors, as the advisor deems appropriate.

**Brokerage.** Through Sanders Morris, we purchase and sell stocks and other securities for high net worth clients, often on a discretionary basis, in consideration for brokerage commissions based on trading activity. In addition, we provide institutional trading and other services to money managers, institutions, and individual accounts. We also provide clients with access to private investments that are sourced by us in consideration for a placement fee or commission. Finally, we provide margin loans offered through our clearing firm (Pershing LLC) and periodically serve as a member of an underwriting or selling group member in public offerings, which we offer to our clients. As of December 31, 2023, Sanders Morris has approximately \$2.7 million in net regulatory capital as defined by FINRA to support its broker-dealer activities.

Sanders Morris earns revenue by charging fees and trading commissions for managing the investment assets of clients. Fees and trading commissions are typically charged based on trading activity and/or portfolio size. In addition, we also generate substantial revenue from a traditional, commission-based structure where we earn commissions on client purchase and sale transactions. Sanders Morris also serves as a placement agent on a "best efforts" basis of private placements of equity and fixed income securities. Sanders Morris participates in syndicates of public offerings, typically as a selling group member. Sanders Morris can also participate in public offerings as an underwriter, which means that Sanders Morris takes principal risk on the placement of the securities but earns a higher fee.

Finally, Sanders Morris has an institutional trading business, which is based in Dallas, Texas. This group provides trading, proprietary trading ideas and research, structured solutions and other financial services to clients that include: registered investment advisors, high net worth families and individuals, money managers, hedge funds and others. This business typically charges a commission on trading activity. It competes on the basis of service and solutions.

**Insurance.** Through our insurance agency, HWG, we provide disability and life insurance as a broker. HWG is an insurance agency licensed under the TDI. HWG generates its commissions through the sale of policies as a broker to clients and also receives renewal premiums from past policies sold (and which are renewing). HWG is currently generating most of its revenues from renewals, and continues to tailor its team to generate new business.



## **Competition**

The market for financial services is rapidly changing and intensely competitive and is likely to become more competitive as the number and types of market entrants increases. The Bank competes in both lending and attracting funds with a wide range of financial institutions within our markets, including local, regional and national commercial banks, savings and loan associations, and credit unions. We also compete with consumer finance companies, pension trusts, mutual funds, insurance companies, mortgage bankers and brokers, brokerage and investment banking firms, asset management and advisory firms, online and discount brokers, private trust companies, venture capital, private equity and hedge funds, asset-based nonbank lenders, government agencies, third-party payment processors, financial technology companies and certain other non-financial institutions, which may offer more favorable financing alternatives than the Bank. We believe that our principal competitive advantages include our regional focus and our long-standing relationships with our clients.

In addition, the investment services business (including brokerage, private placements, syndication, and other financial advice) is highly competitive. The principal competitive factors influencing our businesses are:

- expertise and quality of the professional staff;
- reputation in the marketplace;
- existing client relationships;
- performance of investment strategies or product offerings;
- advertising and sales promotion efforts,
- types, quality, and price of our products and services; and
- the technology platform through which a customer accesses our products and services.

The financial services industry has become considerably more concentrated as many securities firms have either ceased operations, been acquired by, or merged into other firms. Many of these larger firms have significantly greater financial and other resources than we do and can offer their customers more product offerings, lower pricing, broader research capabilities, access to international markets, and other products and services we do not offer, which may give these firms a competitive advantage over us.

As we seek to expand our business, we face competition in the pursuit of clients interested in our services, the recruitment and retention of wealth management professionals, and the identification and acquisition of other wealth management firms that can be integrated into our group.

## **Our Market Area**

We are based in Dallas, Texas, which is our largest market. The Bank's principal banking markets include Dallas, Tarrant, Denton, Collin and Rockwall counties in North Texas. However, our business is also national in scope. Our national business includes: banking for small businesses (particularly dental practices), SBA and USDA loans, trust and custodial services, and participant directed recordkeeping and third-party administration. In addition, we provide investment advisory and brokerage services through Tectonic Advisors and Sanders Morris.

## **Human Capital Resources**

We had approximately 199 employees as of December 31, 2023. We believe our employee relations to be good and we have no collective bargaining agreements with any employees.

As part of our business philosophy, we believe that we must offer and maintain market competitive compensation and benefit programs in order to attract and retain employees who serve our customers, including competitive compensation, paid time off, an employee retirement plan, bonus and other incentive compensation plans, and modern equipment and support.

The health and well-being of our employees is a priority for our business. Our full-time officers and employees are provided hospitalization and major medical insurance. We pay a substantial portion of the premiums for these coverages. We also provide other basic insurance coverages including dental, life, and long-term disability insurance.



**Other Available Information**

We file or furnish with the SEC annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and other reports required by Section 13(a) or 15(d) of the Exchange Act. Electronic copies of our SEC filings are available to the public at the SEC's website at <https://www.sec.gov>. In addition, our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and other reports required by Section 13(a) or 15(d) of the Exchange Act are available through our website, [www.t.financial](http://www.t.financial), as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC.

The Company routinely posts important information for investors on its website, [www.t.financial](http://www.t.financial). The Company intends to use its website as a means of disclosing material non-public information and for complying with its disclosure obligations under SEC Regulation FD (Fair Disclosure). Accordingly, investors should monitor the Company's website, in addition to following the Company's press releases, SEC filings, public conference calls, presentations and webcasts.

Our website and the information contained on or accessible through our website is not incorporated by reference into, and is not a part of, this Form 10-K.

## SUPERVISION AND REGULATION

*Set forth below is a description of the significant elements of the laws and regulations applicable to the Company and its operating subsidiaries. The description is qualified in its entirety by reference to the full text of the statutes, regulations and policies that are described. Moreover, these statutes, regulations and policies are continually under review by the U.S. Congress and state legislatures, and federal and state regulatory agencies. A change in statutes, regulations or regulatory policies applicable to the Company or its operating subsidiaries could have a material effect on our business.*

### Regulatory Agencies

As a registered bank holding company, the Company is subject to the supervision and regulation of the Federal Reserve and, acting under delegated authority, the FRB, pursuant to the Bank Holding Company Act of 1956, as amended (the “BHC Act”). As a national bank, the Bank is subject to the supervision and regulation of the Office of the Comptroller of the Currency (the “OCC”). Sanders Morris is a registered broker-dealer with the SEC and FINRA, and a registered investment advisor with the SEC. Tectonic Advisors is an SEC registered investment advisor. HWG is an insurance agency registered with the TDI.

### Bank Holding Company Regulation

**BHC Act.** As a registered bank holding company, the Company is required to furnish to the Federal Reserve annual and quarterly reports of its operations and may also be required to furnish such additional information and reports as the Federal Reserve or the FRB may require. The Company elected to become a financial holding company in 2018, as further described under “—Financial Holding Company Status.”

Under the BHC Act, the Company must obtain the prior approval of the Federal Reserve before (i) acquiring direct or indirect ownership or control of any class of voting securities of any bank or bank holding company if, after the acquisition, the Company would directly or indirectly own or control 5% or more of the class; (ii) acquiring all or substantially all of the assets of another bank or bank holding company; or (iii) merging or consolidating with another bank holding company.

Under the BHC Act, any company must obtain the approval of the Federal Reserve prior to acquiring control of the Company or the Bank. For purposes of the BHC Act, “control” is conclusively presumed to exist upon the acquisition of 25% or more of the outstanding voting securities of a bank or bank holding company, but may arise based on facts and circumstances even with ownership below 5.00% up to 24.99%. On September 30, 2020, the Federal Reserve’s final rule revising the Federal Reserve’s regulations related to determinations of whether a company has “control” over another company, including a bank holding company or a bank, for purposes of the BHC Act, became effective. The final rule created a tiered system of non-control presumptions based upon the percentage of any class of voting securities held by an acquirer and the presence of other indicia of control. The final rule’s four categories of tiered presumptions of non-control, based upon the percentage of ownership of any class of voting securities held by an acquirer, are (i) less than 5%, (ii) 5% to 9.99%, (iii) 10% to 14.99%, and (iv) 15% to 24.99%. By codifying the non-control presumptions, the final rule provides greater transparency with respect to the total level of equity, representative directors, management interlocks, limiting contractual provisions and business relationships that would be permissible to the Federal Reserve in order to avoid a determination of control. The Federal Reserve’s final rule applies to control determinations under the BHC Act, but does not apply to the Change in Bank Control Act of 1978, as amended (the “CIBCA”).

**Change in Bank Control Act.** The CIBCA and the related regulations of the Federal Reserve require any person or group of persons acting in concert (except for companies required to make application under the BHC Act), to file a written notice with the Federal Reserve before the person or group acquires control of the Company. The CIBCA provides that a person, which includes a natural person or entity, directly or indirectly, has “control” of a bank or bank holding company if it (i) owns, controls, or has the power to vote 25% or more of the voting securities of the bank or bank holding company, (ii) controls the election of directors, trustees, or general partners of the company, (iii) has a controlling influence over the management or policies of the company, or (iv) conditions in any manner the transfer of 25% or more of the voting securities of the company upon the transfer of 25% or more of the outstanding shares of any class of voting securities of another company. Accordingly, the CIBCA requires that prior to the acquisition of any class of voting securities of a bank or bank holding company that prior notice to the Federal Reserve be provided, if, immediately after the transaction, the acquiring person (or persons acting in concert) will own, control, or hold the power to vote 25% or more of any class of voting securities of the bank or bank holding company. A rebuttable presumption of control arises under the CIBCA where a person (or persons acting in concert) controls 10% or more, but less than 25%, of a class of the voting stock of a company or insured bank (i) which is a reporting company under the Exchange Act, such as the Company, or (ii) such ownership interest is greater than the ownership interest held by any other person (or persons acting in concert).

**Permitted Activities.** The BHC Act also limits the investments and activities of bank holding companies. In general, a bank holding company is prohibited from acquiring direct or indirect ownership or control of more than 5% of the voting shares of a company that is not a bank or a bank holding company or from engaging directly or indirectly in activities other than those of banking, managing or controlling banks, providing services for its subsidiaries and various non-bank activities that are deemed to be closely related to banking. The activities of the Company are subject to these legal and regulatory limitations under the BHC Act and the implementing regulations of the Federal Reserve.

**Volcker Rule.** Section 13 of the BHC Act, commonly known as the “Volcker Rule,” generally prohibits insured depository institutions and their affiliates (including their holding companies) from sponsoring or acquiring an ownership interest in certain investment funds, including hedge funds and private equity funds. The Volcker Rule also places restrictions on proprietary trading, which could impact certain hedging activities. However, Section 203 of the Economic Growth, Regulatory Relief and Consumer Protection Act (the “EGRRCPA”) exempts community banks from the restrictions of the Volcker Rule if (i) the community bank, and every entity that controls it, has total consolidated assets equal to or less than \$10 billion; and (ii) trading assets and liabilities of the community bank, and every entity that controls it, is equal to or less than 5% of its total consolidated assets. As the consolidated assets of the Company are less than \$10 billion and the Company does not currently exceed the 5% threshold, this aspect of the Volcker Rule does not have any impact on the Company’s consolidated financial statements at this time.

**Financial Holding Company Status.** A bank holding company may also elect to become a “financial holding company,” by which a qualified bank holding company may engage, directly or through its non-bank subsidiaries, in any activity that is financial in nature or incidental to such financial activity or in any other activity that is complementary to a financial activity and does not pose a substantial risk to the safety and soundness of depository institutions or the financial system generally. A bank holding company can successfully elect to be regulated as a financial holding company if all of its depository institution subsidiaries meet certain prescribed standards pertaining to management, capital adequacy and compliance with the Community Reinvestment Act (“CRA”), such as being “well-capitalized” and “well-managed,” and must have a CRA rating of at least “satisfactory.” Financial holding companies remain subject to regulation and oversight by the Federal Reserve.

If a financial holding company ceases to meet the above requirements, the Federal Reserve’s regulations provide that the financial holding company must enter into an agreement with the Federal Reserve to comply with all applicable capital and management requirements. Until the financial holding company returns to compliance, the Federal Reserve may impose limitations or conditions on its activities, and the company may not commence any of the broader financial activities permissible for financial holding companies or acquire a company engaged in such financial activities without prior approval of the Federal Reserve. Restrictions imposed on a financial holding company’s activities by the Federal Reserve may not necessarily be made known to the public. If the financial holding company does not return to compliance within 180 days, the Federal Reserve may require divestiture of the financial holding company’s depository institutions. Failure to satisfy the financial holding company requirements could also result in loss of financial holding company status. The Company made this election in 2018, and became a financial holding company.

**Source of Strength.** In accordance with the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”) and long-standing Federal Reserve policy, a bank holding company is required to act as a source of financial and managerial strength to any subsidiary bank. The holding company is expected to commit resources to support its subsidiary bank, including at times when the holding company may not be in a financial position to provide such support. A bank holding company’s failure to meet its source-of-strength obligations may constitute an unsafe and unsound practice. The source-of-strength doctrine most directly affects bank holding companies in situations where the bank holding company’s subsidiary bank fails to maintain adequate capital levels.

**Sound Banking Practice.** The Federal Reserve also has the power to order a bank holding company to terminate any activity or investment, or to terminate its ownership or control of any subsidiary, when it has reasonable cause to believe that the continuation of such activity or investment or such ownership or control constitutes a serious risk to the financial safety, soundness or stability of any subsidiary bank of the bank holding company. For example, a holding company could not impair its subsidiary bank’s soundness by causing it to make funds available to non-banking subsidiaries or their customers if the Federal Reserve believed it not prudent to do so.

The Federal Reserve has the power to assess civil money penalties for unsafe or unsound practices. The Financial Institutions Reform, Recovery and Enforcement Act of 1989 (“FIRREA”), expanded the Federal Reserve’s authority to prohibit activities of bank holding companies and their non-banking subsidiaries which represent unsafe and unsound banking practices or which constitute violations of laws or regulations. FIRREA increased the amount of civil money penalties, which the Federal Reserve can assess for 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 \$1.0 million for each day the activity continues. FIRREA also expanded the scope of individuals and entities against which such penalties may be assessed.

***Dividends, Distributions, Stock Redemptions and Repurchases.*** Dividends and distributions from our subsidiary companies are the Company's principal source of cash revenues. The Company's earnings and activities are affected by legislation, regulations, local legislative and administrative bodies and decisions of courts in the jurisdictions in which we conduct business. These include limitations on the ability of the Bank to pay dividends to the Company and the Company's ability to pay dividends to its shareholders. Consistent with its policy that bank and financial holding companies should serve as a source of financial strength for their subsidiary banks, it is the policy of the Federal Reserve that bank holding companies should pay cash dividends on preferred and 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 subsidiary. Consistent with such policy, a banking organization should have comprehensive policies on dividend payments that clearly articulate the organization's objectives and approaches for maintaining a strong capital position and achieving the objectives of the policy statement.

In addition, we are subject to certain restrictions on the making of distributions as a result of the requirement that the Bank maintain an adequate level of capital as described below. As a Texas corporation, we are restricted under the Texas Business Organizations Code (the "TBOC") from paying dividends under certain conditions. Under Texas law, we cannot pay dividends to shareholders if the dividends exceed our surplus or if after giving effect to the dividends, we would be insolvent.

In the event that the Board authorizes the payment of a dividend by the Company, any such dividend will be consistent with our capital needs, asset quality and overall financial condition (as a financial holding company). However, there can be no assurance that this will be the case in the future and, if it is found that our dividend is not consistent with our capital needs and/or asset quality or if our financial condition deteriorates, we may not be able to pay dividends on our Series B preferred stock.

Bank holding companies must consult with the Federal Reserve before redeeming or repurchasing any equity or other capital instrument included in tier 1 or tier 2 capital prior to stated maturity, if (x) such redemption or repurchase could have a material effect on the level or composition of the organization's capital base, or (y) as a result of such redemption or repurchase, there is a net reduction of the outstanding amount of common stock or preferred stock outstanding below the amounts outstanding at the beginning of the quarter in which the redemption or repurchase occurs. In addition, bank holding companies are unable to repurchase shares equal to 10% or more of their net worth if they would not be well-capitalized (as defined by the Federal Reserve) after giving effect to such repurchase. Bank holding companies experiencing financial weaknesses, or that are at significant risk of developing financial weaknesses, must consult with the Federal Reserve before redeeming or repurchasing common stock or other regulatory capital instruments.

***Imposition of Liability for Undercapitalized Subsidiaries.*** The Federal Deposit Insurance Corporation Act of 1991 ("FDICIA"), requires bank regulators to take "prompt corrective action" to resolve problems associated with insured depository institutions. 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 until it becomes "adequately capitalized." For purposes of this statute, the Company has control of the Bank. Under FDICIA, the aggregate liability of all companies controlling a particular institution is limited to the lesser of 5% of the depository institution's total assets at the time it became undercapitalized or the amount necessary to bring the institution into compliance with applicable capital standards. FDICIA grants greater powers to bank regulators in situations where an institution becomes "significantly" or "critically" undercapitalized or fails to submit a capital restoration plan. For example, a bank holding company controlling such an institution can be required to obtain prior Federal Reserve approval of proposed distributions, consent to a merger or divest the troubled institution or other affiliates.

***Anti-Tying Restrictions.*** Bank holding companies and affiliates are prohibited from tying the provision of services, such as extensions of credit, to other services offered by the holding company or its affiliates. While we and our other affiliates offer services, no such services are tied to one another or conditioned upon one another.

## **Bank Regulation**

The Bank is a national bank chartered under the National Bank Act. The Bank is a member of the Federal Reserve. In addition, its deposits are insured by the Federal Deposit Insurance Corporation ("FDIC") to the maximum extent permitted by law. National banks, such as the Bank, are subject to extensive regulation, supervision and examination by the OCC. As an insured depository institution and member bank, the Bank is also subject to regulation by the FDIC and the Federal Reserve, although the OCC is the Bank's primary federal regulator. The bank regulatory agencies have the power to enforce compliance with applicable banking laws and regulations. These 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.

**National Banking Associations.** Banks organized as national banking associations under the National Bank Act are subject to regulation and examination by the OCC. The supervision and regulation by the OCC is primarily intended to protect the interests of depositors of the Bank, not the Bank's shareholders. The National Bank Act, among other things:

- restricts investments and other activities of the Bank;
- restricts the nature and amount of loans that the Bank may make and the interest that may be charged; and
- requires the Bank to maintain reserves against deposits.

**Deposit Insurance.** The FDIC insures the deposits of federally insured banks, such as the Bank, and thrifts, up to prescribed statutory limits for each depositor through the Deposit Insurance Fund (the "DIF"), and safeguards the safety and soundness of the banking and thrift industries. The Dodd-Frank Act set the standard maximum deposit insurance amount as \$250,000. The amount of FDIC assessments paid by each insured depository institution is based on the Bank's total assets and its relative risk of default as measured by regulatory capital ratios and other supervisory factors. Under the Dodd-Frank Act, each institution's assessment base is determined based on its average consolidated total assets less average tangible equity, and there is a scorecard method for calculating assessments that combines CAMELS (an acronym that refers to the five components of a bank's condition that are addressed: capital adequacy, asset quality, management, earnings, and liquidity) ratings and specified forward-looking financial measures to determine each institution's risk to the DIF.

In accordance with the Dodd-Frank Act, the FDIC adopted a plan to restore the DIF to the 1.35% ratio but did not change its assessment schedule. Under the FDIC's restoration plan, FDIC staff will update its projections for the DIF balance and DIF reserve ratio at least semiannually while the restoration plan is in effect. On October 18, 2022, the FDIC adopted a final rule applicable to all insured depository institutions increasing initial base deposit insurance assessment rate schedules by 2 basis points, beginning in the first quarterly assessment period of 2023. The FDIC also issued a notice maintaining a DIF reserve ratio of 2.0% for 2023. The increase in assessment rate schedules is intended to increase the likelihood that the DIF reserve ratio reaches the statutory minimum of 1.35% by September 30, 2028, the statutory deadline set by the Dodd-Frank Act. The new assessment rate schedules will remain in effect unless and until the DIF reserve ratio meets or exceeds 2.0% in order to support growth in the DIF in progressing toward the FDIC's long-term goal of a 2.0% designated reserve ratio for the DIF. FDIC staff may in the future recommend additional assessment rate adjustments if deemed necessary.

Separately, in connection with the U.S. Treasury Secretary's invocation of the systemic risk exception declared on March 12, 2023, in response to the failure of two insured depository institutions and the appointment of the FDIC as receiver for such failed insured depository institutions, the FDIC adopted a final rule in November 2023 that implements a special assessment to recover the DIF's losses from protecting uninsured depositors following the closures of such failed insured depository institutions. This rule is effective on April 1, 2024 and affects only those insured depository institutions with more than \$5 billion in total assets. Affected institutions must pay such special assessment over eight quarterly assessment periods, the first of which will be reflected on the first quarterly assessment period for January 1 through March 31, 2024, with the first payment due on June 28, 2024. This rule is not applicable for the Company. However, the FDIC also reserved the right to impose a one-time "shortfall assessment" at the conclusion of the special assessment if there are DIF losses that have not been fully recovered. It is possible that further increases in deposit insurance are adopted by the FDIC that could apply to the Bank.

Additionally, under the Federal Deposit Insurance Act (the "FDIA"), the FDIC may terminate deposit insurance upon a finding 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.

**Payment of Dividends.** The Company is a legal entity separate and distinct from the Bank. The Company historically has received all of its revenue from distributions from Tectonic Advisors and Sanders Morris. However, to the extent the Company desires to have dividends paid by the Bank, the Bank may be limited in its ability to pay dividends without prior regulatory approval. The Bank is required by federal law to obtain the prior approval of the OCC to declare and pay dividends if the total of all dividends declared in any calendar year would exceed the total of (1) the Bank's net profits (as defined and interpreted by regulation) for that year plus (2) its retained net profits (as defined and interpreted by regulation) for the preceding two calendar years, less any required transfers to surplus. In addition, the Bank may only pay dividends to the extent that retained net profits (including the portion transferred to surplus) exceed bad debts (as defined by regulation).

The payment of dividends by the Bank is affected by the requirement to maintain adequate capital pursuant to applicable capital adequacy guidelines and regulations, and the Bank is generally prohibited from paying any dividends if, following payment thereof, the institution would be undercapitalized. Notwithstanding the availability of funds for dividends, however, the OCC may prohibit the payment of dividends by the Bank if the OCC determines such payment would constitute an unsafe or unsound practice. In addition, under the Basel III rules, institutions that seek the freedom to pay dividends will have to maintain the capital conservation buffer.

**Regulatory Capital Requirements.** Under the Basel III capital regulations, the minimum capital level requirements are (i) a common equity Tier 1 (“CET1”) capital ratio of 4.5%; (ii) a Tier 1 capital ratio of 6.0%; (iii) a total capital ratio of 8.0%; and (iv) a Tier 1 leverage ratio of 4.0%. CET1 generally consists of common stock; retained earnings; accumulated other comprehensive income, or AOCI, unless an institution elects to exclude AOCI from regulatory capital; and certain minority interests; all subject to applicable regulatory adjustments and deductions. Tier 1 capital generally consists of CET1 and noncumulative perpetual preferred stock. Tier 2 capital generally consists of other preferred stock and subordinated debt meeting certain conditions plus an amount of the allowance for loan and lease losses up to 1.25% of assets. Total capital is the sum of Tier 1 and Tier 2 capital. As of December 31, 2023, the Bank exceeded all Basel III regulatory minimum capital requirements.

In addition to the minimum capital requirements, the Bank must maintain a capital conservation buffer that consists of additional CET1 capital greater than 2.5% of risk-weighted assets above the required minimum levels in order to avoid limitations on paying dividends, repurchasing shares and paying discretionary bonuses.

The CET1 requirements also changed the risk-weighting of certain assets including a 150% risk weight (up from 100%) for certain high volatility commercial real estate acquisition development and construction loans and for non-residential mortgage loans that are 90 days or more past due or otherwise on non-accrual status; a 20% (up from 0%) credit conversion factor for the unused portion of a commitment with an original maturity of one year or less that is not unconditionally cancellable; and a 250% risk weight (up from 100%) for mortgage servicing rights and deferred tax assets that are not deducted from capital.

**Community Bank Leverage Ratio.** On September 17, 2019, the federal banking regulators published final rules implementing a simplified measure of capital adequacy for certain banking organizations that have less than \$10 billion in total consolidated assets. Under the final rules, which went into effect on January 1, 2020, depository institutions and depository institution holding companies that have less than \$10 billion in total consolidated assets and meet other qualifying criteria, including a leverage ratio of greater than 9%, off-balance-sheet exposures of 25% or less of total consolidated assets and trading assets plus trading liabilities of 5% or less of total consolidated assets, are deemed “qualifying community banking organizations” and are eligible to opt into the “Community Bank Leverage Ratio,” or CBLR, framework. A qualifying community banking organization that elects to use the CBLR framework and that maintains a leverage ratio of greater than 9% is considered to have satisfied the generally applicable risk-based and leverage capital requirements under the Basel III rules and, if applicable, is considered to have met the “well capitalized” ratio requirements for purposes of its primary federal regulator’s prompt corrective action rules, discussed below. The final rules include a two-quarter grace period during which a qualifying community banking organization that temporarily fails to meet any of the qualifying criteria, including the greater-than-9% CBLR requirement, is generally still deemed “well capitalized” so long as the banking organization maintains a leverage capital ratio greater than 8%. A banking organization that fails to maintain a leverage capital ratio greater than 8% is not permitted to use the grace period and must comply with the generally applicable requirements under the Basel III rules and file the appropriate regulatory reports.

Although the Company and the Bank are qualifying community banking organizations, the Company and the Bank have elected not to use the CBLR framework, but may make such an election in the future.

**Prompt Corrective Regulatory Action.** Under applicable federal statutes, the OCC is required to take “prompt corrective action” if the Bank does not meet specified minimum capital requirements. For these purposes, the law establishes five capital categories: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized. Under the OCC’s prompt corrective action regulations, an institution is deemed to be:

- “well capitalized” if it has a total capital ratio of 10.0% or greater, a Tier 1 capital ratio of 8.0% or greater, a CET1 capital ratio of 6.5% or greater, a Tier 1 leverage ratio of 5.0% or greater and is not subject to a capital maintenance requirement;
- “adequately capitalized” if it has a total capital ratio of 8.0% or greater, a Tier 1 capital ratio of 6.0% or greater, a CET1 capital ratio of 4.5% or greater and a Tier 1 leverage ratio of 4.0% or greater;
- “undercapitalized” if it has a total capital ratio of less than 8.0%, a Tier 1 capital ratio of less than 6.0%, a CET1 capital ratio of less than 4.5% or a Tier 1 leverage ratio of less than 4.0%;
- “significantly undercapitalized” if it has a total capital ratio of less than 6.0%, a Tier 1 capital ratio of less than 4.0%, a CET1 capital ratio of less than 3.0% or a Tier 1 leverage ratio of less than 3.0%; and
- “critically undercapitalized” if it has a ratio of tangible equity to total assets that is equal to or less than 2.0%.

If the Bank were to become undercapitalized, it would be subject to growth limitations and would be required to submit a capital restoration plan to the OCC. The OCC may not accept such a plan without determining, among other things, that the plan is based on realistic assumptions and is likely to succeed in restoring the Bank's capital. In addition, for a capital restoration plan to be acceptable, the Company must guarantee that the Bank will comply with such capital restoration plan. If the Bank were to fail to submit an acceptable plan, it would be treated as if it were "significantly undercapitalized." "Significantly undercapitalized" depository institutions may be subject to a number of requirements and restrictions, including orders to sell sufficient voting stock to become "adequately capitalized," requirements to reduce total assets and cessation of receipt of deposits from correspondent banks and other depository sources, particularly if such deposits are higher cost deposits. "Critically undercapitalized" institutions are subject to the appointment of a receiver or conservator.

As of December 31, 2023, the Bank qualified as "well capitalized" under the prompt corrective action rules.

**Interstate Banking and Branching.** Effective June 1, 1997, the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 (the "Riegle-Neal Act") amended the FDIA, 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, 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 opts 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.

However, under the Dodd-Frank Act, the national branching requirements have been relaxed and national banks and state banks are able to establish branches in any state if that state would permit the establishment of the branch by a state bank chartered in that state. The OCC accepts applications for interstate merger and branching transactions, subject to certain limitations on the ages of the banks to be acquired and the total amount of deposits within the state that a bank or financial holding company may control. Since our primary service area is Texas, we do not expect that the ability to operate in other states will have any material impact on our growth strategy. We may, however, face increased competition from out-of-state banks that branch or make acquisitions in our primary markets in Texas.

**Restrictions on Transactions with Affiliates.** The Bank is subject to the provisions of Section 23A and 23B of the Federal Reserve Act (the "Affiliates Act"). Affiliates of a bank include, among other entities, the bank's holding company and companies that are under common control with the bank. In our case, Tectonic Advisors, Sanders Morris, HWG and Cain Watters are all considered affiliates of the Bank.

These provisions place limits on the amount of:

- loans or extensions of credit to affiliates;
- investments in affiliates;
- assets that may be purchased from affiliates;
- the amount of loans or extensions of credit to third parties collateralized by the securities or obligations of affiliates; and
- the guarantee, acceptance or letter of credit issued on behalf of an affiliate.

The total amount of the above transactions is limited in amount, as to any one affiliate, to 10% of the Bank's capital and surplus and, as to all affiliates combined, to 20% of the Bank's capital and surplus. In addition to the limitation on the amount of these transactions, each of the above transactions must also meet specified collateral requirements. The Bank must also comply with other provisions designed to avoid the purchase or acquisition of low-quality assets from affiliates. The Dodd-Frank Act expanded the scope of Section 23A of the Affiliates Act, which now includes investment funds managed by an institution as an affiliate, as well as other procedural and substantive hurdles.

Section 23B of the Affiliates Act, among other things, prohibits the Bank from engaging in any transaction with an affiliate unless the transaction is on terms substantially the same, or at least as favorable to the bank or its subsidiaries, as those prevailing at the time for comparable transactions with nonaffiliated companies.



**Loans to Insiders.** Under federal law, the Bank is also subject to restrictions on extensions of credit to its executive officers, directors, principal shareholders and their related interests. These extensions of credit (1) must be made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with third parties, (2) must follow credit underwriting procedures at least as stringent as those applicable to comparable transactions with third parties, and (3) must not involve more than the normal risk of repayment or present other unfavorable features. The Dodd-Frank Act expanded coverage of transactions with insiders by including credit exposure arising from derivative transactions (which are also covered by the expansion of Section 23A of the Affiliates Act). The Dodd-Frank Act prohibits an insured depository institution from purchasing or selling an asset to an executive officer, director, or principal shareholder (or any related interest of such a person) unless the transaction is on market terms, and, if the transaction exceeds 10% of the institution's capital, it is approved in advance by a majority of the disinterested directors.

**Commercial Real Estate Lending Concentrations.** The federal banking agencies, including the OCC, have promulgated guidance governing financial institutions with concentrations in commercial real estate lending. The guidance provides that a bank has a concentration in commercial real estate lending if (i) total reported loans for construction, land development, and other land represent 100% or more of total capital or (ii) total reported loans secured by multifamily and non-farm nonresidential properties (excluding loans secured by owner-occupied properties) and loans for construction, land development, and other land represent 300% or more of total capital and the bank's commercial real estate loan portfolio has increased 50% or more during the prior 36 months. If a concentration is present, management must employ heightened risk management practices that address the following key elements: including board and management oversight and strategic planning, portfolio management, development of underwriting standards, risk assessment and monitoring through market analysis and stress testing, and maintenance of increased capital levels as needed to support the level of commercial real estate lending.

On December 18, 2015, the federal banking agencies jointly issued a "Statement on Prudent Risk Management for Commercial Real Estate Lending." In June 2023, in response to the increased risk relating to commercial real estate loans, the federal banking agencies issued a final Interagency Policy Statement on Prudent Commercial Real Estate Loan Accommodations and Workouts. The new policy statement updates, expands on and supersedes existing guidance from 2009 and supplements the guidance from 2015. Most notably, it (i) adds a new discussion of short-term loan accommodations, (ii) expands guidance regarding the evaluation and assessment of guarantors to also encompass loan sponsors, (iii) incorporates information about changes to accounting principles since 2009, and (iv) updates and expands the illustrative examples of commercial real estate loan workouts.

As of December 31, 2023, the Company did not exceed the levels to be considered to have a concentration in commercial real estate lending and believes its credit administration to be consistent with the aforementioned policy statements and advisory guidance.

**Brokered Deposit Restrictions.** Well capitalized institutions are not subject to limitations on brokered deposits, while an adequately capitalized institution is able to accept, renew or roll over brokered deposits only with a waiver from the FDIC and are subject to certain restrictions on the yield paid on such deposits. Undercapitalized institutions are generally not permitted to accept, renew, or roll over brokered deposits. As of December 31, 2023, the Bank qualified as "well capitalized" for purposes of the brokered deposit restrictions.

**Technology Risk Management, Cybersecurity and Consumer Privacy.** Federal banking regulators have issued various policy statements emphasizing the importance of technology risk management and supervision in evaluating the safety and soundness of depository institutions with respect to banks that contract with outside vendors to provide data processing and core banking functions. The use of technology-related products, services, delivery channels and processes exposes a bank to various risks, particularly operational, privacy, security, strategic, reputation and compliance risk. Banks are generally expected to prudently manage technology-related risks as part of their comprehensive risk management policies by identifying, measuring, monitoring and controlling risks associated with the use of technology.

On July 26, 2023, the SEC adopted final rules that require public companies to promptly disclose material cybersecurity incidents in a Current Report on Form 8-K and detailed information regarding their cybersecurity risk management, strategy, and governance on an annual basis in an Annual Report on Form 10-K. Companies are required to report on Form 8-K any cybersecurity incident they determine to be material within four business days of making that determination. See Item 1C "Cybersecurity" in Part I of this Form 10-K. These SEC rules, and any other regulatory guidance, are in addition to notification and disclosure requirements under state and federal banking law and regulations.



Under Section 501 of the Gramm-Leach-Bliley Act of 1999 (the “GLBA”), the federal banking agencies have established appropriate standards for financial institutions regarding the implementation of safeguards to ensure the security and confidentiality of customer records and information, protection against any anticipated threats or hazards to the security or integrity of such records and protection against unauthorized access to or use of such records or information in a way that could result in substantial harm or inconvenience to a customer. Among other matters, the rules require each bank to implement a comprehensive written information security program that includes administrative, technical and physical safeguards relating to customer information.

Under the GLBA, a financial institution must also provide its customers with a notice of privacy policies and practices. Section 502 prohibits a financial institution from disclosing nonpublic personal information about a customer to nonaffiliated third parties unless the institution satisfies various notice and opt-out requirements and the customer has not elected to opt out of the disclosure. Under Section 504, the agencies are authorized to issue regulations as necessary to implement notice requirements and restrictions on a financial institution’s ability to disclose nonpublic personal information about customers to nonaffiliated third parties. Under the final rule the regulators adopted, all banks must develop initial and annual privacy notices which describe in general terms the bank’s information sharing practices. Banks that share nonpublic personal information about customers with nonaffiliated third parties must also provide customers with an opt-out notice and a reasonable period of time for the customer to opt out of any such disclosure (with certain exceptions). Limitations are placed on the extent to which a bank can disclose an account number or access code for credit card, or deposit or transaction accounts to any nonaffiliated third party for use in marketing.

In November 2021, the federal bank regulatory agencies issued a joint rule establishing computer-security incident notification requirements for banking organizations and their service providers. Beginning May 1, 2022, a bank holding company, such as the Company, and an FDIC-supervised depository institution, such as the Bank, are required to notify the Federal Reserve or FDIC, respectively, as soon as possible and no later than 36 hours after a determination that a computer-security incident that rises to the level of a notification incident has occurred.

**Anti-Money Laundering.** Under federal law, including the Bank Secrecy Act (the “BSA”), as amended by the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (the “USA PATRIOT Act”), and as further amended by the National Defense Authorization Act for Fiscal Year 2021 (the “National Defense Authorization Act”), and implementing regulations, certain types of financial institutions, including insured depository institutions, must maintain anti-money laundering (“AML”) programs that include established internal policies, procedures and controls; a designated compliance officer; an ongoing training program; and testing of the program by an independent audit function. Financial institutions are restricted from entering into specified financial transactions and account relationships and must meet enhanced standards for due diligence, client identification and recordkeeping, including in their dealings with non-U.S. financial institutions and non-U.S. clients. Financial institutions must take reasonable steps to conduct enhanced scrutiny of account relationships to guard against money laundering and to report any suspicious information maintained by financial institutions.

On May 10, 2016, the Financial Crimes Enforcement Network (“FinCEN”) issued a final rule regarding customer due diligence requirements for covered financial institutions in connection with their BSA and AML policies. The final rule adds a requirement that banks understand the nature and purpose of customer relationships and identify the “beneficial owner” (25% or more ownership interest) of legal entity customers. The formal implementation date was May 11, 2018. Bank regulators routinely examine institutions for compliance with these obligations and they must consider an institution’s AML compliance when considering regulatory applications filed by the institution, including applications for banking mergers and acquisitions. The regulatory authorities have imposed “cease and desist” orders and civil money penalty sanctions against institutions found to be violating these obligations.

Further, on January 1, 2021, Congress passed the National Defense Authorization Act, which enacted the most significant overhaul of the BSA and related AML laws since the USA PATRIOT Act. Notable amendments include (1) significant changes to the collection of beneficial ownership information and the establishment of a beneficial ownership registry, which requires corporate entities (generally, any corporation, limited liability company, or other similar entity with 20 or fewer employees and annual gross income of \$5 million or less) to report beneficial ownership information to FinCEN (which will be maintained by FinCEN and made available upon request to financial institutions); (2) enhanced whistleblower provisions, which provide that one or more whistleblowers who voluntarily provide original information leading to the successful enforcement of violations of the anti-money laundering laws in any judicial or administrative action brought by the Secretary of the Treasury or the Attorney General resulting in monetary sanctions exceeding \$1 million (including disgorgement and interest but excluding forfeiture, restitution, or compensation to victims) will receive not more than 30 percent of the monetary sanctions collected and will receive increased protections; (3) increased penalties for violations of the BSA; (4) improvements to existing information sharing provisions that permit financial institutions to share information relating to suspicious activity reports (SARs) with foreign branches, subsidiaries, and affiliates (except those located in China, Russia, or certain other jurisdictions) for the purpose of combating illicit finance risks; and (5) expanded duties and powers of FinCEN. Many of the amendments, including those with respect to beneficial ownership, require the Department of Treasury and FinCEN to promulgate rules.

On September 29, 2022, FinCEN issued a final rule establishing a beneficial ownership information reporting requirement, pursuant to the CTA. The rule requires most corporations, limited liability companies, and other entities created in or registered to do business in the United States to report information about their beneficial owners—the persons who ultimately own or control the company, to FinCEN. On December 22, 2023, FinCEN issued a final rule regarding access by authorized recipients to beneficial ownership information that will be reported to FinCEN pursuant to Sec. 6403 of the CTA, which is part of the NDAA. The regulations implement strict protocols required by the CTA to protect sensitive personally identifiable information reported to FinCEN and establish the circumstances in which specified recipients have access to beneficial ownership information, along with data protection protocols and oversight mechanisms applicable to each recipient category. The disclosure of beneficial ownership information to authorized recipients in accordance with appropriate protocols and oversight will help law enforcement and national security agencies prevent and combat money laundering, terrorist financing, tax fraud, and other illicit activity, as well as protect national security.

**Office of Foreign Assets Control (“OFAC”) Regulation.** The United States has imposed economic sanctions that affect transactions with designated foreign countries, nationals and others. These are typically known as the OFAC rules based on their administration by OFAC. The OFAC-administered sanctions targeting countries take many different forms. Generally, however, they contain one or more of the following elements: (i) restrictions on trade with, or investment in, a sanctioned country, including prohibitions against direct or indirect imports from and exports to a sanctioned country and prohibitions on “U.S. persons” engaging in financial transactions relating to making investments in, or providing investment-related advice or assistance to, a sanctioned country; and (ii) the blocking of assets in which the government or specially designated nationals of the sanctioned country have an interest by prohibiting transfers of property subject to U.S. jurisdiction (including property in the possession or control of U.S. persons). Blocked assets (e.g., property and bank deposits) cannot be paid out, withdrawn, set off or transferred in any manner without a license from OFAC. The Bank is responsible for, among other things, blocking accounts of, and transactions with, such targets and countries, prohibiting unlicensed trade and financial transactions with them and reporting blocked transactions after their occurrence. Failure to comply with these sanctions could have serious legal and reputational consequences.

**Consumer Financial Protection Bureau (“CFPB”).** The CFPB was created under the Dodd-Frank Act to centralize responsibility for consumer financial protection with broad rulemaking, supervision and enforcement authority over a wide range of consumer protection laws that apply to all banks and thrifts, including the Equal Credit Opportunity Act, Truth in Lending Act (“TILA”), Real Estate Settlement Procedures Act, Fair Credit Reporting Act, Home Mortgage Disclosure Act, Truth in Savings Act, Fair Debt Collection Act, the consumer financial privacy provisions of the GLBA and certain other statutes. Banking institutions with total assets of \$10.0 billion or less, such as the Bank, remain subject to the supervision and enforcement of their primary federal banking regulator with respect to the federal consumer financial protection laws and such additional regulations as may be adopted by the CFPB.

**Community Reinvestment Act.** The CRA and the regulations issued thereunder are intended to encourage banks to help meet the credit needs of their entire communities, including low- and moderate-income neighborhoods, consistent with safe and sound operations. The regulators examine banks and assign each bank a public CRA rating. The CRA then requires bank regulators to take into account the bank’s record of meeting the needs of its community when considering certain applications by a bank, including applications to establish a banking center or to conduct certain mergers or acquisitions. The Federal Reserve is also required to consider the CRA records of a bank holding company’s controlled banks when considering an application by the bank holding company to acquire a bank or to merge with another bank holding company.

The federal banking agencies have adopted regulations which measure a bank’s compliance with its CRA obligations on a performance based evaluation system. This system bases CRA ratings on an institution’s actual lending service and investment performance rather than the extent to which the institution conducts needs assessments, documents community outreach or complies with other procedural requirements. The ratings range from a high of “outstanding” to a low of “substantial noncompliance.” The Bank had a CRA rating of “satisfactory” as of its most recent CRA assessment.

An unsatisfactory CRA record could substantially delay approval or result in denial of an application. See “Risk Factors—Risks Related to Our Regulatory Environment—We are subject to numerous laws designed to protect consumers, including the CRA and fair lending laws, and failure to comply with these laws could lead to a wide variety of sanctions.”

**Regulation Z.** On April 5, 2011, the Federal Reserve’s final rule on loan originator compensation and steering (Regulation Z) became final. Regulation Z is more commonly known as the regulation that implements TILA. Regulation Z address two components of mortgage lending, i.e., loans secured by a dwelling, and implements restrictions and guidelines for: (i) prohibited payments to loan originators, and (ii) prohibitions on steering. Under Regulation Z, a creditor is prohibited from paying, directly or indirectly, compensation to a mortgage broker or any other loan originator that is based on a mortgage transaction’s terms or conditions, except the amount of credit extended, which is deemed not to be a transaction term or condition. In addition, Regulation Z prohibits a loan originator from “steering” a consumer to a lender or a loan that offers less favorable terms in order to increase the loan originator’s compensation, unless the loan is in the consumer’s interest. Regulation Z also contains a record-retention provision requiring that, for each transaction subject to Regulation Z, the financial institution maintain records of the compensation it provided to the loan originator for that transaction as well as the compensation agreement in effect on the date the interest rate was set for the transaction. These records must be maintained for two years.

**UDAP and UDAAP.** Banking regulatory agencies have increasingly used a general consumer protection statute to address “unfair”, “deceptive” or “abusive” acts and business practices that may not necessarily fall directly under the purview of a specific banking or consumer finance law. Section 5 of the Federal Trade Commission Act, referred to as the FTC Act, is the primary federal law that prohibits unfair or deceptive acts or practices, referred to as UDAP, and unfair methods of competition in or affecting commerce. “Unjustified consumer injury” is the principal focus of the FTC Act. UDAP laws and regulations were expanded under the Dodd-Frank Act to apply to “unfair, deceptive or abusive acts or practices” referred to as UDAAP, and were delegated to CFPB for rulemaking. The federal banking agencies have the authority to enforce such rules and regulations. Under the Dodd-Frank Act, CFPB looks to various factors to assess whether an act or practice is unfair, including whether it causes or is likely to cause substantial injury to consumers, the injury is not reasonably avoidable by consumers, and the injury is not outweighed by countervailing benefits to consumers or to competition. A key focus of CFPB is whether an act or practice hinders a consumer’s decision-making.

### ***Incentive Compensation Guidance***

The federal bank regulatory agencies have issued comprehensive guidance intended to ensure that the incentive compensation policies of banking organizations do not undermine the safety and soundness of those organizations by encouraging excessive risk-taking. The incentive compensation guidance sets expectations for banking organizations concerning their incentive compensation arrangements and related risk-management, control and governance processes. The incentive compensation guidance, which covers all employees that 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: (1) balanced risk-taking incentives; (2) compatibility with effective controls and risk management; and (3) strong corporate governance. Any deficiencies in compensation practices that are identified may be incorporated into the organization’s supervisory ratings, which can affect its ability to make acquisitions or take other actions. In addition, under the incentive compensation guidance, a banking organization’s federal supervisor may initiate enforcement action if the organization’s incentive compensation arrangements pose a risk to the safety and soundness of the organization. Further, the Basel III capital rules limit discretionary bonus payments to bank executives if the institution’s regulatory capital ratios fail to exceed certain thresholds.

In October 2022, the SEC adopted a final rule directing national securities exchanges and associations, including the NASDAQ, to implement listing standards that require listed companies to adopt policies mandating the recovery or “clawback” of excess incentive-based compensation earned by a current or former executive officer during the three fiscal years preceding the date the listed company is required to prepare an accounting restatement, including to correct an error that would result in a material misstatement if the error were corrected in the current period or left uncorrected in the current period. The final rule requires the Company to adopt a clawback policy within 60 days after such listing standard becomes effective. In accordance with Rule 10D-1 promulgated by the SEC under the Exchange Act and Nasdaq Listing Rule 5608, the Company adopted and implemented a compensation recovery policy, effective as of October 2, 2023.

**Other Regulations.** The Bank’s operations are also subject to various federal laws such as the:

- 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 and its amendment, the Fair and Accurate Credit Transactions Act of 2003, governing the use and provision of information to credit reporting agencies;
- Fair Debt Collection Act, governing the manner in which consumer debts may be collected by collection agencies;

- Right to Financial Privacy Act, which imposes a duty to maintain the confidentiality of consumer financial records and prescribes procedures for complying with administrative subpoenas of financial records; and
- Electronic Funds Transfer Act and Regulation E issued by the Federal Reserve to implement that act, which govern automatic deposits to, and withdrawals from, deposit accounts and customers' rights and liabilities arising from the use of automated teller machines and other electronic banking services.

**Effect of Governmental Monetary Policies.** The commercial banking business is affected not only by general economic conditions but also by the monetary policies of the Federal Reserve. Some of the instruments of monetary policy available to the Federal Reserve include changes in the discount rate on member bank borrowings, the fluctuating availability of borrowings at the "discount window," open market operations, the imposition of, and changes in, reserve requirements against member banks' deposits and assets of foreign branches, the imposition of, and changes in, reserve requirements against certain borrowings by banks and their affiliates and the placing of limits on interest rates that member banks may pay on time and savings deposits. Such policies influence to a significant extent the overall growth of bank loans, investments and deposits as well as the interest rates charged on loans or paid on time and savings deposits. We cannot predict the nature of future fiscal and monetary policies and the effect of such policies on our future business and our earnings.

**Environmental Laws Potentially Impacting the Bank.** We are subject to state and federal environmental laws and regulations. The Comprehensive Environmental Response, Compensation and Liability Act, ("CERCLA"), is a federal statute that generally imposes strict liability on all prior and present "owners and operators" of sites containing hazardous waste. However, Congress acted to protect secured creditors by providing that the term "owner and operator" excludes a person whose ownership is limited to protecting its security interest in the site. Since the enactment of the CERCLA, this "secured creditor exemption" has been the subject of judicial interpretations which have left open the possibility that lenders could be liable for cleanup costs on contaminated property that they hold as collateral for a loan, which costs often substantially exceed the value of the property.

**Regulatory Reform and Legislation.** From time to time, various legislative and regulatory initiatives are introduced in Congress, as well as by regulatory agencies. These initiatives and others may at times include proposals to expand or contract the powers of bank holding companies and depository institutions or proposals to substantially change the financial institution regulatory system. Such legislation could change banking statutes and the operating environment of the Company or the Bank in substantial and unpredictable ways. If enacted, such legislation could increase or decrease the cost of doing business, limit or expand permissible activities or affect the competitive balance among banks, savings associations, credit unions and other financial institutions. The Company cannot predict whether any such legislation will be enacted, and, if enacted, the effect that it, or any implementing regulations, would have on the financial condition or results of operations of the Company. A change in statutes, regulations or regulatory policies applicable to the Company or our subsidiaries could have a material effect on the Company's business, financial condition and results of operations.

#### **Broker-Dealer Regulation**

The securities industry is heavily regulated. The SEC is responsible for the administration of the federal securities laws and serves as a supervisory body over all national securities exchanges and associations. The regulation of broker-dealers has, to a large extent, been delegated by the federal securities laws to the FINRA and other self-regulatory organizations ("SROs"). These SROs include, among others, all the national securities and commodities exchanges and the FINRA. Subject to approval by the SEC and certain other regulatory authorities, SROs adopt rules that govern the industry and conduct periodic examinations of the operations of our broker-dealer subsidiary. Sanders Morris is registered in all 50 states and is also subject to regulation under the laws of these jurisdictions.

**Broker-Dealer Net Capital Rules.** As a registered broker-dealer and member of FINRA, Sanders Morris is subject to certain net capital requirements of Rule 15c3-1 under the Exchange Act. The net capital rules, which specify minimum net capital requirements for registered broker-dealers, are designed to measure the financial soundness and liquidity of broker-dealers. Failure to maintain the required net capital may subject a firm to suspension or revocation of registration by the SEC and suspension or expulsion by other regulatory bodies, and ultimately may require its liquidation. Further, a decline in a broker-dealer's net capital below certain "early warning levels," even though above minimum capital requirements, could cause material adverse consequences for the broker-dealer. Sanders Morris conducts business on a national basis as an introducing firm, using a third-party firm for securities clearing and custody functions.

**Broker-Dealer Supervision.** Sanders Morris is subject to other rules and regulations covering all aspects of the securities business, including sales and trading practices, public offerings, use and safekeeping of clients' funds and securities, recordkeeping and reporting, and the conduct of directors, officers and employees. Broker-dealers are also regulated by state securities administrators in those jurisdictions where they do business. Compliance with many of the rules and regulations applicable to us involves a number of risks because the rules and regulations are subject to varying interpretations. Regulators make periodic examinations and review annual, monthly and other reports on Sanders Morris' operations, track record and financial condition. Violations of rules and regulations governing a broker-dealer's actions could result in censure, penalties and fines, the issuance of cease-and-desist orders, the suspension or expulsion from the securities industry of such broker-dealer or its officers or employees, or other similar adverse consequences. The rules of the Municipal Securities Rulemaking Board, which are enforced by the SEC and FINRA, apply to the municipal securities activities of Sanders Morris.

**Anti-Money Laundering.** Sanders Morris, like the Bank, is subject to the BSA and the USA PATRIOT Act. These acts contain anti-money laundering and financial transparency laws and mandate the implementation of various regulations applicable to broker-dealers and other financial services companies. Sanders Morris, like the Bank, has established policies, procedures and systems designed to comply with these regulations.

**Securities Investor Protection Corporation ("SIPC").** As a registered broker-dealer and FINRA member organization, Sanders Morris is required by federal law to belong to the SIPC, which provides, in the event of the liquidation of a broker-dealer, protection for securities held in customer accounts held by the firm of up to \$500,000 per customer, subject to a limitation of \$250,000 on claims for cash balances. SIPC is principally funded through assessments on registered broker-dealers. SIPC protection does not insure against fluctuations in the market value of securities.

**Regulation BI and Form CRS Relationship Summary ("Form CRS").** On June 5, 2019, the SEC adopted Regulation Best Interest ("Regulation BI"), elevating the standard of care for broker-dealers from the current "suitability" requirement to a "best interest" standard when making a recommendation of any securities transaction to a retail customer. The "best interest" standard requires a broker-dealer to make recommendations without putting its financial interests ahead of the interests of a retail customer. The SEC also adopted Form CRS, which requires registered investment advisors ("RIAs") and broker-dealers to deliver to retail investors a succinct, plain English summary about the relationship and services provided by the firm and the required standard of conduct associated with the relationship and services. In connection with adopting Regulation BI, the SEC added new record-making and recordkeeping rules. The compliance date for Regulation BI and the related rules is June 30, 2020, and Sanders Morris and Tectonic Advisors met this requirement. Regulation BI imposes disclosure and policy and procedural obligations that could impact the compensation our wealth management business and its representatives receive for selling certain types of products, particularly those that offer different compensation across different share classes (such as mutual funds and variable annuities). In addition, Regulation BI prohibits a broker-dealer and its associated persons from using the term "adviser" or "advisor" if the broker-dealer is not an RIA or the associated person is not a supervised person of an RIA.

#### **Investment Advisor Regulation**

As registered investment advisors under the Investment Advisers Act of 1940 (the "Advisers Act"), Tectonic Advisors and Sanders Morris are subject to the requirements of regulations under both the Advisers Act and certain state securities laws and regulations. Such requirements relate to, among other things, limitations on the ability of investment advisors to charge performance-based or non-refundable fees to clients, record-keeping and reporting requirements, disclosure requirements, limitations on principal transactions between an advisor or its affiliates and advisory clients, and general anti-fraud prohibitions.

**ERISA.** Certain of our subsidiaries are subject to the Employee Retirement Income Security Act ("ERISA") and Sections 4975(c)(1)(A), (B), (C) or (D) of the Internal Revenue Code of 1986, as amended (the "Code"), and to regulations promulgated thereunder, insofar as they are a "fiduciary" under ERISA with respect to benefit plan clients or otherwise deal with benefit plan clients. ERISA and applicable provisions of the Code impose certain duties on persons who are fiduciaries under ERISA, prohibit certain transactions involving ERISA plan clients (including, without limitation, employee benefit plans (as defined in Section 3(3) of ERISA), individual retirement accounts and Keogh plans) and provide monetary penalties for violations of these prohibitions.

**Investment Advisor Supervision.** The SEC is authorized to institute proceedings and impose sanctions for violations of the Advisers Act, ranging from fines and censure to termination of an investment adviser's registration. Investment advisers also are subject to certain state securities laws and regulations. Non-compliance with the Advisers Act or other federal and state securities laws and regulations could result in investigations, sanctions, disgorgement, fines or other similar consequences.

## Insurance Regulation

HWG is an insurance agency registered with the TDI. It provides life, disability, property and casualty insurance to clients. Regulation of insurance brokerage is generally performed at a state, rather than a national, level. HWG operates in multiple states/jurisdictions, and as a result, both HWG and its employees are subject to various state regulatory and licensing requirements. HWG monitors compliance with the various state insurance regulators, and also has relationships with third party vendors to ensure compliance and awareness among HWG and its employees of relevant requirements and changes, and emerging regulatory issues.

### Item 1A. Risk Factors.

*Our business and results of operations are subject to numerous risks and uncertainties, many of which are beyond our control. The material risks and uncertainties that management believes affect the Company are described below. Additional risks and uncertainties that management is not aware of, or that management currently deems immaterial, may also impair the Company's business operations. This Form 10-K is qualified in its entirety by these risk factors. If any of the following risks actually occur, our business, financial condition and results of operations could be materially and adversely affected. If this were to happen, the value of our securities could decline significantly, and you could lose all or part of your investment. Some statements in the following risk factors constitute forward-looking statements. Please refer to "Cautionary Note Regarding Forward-Looking Statements" elsewhere in this Form 10-K.*

### Summary of Risk Factors

Below is a summary of the principal factors that we believe make an investment in our securities risky. This summary does not address all of the risks that we face. Additional discussion of the risks summarized in this risk factor summary, and other risks that we face, can be found below and should be carefully considered, together with other information in this Form 10-K and our other filings with the SEC, before making an investment decision regarding our securities.

#### Risks Related to Our Business:

- Liquidity risk, including our ability to maintain our deposit base or other funding sources, could adversely affect our ability to fund operations and hurt our financial condition.
- We depend on wholesale funding sources, which causes our cost of funds to be higher and poses future funding risks if the Bank becomes less than "well capitalized", which may require us to liquidate loans or impede our growth.
- We may not be able to grow and maintain our deposit base or other funding sources, and deposit outflows may increase reliance on wholesale borrowings and brokered deposits.
- We are subject to interest rate risk and changes in interest rates could affect our net interest margins and net interest income, the value of assets and obligations, and the availability and cost of capital or liquidity.
- Our securities portfolio is subject to risk of loss; the fair value of our investment securities can fluctuate due to factors outside of our control.
- We are subject to consolidated capital ratio requirements and therefore have to hold additional capital.
- If we are unable to sell additional services and products to existing clients or attract new clients in a manner that is cost-effective and assures client success, we will not be able to grow our business.
- We may not be able to implement aspects of our expansion strategy, which may adversely affect our ability to maintain our historical earnings trends.
- New lines of business or new products and services may subject us to additional risks.
- Acquisitions may subject us to integration risks and other unknown risks.
- Growth of our business could result in increased costs.
- The soundness of other financial institutions could adversely affect us. Negative public opinion regarding us or failure to maintain our reputation in the communities we serve could adversely affect our business and prevent us from growing our business.
- Significant revenues and profits are generated as a result of our relationship with Cain Watters, and a change in the relationship or decline in Cain Watters' business could adversely affect us.
- We depend on key personnel, and may have difficulty identifying, attracting and retaining necessary personnel to execute our business strategy and successfully expand our operations. This risk includes the risk of retirement of key professionals in leadership roles, including loan officers, members of our SBA team, and financial advisors and brokers.
- The employment market has become increasingly competitive; We may have difficulty attracting and retaining skilled personnel.
- A decline in general business and economic conditions and any regulatory responses to such conditions could have a material adverse effect on our business, financial position, results of operations and growth prospects.



- Lower trucking margins and revenues negatively impact trucking industry and factoring.
- Our business is concentrated in, and dependent upon, the continued growth and welfare of our primary market, and adverse economic conditions in such market could negatively impact our operations and clients.
- We have a loan concentration related to the acquisition and financing of dental practices.
- A governmental shutdown or curtailment of government guaranteed loan programs could affect a segment of our business.
- We face specific risks associated with retention of unguaranteed portions of SBA loans.
- Commercial lending generally involves a higher degree of risk than retail residential mortgage lending.
- The level of our commercial real estate loan portfolio may subject us to heightened regulatory scrutiny.
- Our factoring services through the Bank's Integra Division are concentrated in the transportation industry and economic conditions or other factors negatively impacting the transportation industry could adversely affect our factoring business.
- The success of our trust services is dependent upon market fluctuations and a non-diversified source for its growth.
- We are subject to possible claims and litigation pertaining to fiduciary responsibility.
- We could suffer material credit losses. Our levels of nonperforming assets could increase, which could adversely affect our results of operations and financial condition, and could result in losses in the future.
- Our allowance for credit losses may not be sufficient to absorb actual losses.
- The small- to medium-sized businesses that we lend to may have fewer resources to weather adverse business conditions, which may impair their ability to repay a loan, and such impairment could adversely affect our results of operations and financial condition.
- Our commercial finance clients, particularly with respect to the Bank's Integra Division, may lack the operating history, cash flows or balance sheet necessary to support other financing options and may expose us to additional credit risk, especially if our additional controls for such products are ineffective in mitigating such additional risks.
- Certain of our loans are not secured by property but dependent on the earning capacity of the borrower. The Company's use of appraisals in deciding whether to make a loan on or secured by real property does not ensure the value of the real property collateral.
- Fee revenue will represent a significant portion of our consolidated revenue and is subject to decline, among other things, in the event of a reduction in, or changes to, the level or type of investment activity by our clients and market declines.
- The business operations of Sanders Morris may face limitations due to net capital requirements.
- The wealth management, trust and brokerage business is highly competitive. If we are not able to compete successfully against current and future competitors, our business, financial condition, and results of operations will be adversely affected.
- Underperformance or declines in our investments may reduce the profitability of our wealth management and advisory business.
- Our wealth management and brokerage business is subject to reputational risk.
- Standard investment management contracts we have with our clients are terminable without cause and on relatively short notice by our clients.
- We continue to experience pricing pressures in areas of our business which may impair our future revenue and profitability.
- We face strong competition from other insurance agencies, which may adversely affect our operations and financial condition.
- A failure to appropriately identify and address potential conflicts of interest could adversely affect our businesses. We may incur significant losses due to ineffective risk management processes and strategies.
- If we fail to maintain effective internal control over financial reporting, we may not be able to report our financial results accurately and timely, in which case our business may be harmed.
- Our estimates and assumptions in the preparation of our financial statements may not be accurate.
- We may be required to recognize a significant charge to earnings if our goodwill or other intangible assets become impaired.
- We may elect or be compelled to seek additional capital, but that capital may not be available, or it may be dilutive.
- We face intense competition from larger banks and financial institutions that could hurt our business.
- A third party systems failure could significantly disrupt our business, result in regulatory action against us, or limit our growth.
- Fraudulent activity, breaches of our information security, and cybersecurity attacks could adversely affect our ability to conduct our business, manage our exposure to risk, result in the disclosure or misuse of confidential or proprietary information, increase our costs to maintain and update our operational and security systems and infrastructure, and adversely impact our results of operations, liquidity and financial condition, as well as cause legal or reputational harm.
- Factoring products offered by the Bank's Integra Division may expose us to an increased risk of fraud.
- We rely on client and counterparty information, which subjects us to risks if that information is not accurate or is incomplete.
- Climate change and related legislative and regulatory initiatives may materially affect the Company's business and results of operations.
- The Company is subject to environmental risks associated with owning real estate or collateral.

Risks Related to Our Regulatory Environment:

- We are subject to extensive government regulation and supervision, which could constrain our growth and profitability.
- Recent bank failures and the related negative impact on customer confidence in the safety and soundness of the banking industry may adversely affect our business, earnings and financial condition.
- Federal banking agencies periodically conduct examinations of our banking business, and our failure to comply with any supervisory actions which we are, or may become, subject to as a result of such examinations may adversely affect us.
- We are subject to numerous laws designed to protect consumers and failure to comply with these laws could lead to a wide variety of sanctions.
- We face a risk of noncompliance and enforcement action with the BSA and other anti-money laundering laws.
- Additional regulations and rule making impacting the transportation industry may have a disproportionate impact on the small-to-mid-sized trucking businesses that comprise our primary transportation factoring clients and adversely affect the factoring business conducted by the Bank's Integra Division.
- Sanders Morris and Tectonic Advisors are subject to substantial regulation and failure to comply with applicable requirements will adversely affect our business.
- Regulations relating to privacy, information security and data protection could increase our costs, affect or limit how we collect and use personal information and adversely affect our business opportunities.
- We can be subject to legal and regulatory proceedings, investigations and inquiries related to conduct risk.

Risks Related to an Investment in the Series B Preferred Stock:

- The Series B preferred stock is subordinate to our existing and future indebtedness, which could adversely impact our ability to pay dividends on the Series B preferred stock.
- The Series B preferred stock may be junior in rights and preferences to our future preferred stock. Additional issuances of preferred stock or securities convertible into preferred stock may dilute existing holders.
- Dividends on the Series B preferred stock are discretionary and non-cumulative, and our future ability to pay dividends is subject to restrictions.
- The replacement of the London Inter-bank Offered Rate ("LIBOR") on our Series B preferred stock with the Secured Overnight Financing Rate ("SOFR") could increase our interest payments and may adversely affect the value of the Series B preferred stock. Dividends on the Series B preferred stock will vary beginning on May 15, 2024 and any dividends declared may be less than the initial fixed annual rate in effect prior to May 15, 2024.
- The Series B preferred stock may be redeemed at our option, and you may not be able to reinvest the redemption price you receive in a similar security.
- Investors should not expect us to redeem the Series B preferred stock on or any time after the date it becomes redeemable.
- Holders of the Series B preferred stock have limited voting rights.
- A liquid market for the Series B preferred stock may not be sustained, which may impair your ability to sell your shares.
- The market price of the Series B preferred stock may become subject to substantial fluctuations.
- Securities analysts may not continue coverage on us.
- The Series B preferred stock is not rated.
- Subject to regulatory requirements and the terms of the Series B preferred stock, the Company may, and currently intends to, pay dividends on its common stock and any such payment reduces the capital of the Company available to the Series B preferred stock.
- Our management and board of directors have significant control over our business.
- We are a "controlled company" within the meaning of the rules of NASDAQ, and as such, we qualify for exemptions from certain corporate governance requirements. As a result, you may not have the same protections afforded to shareholders of companies that are subject to such requirements.
- The interests of our controlling shareholders may not coincide with yours and with whose decisions you may disagree.
- Our corporate organizational documents and provisions of federal and state law to which we are subject contain certain provisions that could have an anti-takeover effect and may delay, make more difficult or prevent an attempted acquisition that you may favor or an attempted replacement of our board of directors or management.
- We are an "emerging growth company," and the reduced reporting requirements applicable to emerging growth companies may make the Series B preferred stock less attractive to investors.
- An investment in the Series B preferred stock is not an insured deposit and is subject to risk of loss.



## Risks Related to Our Business

***Liquidity risk, including our ability to maintain our deposit base or other funding sources, could adversely affect our ability to fund operations and hurt our financial condition.***

Liquidity is essential to our banking business, as we use cash to make loans and purchase investment securities and other interest-earning assets and to fund deposit withdrawals that occur in the ordinary course of our business. Our principal sources of liquidity include earnings, deposits, repayment by clients of loans we have made to them, and the proceeds from sales by us of our equity securities or from borrowings that we may obtain. In addition, from time to time, we borrow from the FHLB. Potential alternative sources of liquidity include the sale of loans, the acquisition of national market non-core deposits, the issuance of additional collateralized borrowings such as the FHLB, advances, access to the Federal Reserve discount window, the BTFP and the issuance of additional equity securities and/or debt.

If our ability to obtain funds from these sources becomes limited, these sources become restricted or are eliminated, or the costs of those funds increase, or we are unable to effectively manage the repayment and maturity schedules of our loans and investment securities, whether due to factors that affect us specifically, including our financial performance, or due to factors that affect the financial services industry in general, including weakening economic conditions or negative views and expectations about the prospects for the financial services industry as a whole, then our ability to grow our banking and investment advisory and trust businesses would be harmed, which could have a material adverse effect on our business, financial condition, results of operations and prospects. Further, the Company may incur substantially higher funding costs in order to obtain the necessary funds to support the Company's operations and growth or may be required to sell or restrict operations, or restrict the payment of dividends. Furthermore, if the Company is unable to raise adequate funds through external sources, the Company may need to sell assets with unrealized losses in order to generate additional liquidity, which could decrease the capital of the Company and have an adverse effect on our business, financial condition and results of operations.

***We depend on wholesale funding sources, which causes our cost of funds to be higher when compared to other financial institutions and poses future funding risks if the Bank becomes less than “well capitalized” under the prompt corrective action framework, or PCA, which may require us to liquidate loans or impede our growth.***

We use certain non-core, wholesale funding sources, including the FHLB advances and deposit listing services. As of December 31, 2023, our use of such wholesale funding sources amounted to approximately \$286 million, or 51.8% of total funding. Although we intend to increase our efforts to reduce our reliance on wholesale funding sources, we may not be able to increase our market share of core-deposit funding in our highly competitive market area. We further expect to increase our core funding as we develop the capacity for consumers to open on-line digital accounts. The rates on these digital accounts can be highly competitive and may increase our cost of funds, which could have a material adverse effect on our net interest income margins. Listing service deposit rates are very market sensitive. At times, the cost of these funds can exceed the cost of core deposits in our market area as well as digital deposits, which could have a material adverse effect on our net interest income margins. Wholesale funding is subject to certain practical limits such as the FHLB's and BTFP's maximum borrowing capacity and our liquidity targets. Our maximum borrowing capacity from the FHLB and BTFP is based on the amount and fair market value and face amount, respectively, of commercial loans and securities we can pledge. If we are unable to pledge sufficient collateral to secure funding from the FHLB, we may lose access to this source of liquidity that we have historically relied upon. Additionally, we are required to establish limits on certain types of deposits including brokered deposits and listing service deposits, as well as total wholesale funding sources. If we reach these limits, future asset growth may be reduced or halted. If we are unable to access any of these types of funding sources or if our costs related to them increase, our liquidity and ability to support demand for loans could be materially adversely affected. If we were not able to replace such wholesale funding, we may have to liquidate loans, which may be at losses that would have a material adverse effect on our capital, our business and your investment in the Company.

***We may not be able to grow and maintain our deposit base, and deposit outflow may increase reliance on wholesale borrowings and brokered deposits.***

Our future growth will largely depend on our ability to maintain and grow our deposit base and our ability to retain our trust clients, who provide deposits. As of December 31, 2023, the Bank had a loan to deposit ratio of 93.9%. In the current environment of elevated interest rates, our deposits may not be as stable or as interest rate insensitive as similar deposits may have been in the past, and some existing or prospective deposit customers of banks generally, including the Bank, may be inclined to pursue other investment alternatives, which may negatively impact our net interest margin. Additionally, negative news about the Company or the Bank, or the banking industry in general, could negatively impact market and/or customer perceptions of the Company and the Bank, which could lead to a loss of depositor confidence and an increase in deposit withdrawals. The account and deposit balances can decrease when clients perceive alternative investments, such as the stock market or real estate, as providing a better risk/return tradeoff. In addition, if interest rates rise, competition for deposits may increase, which could result in clients moving money out of the Bank. As a general matter, deposits are typically a lower cost source of funds than external wholesale funding (brokered deposits and borrowed funds), because interest rates paid for deposits are typically less than interest rates charged for wholesale funding. If, as a result of competitive pressures, market interest rates, alternative investment opportunities that present more attractive returns to customers, general economic conditions or other events, the balance of the Company's deposits decreases relative to the Company's overall banking operations, the Company may have to rely more heavily on wholesale or other sources of external funding, or may have to increase deposit rates to maintain deposit levels in the future. Any such increased reliance on wholesale funding, or increases in funding rates in general, could have a negative impact on the Company's net interest income and, consequently, on its results of operations and financial condition. Furthermore, the portion of our deposit portfolio that is comprised of large uninsured deposits may be more likely to be withdrawn rapidly under adverse economic conditions. If our clients, including our trust clients, move money out of bank deposits into investments or to other financial institutions, we could lose a relatively low-cost source of funds, increasing our funding costs and reducing our net interest income and net income.

***The Company is subject to interest rate risk and changes in interest rates could affect our net interest margins and net interest income, the value of our assets and obligations, and the availability and cost of capital or liquidity.***

Our profitability is dependent to a large extent on our net interest income, which is the difference between interest income we earn as a result of interest paid to us on loans and investments and interest we pay to third parties such as our depositors and those from whom we borrow funds. As interest rates change, net interest income is affected.

Interest rates are highly sensitive to many factors that are beyond our control, including (among others) general and regional and local economic conditions, the monetary policies of the Federal Reserve, bank regulatory requirements, competition from other banks and financial institutions and a change over time in the mix of our loans and investment securities, on the one hand, and on our deposits and other liabilities, on the other hand. Sustained low levels of market interest rates, as we have experienced prior to 2022, would continue to place downward pressure on our net interest margins and, therefore, on our earnings. Conversely, increases in interest rates, though they could increase our interest margins absent a commensurate rise in our cost of funds, also have the potential to affect borrowers' ability to repay, particularly for the small and medium sized businesses to which we lend, subjecting us to potential loan losses. This effect could be exacerbated by an inflationary environment. In 2022 and 2023, the Federal Open Market Committee ("FOMC") of the Federal Reserve repeatedly raised their target benchmark interest rate in response to the ongoing inflationary environment in the United States, resulting in subsequent prime rate increases of 525 basis points between March of 2022 and July of 2023. Further, substantially higher interest rates generally reduce loan demand and may result in slower loan growth and may encourage current borrowers to repay loans early. All of these factors are detrimental to our business, and the interplay between these factors can be complex and unpredictable.

Our net interest margins and earnings also could be adversely affected if we are unable to adjust our interest rates on loans and deposits on a timely basis in response to changes in economic conditions or monetary policies. For example, if the rates of interest we pay on deposits, borrowings and other interest-bearing liabilities increase faster than we are able to increase the rates of interest we charge on loans or the yields we realize on investments and other interest-earning assets, our net interest income and, therefore, our earnings will decrease. Conversely, in an environment of decreasing interest rates, loan originations may also decline, and our borrowers may experience difficulties meeting their obligations or seek to refinance their loans for lower rates, which may adversely affect income from these lending activities and negatively impact our net interest margin. These circumstances could not only result in increased loan defaults, foreclosures and charge-offs, but also reduce collateral values and necessitate further increases to the allowance for credit losses, which could have a material adverse effect on our business, financial condition and results of operations. Also, changes in interest rates might impact the values of equity and debt securities under management and administration, which may have a negative impact on fee income.

Further, rising short-term interest rates are likely to result in declines in both fixed income (bond) and stock prices. Declining fixed income and stock prices will result in a decline in the value and potentially the volume of both trust assets on which the Bank provides fiduciary services and the assets under management at Tectonic Advisors and Sanders Morris, as well as declining capital markets, private placement and brokerage activities of Sanders Morris – as does an economic recession. This will have an adverse impact on the revenues and earnings of the Company. An economic recession will also result in higher losses on the Bank's loan portfolio and its factored receivables portfolio and decreased economic activity, both of which negatively impact Bank earnings and capital. Thus, an economic recession negatively impacts almost every aspect of the Company's business and will have a negative and adverse effect on the earnings, capital and financial position of the Company.

***Our securities portfolio is subject to risk of loss; the fair value of our investment securities can fluctuate due to factors outside of our control.***

As of December 31, 2023, the fair value of our investment securities portfolio was \$46.8 million. The Bank invests a portion of its assets in U.S. Treasuries, U.S. government agencies, mortgage-backed securities, direct obligations of quasi government agencies including Fannie Mae, Freddie Mac, and the FHLB, and federal funds sold. In addition, the Bank may make investments in certain municipal or state obligations or securities that it believes have a similar risk profile thereto, or Other Securities. Other Securities include, among other things, securities issued pursuant to PACE and PID/TIRZ programs. These programs are created by state and local municipalities to finance energy efficiency upgrades or renewable energy installations for residential, commercial and industrial property owners. Investments in instruments other than U.S. Treasuries carry a degree of risk, including risk of default, market fluctuations and lack of liquidity.

Factors beyond our control can significantly influence and cause adverse changes to occur in the fair values of securities in that portfolio. These factors include, but are not limited to, rating agency actions in respect of the investment securities in our portfolio, defaults by the issuers of such securities, concerns with respect to the enforceability of the payment or other key terms of such securities, changes in market interest rates, continued instability in the capital markets and lack of liquidity or marketability. Any of these factors, as well as others, could cause other-than-temporary impairments and realized or unrealized losses in future periods and declines in other comprehensive income, which could materially and adversely affect our business, results of operations, financial condition and prospects. As discussed above, the FOMC repeatedly raised their target benchmark interest rate in 2022 and 2023, resulting in subsequent prime rate increases of 525 basis points between March of 2022 and July of 2023, and further resulting in a significant increase in market interest rates during the year ended December 31, 2023. If market interest rates continue to rise, the market value of the fixed income bond portfolio will decrease, resulting in unrealized losses, and depending on the extent of the rise in interest rates, the increase in unrealized losses could be significant over the short-term. The non-credit portion of unrealized losses on the Bank's available for sale securities portfolio are booked to AOCI, a component of shareholders' equity, and unrealized losses net of the related tax effect as of December 31, 2023 totaled \$1.8 million, which represents approximately 1.7% of our total capital. A significant increase in market rates may have a negative impact on book value per common share and return on average shareholders' equity ratios. The Company's bond portfolio is expected to mature at par and therefore the unrealized losses in the portfolio that result from higher market interest rates will decrease as the bonds become closer to maturity. However, if the Company were required to sell investment securities with an unrealized loss for any reason, including liquidity needs, the unrealized loss would become realized and reduce both net income for the reported period and regulatory capital, which as currently reported, excludes unrealized losses on investment securities.

In addition, the process for determining whether an impairment of a security is other-than-temporary usually requires complex, subjective judgments, which could subsequently prove to have been wrong, regarding the future financial performance and liquidity of the issuer of the security, the fair value of any collateral underlying the security and whether and the extent to which the principal of and interest on the security will ultimately be paid in accordance with its payment terms. Further, any loss from any such Other Securities or any other securities in our portfolio would negatively impact the capital of the Bank and such impact could be material.

***We are subject to consolidated capital ratio requirements, and therefore have to hold additional capital.***

Prior to our initial public offering in May 2019, the Company qualified as a "small bank holding company." This meant, among other things, that the Company was not subject to minimum consolidated capital requirements. Upon consummation of the Tectonic Merger, we ceased to qualify as a small bank holding company and must maintain certain minimum capital ratios on a consolidated basis with the Bank. As described further below, our failure to meet capital requirements could, among other things, affect client and investor confidence, our ability to grow, our costs of funds, our ability to pay dividends on preferred and common stock, our ability to make acquisitions, and adversely affect our business, results of operations and financial condition.

***If we are unable to sell additional services and products to existing clients or attract new clients in a manner that is cost-effective and assures client success, we will not be able to grow our business, which could adversely affect our results of operations and financial condition.***

In order to grow our business, we must continue to attract new clients in a cost-effective manner and enable these clients to realize the benefits associated with our products and services. Part of our strategic plan is to market our suite of financial services and products across the clients of our subsidiaries. We may not be able to attract clients from one of our subsidiaries to use another subsidiary for different financial services or products. This could be for a variety of reasons, including as a result of their continued use of our competitors and/or other impediments that hinder their ability to migrate to or adopt our financial products or services. If we are unable to entice existing clients to expand their use of our financial products and services, we may see an increase in our client acquisition costs which could have a material adverse effect on our business, results of operations and financial condition.

***We may not be able to implement aspects of our expansion strategy, which may adversely affect our ability to maintain our historical earnings trends.***

We may not be able to sustain our growth at the rate we have enjoyed during the past several years. A downturn in local economic market conditions, particularly in the real estate market, a failure to attract and retain high performing personnel, heightened competition from other financial services providers, and an inability to attract additional deposits in a cost-effective manner and lending clients, among other factors, could limit our ability to grow as rapidly as we have in the past and as such may have a negative effect on our business, financial condition and results of operations. In addition, risks associated with failing to maintain effective financial and operational controls as we grow, such as maintaining appropriate loan underwriting procedures, determining adequate allowances and complying with regulatory accounting requirements, including increased credit losses, reduced earnings and potential regulatory penalties and restrictions on growth, all could have a negative effect on our business, financial condition and results of operations.

***New lines of business or new products and services may subject us to additional risk.***

From time to time, we may implement new lines of business or offer new products and services within existing lines of business. There are substantial risks and uncertainties associated with these efforts, particularly in instances where the markets are not fully developed. In acquiring, developing and/or marketing new lines of business and/or new products and services, we may invest significant time and resources. Initial timetables for the introduction and development of new lines of business and/or new products or services may not be achieved and price and profitability targets may not prove feasible. External factors, such as compliance with regulations, competitive alternatives, and shifting market preferences, may also impact the successful implementation of a new line of business and/or a new product or service. Furthermore, any new line of business and/or new product or service could have a significant impact on the effectiveness of our system of internal controls. Failure to successfully manage these risks in the integration, development and implementation of new lines of business and/or new products or services could have a material adverse effect on our business and, in turn, our financial condition and results of operations.

***Acquisitions may subject us to integration risks and other unknown risks.***

Although we plan to continue to grow our business organically, we also intend to pursue acquisition opportunities that we believe complement our activities and have the ability to enhance our profitability and provide attractive risk-adjusted returns. Acquisitions involve inherent uncertainty and we cannot determine all potential events, facts and circumstances that could result in loss or increased costs. Our due diligence or risk mitigation efforts may not be sufficient to protect against any such loss or increased costs. Moreover, any acquisitions may require the approval of our bank regulators and we may not be able to obtain such approvals on acceptable terms, if at all.

In addition, certain events may arise after the date of an acquisition, or we may learn of certain facts, events or circumstances after the closing of an acquisition, that may affect our financial condition or performance or subject us to risk of loss. These events include, but are not limited to: retaining key employees and clients, achieving anticipated synergies, meeting expectations and otherwise realizing the undertaking's anticipated benefits; litigation resulting from circumstances occurring at the acquired entity prior to the date of acquisition; loan downgrades and credit loss provisions resulting from underwriting of certain acquired loans determined not to meet our credit standards; personnel changes that cause instability within a department; and other events relating to the performance of our business.

Mergers and acquisitions frequently result in the recording of goodwill and other intangible assets, which are subject to potential impairments in the future and that could harm our financial results. In addition, if we finance acquisitions by issuing convertible debt or equity securities, our existing shareholders may be diluted, which could affect the market price of the Series B preferred stock. As a result, if we fail to properly evaluate mergers, acquisitions or investments, we may not achieve the anticipated benefits of any such merger or acquisition, and we may incur costs in excess of what we anticipate. The failure to successfully evaluate and execute mergers, acquisitions or investments or otherwise adequately address these risks could materially harm our business, financial condition and results of operations.

***Growth of our business could result in increased costs.***

Our overall profitability would be negatively affected if investments and expenses associated with the growth of our business are not matched or exceeded by the revenue that is derived from such growth. Further, expanding existing and/or new business lines may involve recruiting and hiring new personnel. Hiring new personnel, especially professionals, is an inherently risky endeavor. The person needs to be a good fit within the organization, the person needs to be able to execute within the Company's existing corporate structure (which may differ from his/her previous place of employment) and the person may need to attract his or her clients (and prospective clients) to the Company. If any of these (or other) factors do not occur, the Company may have to terminate such person's employment and/or such person may leave the Company, which means that the cost of hiring, compensation paid and/or termination costs (including potential litigation) may impact the Company's results of operations in a negative and adverse manner. In addition, such personnel may be employed by competitors, and the retention of such individuals may require us to enter into guaranteed compensation contracts for a period following commencement of employment. The compensation terms provided for in such contracts may be fixed in whole or in part. Any guaranteed compensation expenses that cannot be adjusted based on the success or profitability of the offices could reduce our operating margins. Expansion also creates a need for additional compliance, documentation, risk management and internal control procedures, and often involves the hiring of additional personnel to monitor such procedures. To the extent such procedures are not adequate to appropriately monitor any new or expanded business, we could be exposed to a material loss or regulatory sanction.

***The soundness of other financial institutions could adversely affect us.***

Our ability to engage in routine funding transactions could be adversely affected by the actions and commercial soundness of other financial institutions. Financial services institutions are interrelated as a result of trading, clearing, counterparty, or other relationships, or the public's perception of the soundness of the nation's financial system. We have exposure to many different counterparties and we routinely execute transactions with counterparties in the financial services industry, including brokers and dealers, commercial banks, investment banks, mutual and hedge funds, and other institutional clients. As a result, defaults by, or even rumors or questions about, one or more financial services institutions, or the financial services industry generally, could lead to market-wide liquidity problems and could lead to losses or defaults by us or by other institutions. Many of these transactions expose us to credit risk in the event of default of our counterparty or client. In addition, our credit risk may be exacerbated when the collateral held by us cannot be realized upon or is liquidated at prices not sufficient to recover the full amount of the receivable due us. Finally, if the public views the nation's financial system (specifically, small banks and/or investment companies) as unstable, customers might withdraw their funds, resulting in losses. Any such forgoing losses could be material and could materially and adversely affect our business, financial condition, and results of operations.

In addition, we do not provide custodial services for our clients. Instead, client investment accounts are maintained under custodial arrangements with large, well established securities brokerage firms or bank institutions that provide custodial services, or, collectively, custodial firms, either directly or through arrangements made by us with those firms. As a result, the performance of, or even rumors or questions about the integrity or performance of, any of those custodial firms could adversely affect the confidence of our clients in the services provided by those firms or otherwise adversely impact their custodial holdings. Such an occurrence could negatively impact our ability to retain existing or attract new clients and, as a result, could have a material adverse effect on our business, financial condition, results of operations and prospects.

***Negative public opinion regarding us or failure to maintain our reputation in the communities we serve could adversely affect our business and prevent us from growing our business.***

Reputation risk, or the risk to our business, earnings and capital from negative public opinion is inherent in our business. Negative public opinion can result from our actual or alleged conduct in any number of activities, including lending practices, corporate governance and acquisitions, and from actions taken by government regulators and community organizations in response to those activities. Negative public opinion can adversely affect our ability to keep and attract customers and employees and can expose us to litigation and regulatory action and adversely affect our results of operations. Furthermore, to the extent that depositors - particularly uninsured depositors - become concerned about the Bank's financial condition or solvency, such depositors could withdraw their funds and create a "run on the bank". Although we take steps to minimize reputational risk in dealing with our customers and communities, this risk will always be present given the nature of our business. In addition, companies are facing increased scrutiny from customers, regulators, investors, and other stakeholders related to their environmental, social and governance ("ESG") practices and disclosure. Investor advocacy groups, investment funds and influential investors are also increasingly focused on these practices, especially as they relate to the environment, health and safety, diversity, labor conditions and human rights. For example, certain investors are beginning to incorporate the business risks of climate change and the adequacy of companies' responses to climate change and other ESG matters as part of their investment theses. These shifts in investing priorities may result in adverse effects on the trading price of the Company's preferred stock if investors determine that the Company has not made sufficient progress on ESG matters. In addition, new government regulations could also result in new or more stringent forms of ESG oversight and expanding mandatory and voluntary reporting, diligence, and disclosure. Increased ESG-related compliance costs could result in increases to our overall operational costs.

***Significant revenues and profits are generated as a result of our relationship with Cain Watters, and a change in the relationship or decline in Cain Watters' business could adversely affect us.***

Cain Watters provides advisory services to approximately 2,900 dental professionals across the United States and plays a meaningful role in referring trust, TPA, participant directed 401k plans and lending business to the Bank. In addition, Tectonic Advisors generates a substantial portion of its revenues and profits under a long-term contract to provide advisory and due diligence services to assist in the management of assets of clients of Cain Watters. In the event that the Cain Watters' relationship does not continue (for whatever reason), such a change could have a material adverse effect on the profits and operations of the Company.

Historically, the partners of Cain Watters had most of the client relationships. Thus, most of the referrals to the Bank and Tectonic Advisors have historically been through the partners of Cain Watters, each of whom has a relatively long relationship with the Bank and Tectonic Advisors and also is a shareholder of the Company. However, Cain Watters has experienced significant growth over the past few years and has expanded its client service and planning teams to accommodate this growth. The leaders of these teams, called planners, are younger, have significant influence over clients' decisions regarding service providers and are more technologically focused and, given this, may refer their clients to other providers at rates greater than historical averages, which would have (over time) a material adverse effect on the Bank and the Company.

In addition, Cain Watters is subject to, and has periodically faced, business challenges associated with litigation over private placements conducted by affiliates between 2006-2009, which were negatively impacted by the financial crisis and subsequent collapse in the energy markets, and lower assets under management resulting from the market correction. Further, to the extent that clients suffer losses or poor performance on these or other investments, they may move their money from Cain Watters to another advisor, which could have a material adverse impact on Cain Watters and also the Company.

We believe that any material adverse effect on the business of Cain Watters could have a material adverse effect on the Company. Cain Watters' business is primarily focused on dental practices. To the extent that the dental industry is disrupted or dental practices are adversely impacted for whatever reason, the Company's business may be adversely impacted as well.

***We depend on key personnel, and may have difficulty identifying, attracting and retaining necessary personnel, to execute our business strategy and successfully expand our operations. This risk includes the risk of retirement of key professionals in leadership roles, including loan officers, members of our SBA team, and financial advisors and brokers.***

We are reliant on key members of our senior management team, business development officers within the Bank (who are critical to generating loan growth) and financial advisors and brokers (who are critical to driving asset growth at Tectonic Advisors and Sanders Morris). Personnel changes will occur from time to time, and we cannot predict whether significant resignations and retirements will occur or whether we will be able to recruit additional qualified personnel. With the exception of certain members of senior management, none of our professionals are subject to employment agreements and are free to leave at any time. Further, certain of our executive officers, financial advisors and brokers and SBA loan production officers are either financially secure or, in some cases, beyond retirement age for many Americans, and do not have to work. Thus, these individuals are more susceptible to retirement. Departures, particularly of key employees in leadership or client development roles, may cause client defections due to close relationships between clients and such professionals. While we have succession plans in place, the loss of any key employee may have a material adverse effect on our business and prospects. If we are unable to retain our key employees or attract, recruit, integrate, or retain other skilled professionals in the future, our business could suffer materially in the future.

***The employment market has become increasingly competitive; We may have difficulty attracting and retaining skilled personnel.***

The employment market has become increasingly competitive over the past two years. We derive a substantial portion of our revenue from the efforts of our professional team, including loan officers, members of our SBA team, and financial advisors and brokers. Therefore, our future success depends, in large part, on our ability to attract, recruit, and retain qualified financial services professionals. Competition for the best people in many activities engaged in by us is intense including with respect to compensation and emerging workplace practices, accommodations, and remote work options, and we may not be able to replace personnel promptly at acceptable compensation levels or at all, and may have difficulty retaining them. These circumstances have led to escalating compensation packages in the industry. Up-front payments, increased payouts, and guaranteed contracts have made recruiting and retaining these professionals more expensive and more difficult and can lead to departures by current professionals. The unexpected loss of personnel could impact our ability to serve our clients timely, and could also negatively impact our internal operations, including regulatory compliance. A lack of skilled, seasoned personnel with knowledge of our business and our market could reduce the performance of certain areas of our business, increase our error rate in key areas, affect our ability to grow our business, and lead to a lack of talented professionals ready to advance into leadership roles in the longer term. Due to these potential effects, the tightening employment market could have a material adverse impact on our business, financial condition and results of operations.

***A decline in general business and economic conditions and any regulatory responses to such conditions could have a material adverse effect on our business, financial position, results of operations and growth prospects.***

As a business operating in the bank and non-bank financial services industries, our business and operations are sensitive to general business and economic conditions in the United States, generally, and particularly the State of Texas. If the U.S. or Texas economies weaken, our growth and profitability from our lending, deposit and investment operations could be constrained. Unfavorable or uncertain economic and market conditions could lead to credit quality concerns related to borrower repayment ability and collateral protection as well as reduced demand for the products and services we offer. In addition, economic conditions in foreign countries, including global political hostilities, U.S. and foreign tariff policies and uncertainty over the stability of the euro currency, could affect the stability of global financial markets, which could hinder domestic economic growth. Concerns about the performance of international economies can impact the economy and financial markets here in the United States. If the national, regional and local economies experience worsening economic conditions, including high levels of unemployment, our growth and profitability could be constrained. Weak economic conditions are characterized by, among other indicators, deflation, elevated levels of unemployment, fluctuations in debt and equity capital markets, increased delinquencies on commercial, mortgage and consumer loans, residential and commercial real estate, price declines and lower home sales and commercial activity. A significant outbreak of disease pandemics or other adverse public health developments in the population could result in a widespread health crisis that could adversely affect the economies and financial markets of many countries, resulting in an economic downturn that could adversely affect our customers' businesses and results of operations. Our business is also significantly affected by monetary and related policies of the U.S. government and its agencies.



In addition, declines in the U.S. stock markets directly impact our Investment Services segment and also our trust assets. With any such declines, our assets under management and advisement and trust assets decline in value and clients are less apt to invest. Since our investment advisory revenues are based on assets, this leads to a decline in our Investment Services and trust revenues. In addition, even though our brokerage revenues are not based on assets, brokerage revenues may also be impacted by declines in the stock market because investors may be less inclined to trade stocks and/or bonds. Since our brokerage revenues are based on activity, we would likely see a decline in brokerage revenues as a result of stock market declines.

In recent years, economic growth has been uneven, and opinions vary on the strength and direction of the economy. Uncertainties continue regarding the potential for a renegotiation of international trade agreements and the effect of the legislation enacted by the recent presidential administration, and the impact such actions and the policies of the administration of President Joseph Biden may have on economic and market conditions. A trade war or other governmental action related to tariffs or international trade agreements or policies, as well as the current conflict in Ukraine and the Middle East or other potential epidemics or pandemics, have the potential to negatively impact our and/or our customers' costs, demand for our customers' products, and/or the U.S. economy or certain sectors thereof and, thus, adversely affect our business, financial condition, and results of operations.

The Federal Reserve's recent unprecedented rate hikes in response to the inflationary environment may further impact our ability to attract deposits, and could have an adverse effect on our business, financial condition and results of operations as increased interest rates could reduce the demand for loans and affect the ability of our borrowers to repay their indebtedness subjecting us to potential credit losses. Changes in any of these policies are influenced by macroeconomic conditions and other factors that are beyond our control. Adverse economic conditions and government policy responses to such conditions could have a material adverse effect on our business, financial condition, results of operations and growth prospects. All of these factors are detrimental to our business, and the interplay between these factors can be complex and unpredictable.

In addition, the inflationary outlook in the United States remains uncertain. Inflation has been reported at high levels, and could result in higher interest rates for a prolonged period of time, which may expose the Company to interest rate risk. In addition, higher interest rates could slow economic growth and lead to a recessionary environment, which could negatively impact the Company's growth, credit quality, net interest margin and its financial results. The risks to our business from inflation depends on the durability of the current inflationary pressures in our markets. Transitory increases in inflation are unlikely to have a material impact on our business or earnings. However, more persistent inflation could lead to tighter-than-expected monetary policy which could, in turn, increase the borrowings costs of our customers, making it more difficult for them to repay their loans or other obligations. High interest rates may be needed to tame persistent inflationary price pressures, which could also push down asset prices and weaken economic activity. A deterioration in economic conditions in the United States and our markets could result in an increase in loan delinquencies and non-performing assets, decreases in loan collateral values and a decrease in demand for our products and services, all of which, in turn, would adversely affect our business, financial condition and results of operations.

#### ***Lower Trucking Margins and Revenues Negatively Impact Trucking Industry and Factoring***

The trucking industry, particularly over-the-road trucking, is a volatile industry and sees the freight rates increase or decline based on the state of the economy, customer demand and/or supply and demand considerations in the trucking industry. During 2023, freight rates – which are the rates that trucking companies charge customers for transportation services – declined by as much as 30% or more (generally) across the industry from their peak in 2021, for over-the-road trucking. Thus, revenues have declined, on a per truck basis, for most trucking companies by 30% or more from their peak in 2021, causing a significant decline in the amount of factored receivables. Further, diesel prices – a key cost of trucking companies – have continued to stay at elevated levels. The industry did see some relief as the price of diesel fell in 2023, but prices remain elevated as compared to prices in 2021.

***Our business is concentrated in, and dependent upon, the continued growth and welfare of our primary market, and adverse economic conditions in such market could negatively impact our operations and clients.***

Although we provide services nationwide, our business is concentrated primarily in the State of Texas. Our success depends to a certain extent upon the business activity, population, income levels, employment trends, deposits and real estate activity in this primary market. Although our clients' business and financial interests may extend beyond our primary market, adverse conditions that affect our primary market could reduce our growth rate, affect the ability of our clients to repay their loans, affect the value of collateral underlying our loans, affect our ability to attract deposits, affect the ability of our clients to make additional investments or cause such clients to withdraw their investments, affect the value of our assets under management and generally affect our business, financial condition, results of operations and future prospects.



***We have a loan concentration related to the acquisition and financing of dental practices.***

Loan concentrations are considered to exist when there are amounts loaned to a multiple number of borrowers engaged in similar activities that would cause them to be similarly impacted by economic or other conditions. As of December 31, 2023, our loan portfolio included \$78.2 million of loans to the dental industry, representing approximately 15.6% of our total funded loans. These loans include practice acquisition loans, dental equipment loans, and dental facility loans. We had no charge-offs during 2023 and 2022 in our dental portfolio assets. We believe that these loans are conservatively underwritten to credit worthy borrowers and are diversified geographically. However, to the extent that there is a decline in the dental industry in general, we may incur significant losses in our loan portfolio as a result of this concentration.

***A governmental shutdown or curtailment of government guaranteed loan programs could affect a segment of our business.***

A major segment of our business consists of originating and periodically selling government guaranteed loans, in particular those guaranteed by the USDA and SBA. From time to time, the government agencies that guarantee these loans reach their internal limits and cease to guarantee loans. In addition, these agencies may change their rules for loans or Congress may adopt legislation that would have the effect of discontinuing or changing the loan programs. Non-governmental programs could replace government programs for some borrowers, but the terms might not be equally acceptable. Therefore, if these changes occur, the volume of loans to small businesses and industrial borrowers of the types that now qualify for government guaranteed loans could decline. Also, the profitability of these loans could decline. As the funding of the guaranteed portion of 7(a) loans has historically been a major portion of our business, a long-term decrease or discontinuation in the funding for the 7(a) loan program may have an unfavorable impact on our future performance and results of operations. In addition, any default by the U.S. government on its obligations or any prolonged government shutdown could, among other things, impede our ability to originate SBA or USDA loans or sell such loans in the secondary market, which could materially and adversely affect our business, financial condition and results of operations.

***We face specific risks associated with retention of unguaranteed portions of SBA loans.***

The Bank has historically sold a considerable portion of the guaranteed portion of its SBA loans within a short period of time of originating such loans. Upon sale, the Bank retains the unguaranteed portion of such loans. As of December 31, 2023, the unguaranteed portion of our SBA loans totaled \$64.9 million, representing 13.0% of our total loan portfolio. Given that the SBA requires that the Bank only make loans to borrowers that do not have access to conventional bank financing, the unguaranteed portion of these loans carry greater risk than traditional loans. As the Bank's loan portfolio of the unguaranteed portion of SBA loans grows, its risk of loss due to defaults also grows. The Bank has a reserve for such unguaranteed portion of SBA loans. To the extent that this reserve is not adequate to cover losses, the Bank will suffer losses to its capital base and such losses could be material.

***Commercial lending generally involves a higher degree of risk than retail residential mortgage lending.***

Commercial real estate loans are generally viewed as having more risk of default than owner-occupied residential real estate loans and typically have larger balances. The underlying commercial real estate values, lower demand for office and retail space, increase costs to complete construction projects. Customer cash flows can be more easily influenced by adverse conditions in the related industries, the real estate market or in the economy.

Commercial real estate values may be elevated and the outlook for commercial real estate remains dependent on the broader economic environment and, specifically, how major subsectors respond to higher interest rate environment and prices for commodities, goods and services. Credit performance across the industry over the medium- and long-term is susceptible to economic and market forces. Some degree of general instability in the broad commercial real estate market may occur in the coming quarters as loans are refinanced at higher interest rates and in markets with higher vacancy rates under current economic conditions. Instability and uncertainty in the commercial real estate markets could have a material adverse effect on our financial condition and results of operations.

***The level of our commercial real estate loan portfolio may subject us to heightened regulatory scrutiny.***

The banking regulators have promulgated joint guidance on sound risk management practices for financial institutions with concentrations in commercial real estate lending. Under the guidance, a financial institution that is actively involved in commercial real estate lending should perform a risk assessment to identify potential concentrations in commercial real estate lending. A financial institution may have such a concentration if, among other factors: (i) total outstanding loans for construction, land development, and other land represent 100% or more of total risk-based capital (“CRE 1 Concentration”); or (ii) total outstanding loans for construction, land development and other land and loans secured by multifamily and non-owner occupied non-farm, non-residential properties (excluding loans secured by owner-occupied properties) represent 300% or more of total risk-based capital (“CRE 2 Concentration”), and the institution’s commercial real estate loan portfolio has increased by 50% or more during the prior 36-month period. In such an instance, management should employ heightened risk management practices, including board and management oversight and strategic planning, development of underwriting standards, risk assessment and monitoring through market analysis and stress testing. As of December 31, 2023, our CRE 1 Concentration level was 84.33% and our CRE 2 Concentration level was 112.7%. We may, at some point, be considered to have a concentration in the future, or our risk management practices may be found to be deficient, which could result in increased reserves and capital costs as well as potential regulatory enforcement action.

***Our factoring services through the Bank’s Integra factoring division are concentrated in the transportation industry and economic conditions or other factors negatively impacting the transportation industry could adversely affect our factoring business; factoring invoice levels are at historical highs.***

Factoring for small-sized trucking businesses constituted the vast majority of our total factoring portfolio as of December 31, 2023, calculated based on the gross receivables from the purchase of invoices from such trucking businesses compared to our total gross receivables in the purchase of factored receivables as of such date. The Company began providing factoring services for the energy industry and the staffing industry during 2023, and as of December 31, 2023, these services constitute approximately 10% of the Company’s total factoring portfolio. Given the concentration of our factoring business in the transportation industry, economic conditions or other factors that negatively impact the transportation industry could impact our factoring revenues, as the revenues we earn from purchasing transportation invoices are directly correlated with the amount of transportation activity generated by our factoring clients (i.e., the volume of transportation invoices they are able to generate by providing their services). Reductions in economic activity will typically cause a decrease in the volume of goods in commerce available to be transported by our factoring clients. Increased costs associated with operating a trucking business, such as may be caused by increases in the prices of oil and diesel fuel, may cause a diminished demand for trucking services as our clients pass those costs along to their customers. Conversely, decreases in the price of diesel fuel may cause the size of our factoring portfolio to decrease, as the price of diesel fuel typically directly correlates with the size of the invoices we purchase from our factoring clients. Additionally, the factoring industry may not continue its historical growth and we may face increased competition. Our failure to compete effectively in our market could restrain our growth or cause us to lose market share. Any of such events could impact the returns we realize on our factoring activity or result in a decrease in the overall amount of our factoring activity and could have an adverse effect on our business, financial condition and results of operations.

***The success of our trust services is dependent upon market fluctuations and a non-diversified source for its growth.***

We offer traditional fiduciary services such as serving as executor, trustee, agent, administrator or custodian for individuals, nonprofit organizations, employee benefit plans and organizations. As of December 31, 2023, the Bank had approximately \$1.9 billion in trust assets. The level of assets under management is significantly impacted by the market value of the assets. To date, virtually all of the growth in our assets under management relates to one registered investment advisor, Cain Watters, who has advised its clients of the existence of our trust services. We have not compensated the registered investment advisor in any way for making its clients aware of our trust services and cannot assure you that the investment advisor will continue to notify its clients of our trust services or that those clients will open trust accounts at the Bank. Related to this, the Bank and Cain Watters are parties to an agreement which includes a provision obligating each party to preserve the other’s business relationship with their mutual clients. However, in the event that the Cain Watters’ relationship does not continue (for whatever reason) to refer client to the Bank’s trust department, such a change could have a material adverse effect on the future growth and, thus, profits and operations of the Company. In addition, we are subject to regulatory supervision with respect to these trust services that may restrain our growth and profitability.

***We are subject to possible claims and litigation pertaining to fiduciary responsibility.***

Clients could make claims and take legal action pertaining to our performance of our fiduciary responsibilities. Whether client claims and legal action related to our performance of our fiduciary responsibilities are founded or unfounded, if such claims and legal actions are not resolved in a manner favorable to us, they may result in significant financial liability and/or adversely affect our market perception of our products and services as well as impact client demand for those products and services. Although we have not experienced any material claims or litigation pertaining to fiduciary responsibility, the occurrence of any financial liability or reputational damage could have a material adverse effect on our business, which, in turn, could have a material adverse effect on our financial condition and results of operations.

***We could suffer material credit losses.***

There are risks inherent in making any loan, including risks inherent in dealing with individual borrowers, risks of non-payment, risks resulting from uncertainties as to the future value of collateral and risks resulting from changes in economic and industry conditions and increases in inflation and interest rates. Changes in the economy can cause the assumptions that we made at origination to change and can cause borrowers to be unable to make payments on their loans, and significant changes in collateral values can cause us to be unable to collect the full value of loans we make. Increases in interest rates and inflation increase costs and decrease profits, reducing the ability of a borrower to make payments on its loan. There is no assurance that our credit risk monitoring and loan approval procedures are or will be adequate or will reduce the inherent risks associated with lending. Our credit administration personnel and our policies and procedures may not adequately adapt to changes in economic or any other conditions affecting clients and the quality of our loan portfolio. Any failure to manage such credit risks may materially adversely affect our business, financial condition and results of operations.

***Our levels of nonperforming assets could increase, which could adversely affect our results of operations and financial condition, and could result in losses in the future.***

As of December 31, 2023, our nonperforming loans (which consist of non-accrual loans, loans past due 90 days or more and still accruing interest and loan modifications to borrowers experiencing financial difficulty that are not performing in accordance with their modified terms) totaled \$2.6 million. We had no other real estate owned at December 31, 2023. However, our nonperforming assets may continue to remain at low levels or we may experience increases in nonperforming assets in the future. Our nonperforming assets adversely affect our net income in various ways. We do not record interest income on non-accrual loans or other real estate owned, thereby adversely affecting our net interest income, net income and returns on assets and equity, and our loan administration costs increase, which together with reduced interest income adversely affects our efficiency ratio. When we take collateral in foreclosure and similar proceedings, we are required to mark the collateral to its then-fair market value and estimate disposition costs, which may result in a loss. These nonperforming loans and other real estate owned also increase our risk profile and the level of capital our regulators believe is appropriate for us to maintain in light of such risks. The resolution of nonperforming assets requires significant time commitments from management and can be detrimental to the performance of their other responsibilities. Further, since many of our loans are located outside of our primary market area, collecting delinquent loans would be more difficult for our staff relative to our competitors. If we experience increases in nonperforming loans and nonperforming assets, our net interest income may be negatively impacted and our loan administration costs could increase, each of which could have an adverse effect on our net income and related ratios, such as returns on assets and equity.

***Our allowance for credit losses may not be sufficient to absorb actual losses.***

Experience in the banking industry indicates that a portion of our loans in all categories of our lending business will become delinquent, and some may only be partially repaid or may never be repaid at all. Our methodology for establishing the adequacy of the allowance for credit losses depends on subjective application of risk grades as indicators of borrowers' ability to repay. Deterioration in general economic conditions and unforeseen risks affecting clients may have an adverse effect on borrowers' capacity to repay timely their obligations before risk grades could reflect those changing conditions. In times of improving credit quality, with growth in our loan portfolio, the allowance for credit losses may decrease as a percent of total loans. Changes in economic and market conditions may increase the risk that the allowance would become inadequate if borrowers experience economic and other conditions adverse to their businesses. Maintaining the adequacy of our allowance for credit losses may require that we make significant and unanticipated increases in our provisions for credit losses, which could materially affect our results of operations and capital adequacy. Recognizing that many of our loans individually represent a significant percentage of our total allowance for credit losses, adverse collection experience in a relatively small number of loans could require an increase in our allowance.

Federal regulators, as an integral part of their respective supervisory functions, periodically review our allowance for credit losses. The regulatory agencies may require us to change classifications or grades on loans, increase the allowance for credit losses with large provisions for credit losses and recognize further loan charge-offs based upon their judgments, which may be different from ours. Any increase in the allowance for credit losses required by these regulatory agencies could have a negative effect on our results of operations and financial condition.

***Our legal lending limits may impair our ability to attract borrowers and ability to compete with larger financial institutions.***

Our per client lending limit at December 31, 2023, was approximately \$13.9 million. Accordingly, the size of loans which we can offer to potential clients is less than the size which many of our competitors with larger lending limits are able to offer. This limit has affected and will continue to affect our ability to seek relationships with larger businesses in our market area. We accommodate loans in excess of our lending limit through the sale of portions of such loans to other banks. However, we may not be successful in attracting or maintaining clients seeking larger loans or in selling portions of such larger loans on terms that are favorable to us.

***The small- to medium-sized businesses that we lend to may have fewer resources to weather adverse business conditions, which may impair their ability to repay a loan, and such impairment could adversely affect our results of operations and financial condition.***

Our business development and marketing strategies primarily serve the banking and financial services needs of small- to medium-sized businesses. These businesses generally have fewer financial resources in terms of capital or borrowing capacity than larger entities, frequently have smaller market shares than their competition, may be more vulnerable to economic downturns and/or increases in interest rates and inflationary pressure, often need substantial additional capital to expand or compete and may experience substantial volatility in operating results, any of which may impair a borrower's ability to repay a loan. In addition, the success of a small- to medium-sized business often depends on the management skills, talents and efforts of one or two people or a small group of people, and the death, disability or resignation of one or more of these people could have a material adverse impact on the business and its ability to repay its loans. If general economic conditions negatively impact Texas or the specific markets in which we operate and small- to medium-sized businesses are adversely affected or our borrowers are otherwise affected by adverse business conditions, our business, financial condition and results of operations could be adversely affected.

***Our commercial finance clients, particularly with respect to the Bank's Integra factoring division, may lack the operating history, cash flows or balance sheet necessary to support other financing options and may expose us to additional credit risk, especially if our additional controls for such products are ineffective in mitigating such additional risks.***

A significant portion of our loan portfolio consists of commercial finance products. Some of these commercial finance products, particularly asset-based loans and our factored receivables through the Bank's Integra division, arise out of relationships with clients who lack the operating history, cash flows or balance sheet necessary to qualify for other financing options. We attempt to control for the additional credit risk in these relationships through credit management processes employed in connection with these transactions. However, if such controls are ineffective in controlling this additional risk or if we fail to follow the procedures we have established for managing this additional risk, we could be exposed to additional losses with respect to such product lines that could have an adverse effect on our business, financial condition and results of operations.

***Certain of our loans are not secured by property but dependent on the earning capacity of the borrower.***

Certain of our loans are not collateralized or fully collateralized by tangible property, but are made on the basis of the cash flow (earnings) being generated by the borrower. These include, without limitation, certain loans to dentists to either buy out another dentist in a dental practice and/or to buy into a dental practice or to purchase or establish a dental practice. In this case, the borrower may be the dentist and/or the dental practice, neither of which may have sufficient tangible assets (cash, marketable securities, real estate or other tangible assets) to fully secure or even secure a portion of the loan being made. Rather, we look to the earning power and capacity of the dentist and/or dental practice as the primary source of repayment of the loan. In the event that the dentist or dental practice's earning power is insufficient to service or repay the loan, the additional collateral is usually insufficient to cover the outstanding loan balance, in which case we lose substantially all of the loan balance. In the event that these loans default at a high rate, we will likely recover very little from the underlying collateral, in which case the Bank could suffer significant losses and you could lose some or all of your investment in your Series B preferred stock.

***The Company's use of appraisals in deciding whether to make a loan on or secured by real property does not ensure the value of the real property collateral.***

In considering whether to make a loan secured by real property, we generally require an appraisal of the property. However, an appraisal is only an estimate of the value of the property at the time the appraisal is made, and an error in fact or judgment could adversely affect the reliability of an appraisal. In addition, events occurring after the initial appraisal may cause the value of the real estate to decrease. As a result of any of these factors, the value of collateral backing a loan may be less than supposed, and if a default occurs, we may not recover the outstanding balance of the loan.

***Fee revenue represents a significant portion of our consolidated revenue and is subject to decline, among other things, in the event of a reduction in, or changes to, the level or type of investment activity by our clients and market declines.***

A significant portion of our revenue is the result of fee-based services related to investment advisory, trust services, insurance and brokerage activities. This contrasts with many commercial banks that may rely more heavily on interest-based sources of revenue, such as loans. For the year ended December 31, 2023, consolidated non-interest income represented approximately 59.3% of our consolidated gross revenue (which is net interest income plus non-interest income). The level of these fees is influenced by several factors, including the mix and volume of our assets under custody and administration and our assets under management, market declines (which reduce asset values), the value and type of securities positions held (with respect to assets under custody) and the volume of portfolio transactions, and the types of products and services used by our clients.

In addition, our combined clients include private investors, defined benefit and contribution plans, institutional investors, such as mutual funds, collective investment funds, hedge funds and other investment pools, and investment managers. Economic, market or other factors that reduce the level or rates of savings in or with those institutions, either through reductions in financial asset valuations or through changes in investor preferences, could materially reduce our fee revenue or have a material adverse effect on our consolidated results of operations. These clients also, by their nature, are often able to exert pricing pressure, and this, combined with strong competitive forces in the markets for our services, has resulted in, and may continue to result in, significant pressure to reduce the fees we charge for our services in both our asset servicing and asset management business lines.

***The business operations of Sanders Morris may face limitations due to net capital requirements.***

As a registered broker-dealer, Sanders Morris is subject to the net capital rules administered by the SEC and FINRA. These rules, which specify minimum net capital requirements for registered broker-dealers and FINRA members, are designed to assure that broker-dealers maintain adequate net capital in relation to their liabilities and the size of their client's business. These requirements have the effect of requiring that a substantial portion of a broker-dealer's assets be kept in cash or highly liquid investments. Failure to maintain the required net capital may subject a firm to suspension or revocation of its registration by the SEC and suspension or expulsion by FINRA and other regulatory bodies. Compliance with these net capital rules could limit operations that require extensive capital, such as underwriting or trading activities.

These net capital rules could also restrict our ability to withdraw capital in situations where Sanders Morris has more than the minimum required capital. We may be limited in our ability to pay dividends, implement our strategies, pay interest or repay principal on our debt, and redeem or repurchase our outstanding preferred or common stock. In addition, a change in these net capital rules or new rules affecting the scope, coverage, calculation, or amount of the net capital requirements, or a significant operating loss or significant charge against net capital, could have similar effects.

***The wealth management, trust and brokerage business is highly competitive. If we are not able to compete successfully against current and future competitors, our business, financial condition, and results of operations will be adversely affected.***

The wealth management, trust and brokerage business is highly competitive, and we expect it to remain so. We compete directly with many other national and regional full service financial services firms, banks, insurance companies, asset management and advisory firms, and, to a lesser extent, with on-line and discount brokers. Further, many online brokers have gone to a "no commission" structure, putting additional pressure on our brokerage operations. We also compete for wealth management services with commercial banks, private trust companies, sponsors of mutual funds, financial planning firms, venture capital, private equity and hedge funds, and other wealth managers. Moreover, we compete with ETFs that generally track passive investing strategies and charge lower management fees than active strategies, which may affect both the profitability of asset managers, on whose success we in part depend, and the perceived value of our investment services regarding ETFs. A continued lessening of investor interest in actively managed equity funds could decrease demand for and/or pricing on our investment services.

We are a small firm. Many of our competitors have more personnel and financial resources than we do. Larger competitors are able to advertise their products and services on a national or regional basis and may have a greater number and variety of products and distribution outlets for their products, larger client bases, and greater name recognition. These larger and better capitalized competitors may be better able to respond to changes in the wealth management and institutional services industries, to finance acquisitions, to fund internal growth, and to compete for market share generally.

Increased competition may result in pricing pressures, reduced revenue and loss of market share. Further, as a strategic response to changes in the competitive environment, we may from time to time make certain pricing, service, or marketing decisions or acquisitions that also could materially and adversely affect our business and results of operations. In addition, new technologies and the expansion of existing technologies may increase competitive pressures on us. The growth of online wealth management tools that provide automated, algorithm-based portfolio management advice, sometimes called robo-advice, may further accelerate the adoption of passively managed portfolios and reduce demand for and/or pricing on our investment services. Consequently, we may not be able to compete successfully against current and future competitors. If we are unable to compete effectively, our business, financial condition, and results of operations will be adversely affected.

***Underperformance or declines in our investments, in either relative or absolute terms, may reduce the profitability of our wealth management and advisory business.***

Investment performance is one of the most important factors in retaining existing clients and competing for new wealth management business. Underperformance or market declines in our investments could reduce our revenue and impair our growth in a number of ways:

- existing clients may withdraw funds from our wealth management business in favor of better performing products;
- asset-based advisory fees could decline as a result of a decrease in the value of assets under management;
- our ability to attract funds from existing and new clients might diminish;
- firms with which we have business relationships may terminate their relationships with us; and
- our wealth managers and investment advisors may depart, whether to join a competitor or otherwise.

Even when market conditions are generally favorable, our investment performance may be adversely affected by the investment style of our asset managers and the particular investments that they make. To the extent our investment style, security selection or investment results underperform other investment styles, selections or results, in either relative or absolute terms, the revenue and profitability of our wealth management business will likely be reduced and our ability to retain and attract new clients and funds will likely be impaired.

***Standard investment management contracts we have with our clients are terminable without cause and on relatively short notice by our clients, which makes us vulnerable to short-term declines in the performance of the securities under our management.***

Like most investment advisory and wealth management businesses, the investment advisory contracts we have with our clients are typically terminable by the client without cause upon less than 30 days' notice. As a result, even short-term declines in the performance of the securities we manage, which can result from factors outside our control, such as adverse changes in market or economic condition or the poor performance of some of the investments we have recommended to our clients, could lead some of our clients to move assets under our management to other asset classes such as broad index funds or treasury securities, or to investment advisors which have investment product offerings or investment strategies different than ours. Therefore, our operating results are heavily dependent on the financial performance of our investment portfolios and the investment strategies we employ in our investment advisory businesses and even short-term declines in the performance of the investment portfolios we manage for our clients, whatever the cause, could result in a decline in assets under management and a corresponding decline in investment management fees, which would adversely affect our results of operations.

***We continue to experience pricing pressures in areas of our business which may impair our future revenue and profitability.***

We continue to experience pricing pressures on investment advisory fees, as well as trading margins and commissions in fixed income and equity trading. In the fixed income market, regulatory requirements have resulted in greater price transparency, leading to price competition and decreased trading margins. In the equity market, we experience pricing pressure from institutional clients to reduce commissions, partially due to the industry trend toward unbundling fees related to research and execution and the trend towards “no commission” trading. Our trading margins have been further compressed by the use of electronic and direct market access trading, which has created additional competitive pressure. In addition, we face pricing pressures in our advisory business, which has seen new entrants compete for clients on the basis of price. We believe that price competition and pricing pressures in these and other areas will continue as investors continue to reduce the amounts they are willing to pay, including by reducing the number of advisory and brokerage firms they use, and some of our competitors seek to obtain market share by reducing advisory fees, commissions or margins.

***We face strong competition from other insurance agencies, which may adversely affect our operations and financial condition.***

The insurance industry 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, including 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. Our insurance business competes with many other insurers, including large national companies that have greater financial, marketing and management resources than HWG. Many of these competitors also have better ratings and market recognition than our insurance business.

In addition, a number of new, proposed or potential industry developments also could increase competition in HWG’s industry. These developments include changes in practices and other effects caused by the Internet (including direct marketing campaigns by HWG’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 our insurance business from expanding its book of business.

Our 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 our insurance business. New competition could reduce the demand for HWG’s insurance products, which could have a material adverse effect on our financial condition and results of operations.

***A failure to appropriately identify and address potential conflicts of interest could adversely affect our businesses.***

Due to the scope of our businesses and our client base, we regularly address potential conflicts of interest, including situations where our services to a particular client or our own investments or other interests conflict, or are perceived to conflict, with the interests of another client, as well as situations where one or more of our businesses have access to material non-public information that may not be shared with other businesses within the firm and situations where we may be a creditor of an entity with which we also have an advisory or other relationship. In addition, our status as a bank holding company subjects us to heightened regulation and increased regulatory scrutiny by the Federal Reserve with respect to transactions between our entities that are or could be viewed as affiliates of ours and, under the Volcker Rule, transactions between our subsidiaries (including Sanders Morris and Tectonic Advisors) and certain covered funds.

***We may incur significant losses due to ineffective risk management processes and strategies.***

We seek to monitor and control our risk exposures through a risk and control framework encompassing a variety of separate but complementary financial, credit, operational and compliance systems, and internal control and management review processes. However, those systems and review processes and the judgments that accompany their application may not be effective and, as a result, we may not anticipate every economic and financial outcome in all market environments or the specifics and timing of such outcomes, particularly in the event of the kinds of dislocations in market conditions experienced in recent years, which highlight the limitations inherent in using historical data to manage risk. If those systems and review processes prove to be ineffective in identifying and managing risks, we could be subjected to increased regulatory scrutiny and regulatory restrictions could be imposed on our business, including on our potential future business lines, as a result of which our business and operating results could be adversely affected.



***If we fail to maintain effective internal control over financial reporting, we may not be able to report our financial results accurately and timely, in which case our business may be harmed, investors may lose confidence in the accuracy and completeness of our financial reports, we could be subject to regulatory penalties and the price of the Series B preferred stock may decline.***

Our management is responsible for establishing and maintaining adequate internal control over financial reporting and for evaluating and reporting on that system of internal control. Our internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP. As a public company, we are required to comply with the Sarbanes-Oxley Act of 2002 (the “Sarbanes-Oxley Act”), and other rules that govern public companies, including making annual assessments of the effectiveness of our internal control over financial reporting. In addition, when we cease to be an emerging growth company, our independent registered public accounting firm may be required to report on the effectiveness of our internal control over financial reporting. We will continue to periodically test and update, as necessary, our internal control systems, including our financial reporting controls. Our actions, however, may not be sufficient to result in an effective internal control environment. In particular, we may not be able to maintain effective internal control over segment reporting.

Our management may conclude that our internal control over financial reporting is not effective due to our failure to cure any identified material weakness, significant deficiency or otherwise. Moreover, even if our management concludes that its internal control over financial reporting is effective, our independent registered public accounting firm may conclude that our internal control over financial reporting is not effective. In addition, during the course of the evaluation, documentation and testing of our internal control over financial reporting, we may identify deficiencies that we may not be able to remediate in time to meet the deadline imposed by FDICIA. Any such deficiencies may also subject us to adverse regulatory consequences. If we fail to achieve and maintain the adequacy of our internal control over financial reporting, as these standards are modified, supplemented or amended from time to time, we may be unable to report our financial information on a timely basis, we may not be able to conclude on an ongoing basis that we have effective internal control over financial reporting in accordance with the Sarbanes-Oxley Act or the FDICIA, and we may suffer adverse regulatory consequences or violations of listing standards.

Any future failure to maintain effective internal control over financial reporting could impair the reliability of our financial statements which in turn could harm our business, impair investor confidence in the accuracy and completeness of our financial reports and our access to the capital markets, cause the price of the Series B preferred stock to decline and subject us to regulatory penalties and litigation.

***We are required to make significant estimates and assumptions in the preparation of our financial statements and our estimates and assumptions may not be accurate.***

The preparation of our consolidated financial statements in conformity with GAAP requires our management to make significant estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of income and expense during the reporting periods. The processes the Company uses to estimate its probable credit losses and to measure the fair value of financial instruments, as well as the processes used to estimate the effects of changing interest rates and other market measures on the company’s financial condition and results of operations, depends upon the use of analytical and forecasting models. These models reflect assumptions that may not be accurate, particularly in times of market stress or other unforeseen circumstances. Even if these assumptions are adequate, the models may prove to be inadequate or inaccurate because of other flaws in their design or their implementation. If the models the Company uses for interest rate risk and asset-liability management are inadequate, the Company may incur increased or unexpected losses upon changes in market interest rates or other market measures. If the models the Company uses for determining its probable credit losses are inadequate, the allowance for credit losses may not be sufficient to support future charge-offs. If the models the Company uses to measure the fair value of financial instruments are inadequate, the fair value of such financial instruments may fluctuate unexpectedly or may not accurately reflect what the Company could realize upon sale or settlement of such financial instruments. Any such failure in the Company’s analytical or forecasting models could have a material adverse effect on the Company’s business, financial condition and results of operations.

***We may be required to recognize a significant charge to earnings if our goodwill or other intangible assets become impaired.***

Goodwill and purchased intangible assets with indefinite lives are not amortized, but are reviewed for impairment annually and more frequently when events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. We assess the recoverability of the unamortized balance of our finite-lived intangible assets when indicators of potential impairment are present. Factors that may indicate that the carrying value of our goodwill or other intangible assets may not be recoverable include a decline in our stock price and market capitalization and slower growth rates in our industry. We will continue to evaluate the carrying value of our goodwill and other intangible assets. The recognition of a significant charge to earnings in our consolidated financial statements resulting from any impairment of our goodwill or other intangible assets could materially adversely impact our business, financial condition and results of operations.

***We may elect or be compelled to seek additional capital, but that capital may not be available, or it may be dilutive.***

Our ability to raise capital in the future, if needed, will depend on conditions in the capital markets, which are outside our control, and on our financial performance. Accordingly, we cannot be assured of our ability to raise capital when needed, on favorable terms or at all. If we cannot raise additional capital when needed, we will be subject to increased regulatory supervision and the imposition of restrictions on our growth and business. These outcomes could negatively impact our ability to operate or further expand our operations through acquisitions and may result in increases in operating expenses and reductions in revenues that could have a material adverse effect on our financial condition and results of operations. In addition, in order to raise additional capital, we may need to issue shares of our preferred or common stock that would reduce our shareholders' percentage ownership interest to the extent they do not participate in future offerings. Also, if we are unable to raise additional capital, we may be required to take alternative actions which may include the sale of income-producing assets to meet our capital requirements, which could have an adverse impact on our results of operations and ability to generate income.

***We face intense competition from larger banks, financial institutions and financial technology (FinTech) companies that could hurt our business.***

We conduct our business operations in markets where the banking business is highly competitive and is dominated by large multi-state and in-state banks with operations and offices covering wide geographic areas. We also compete with other financial service businesses, including investment advisory and wealth management firms, mutual fund companies, financial technology companies, and securities brokerage and investment banking firms that offer competitive banking and financial products and services as well as products and services that we do not offer. Larger banks and many of those other financial service organizations have greater financial, technology and marketing resources than we do that enable them to conduct extensive advertising campaigns, promote ease of use through technology and/or shift resources to regions or activities of greater potential profitability. They also have substantially more capital and higher lending limits than we do, which enable them to attract larger clients and offer financial products and services that we are unable to offer, putting us at a disadvantage in competing with them for loans and deposits and investment management clients. In addition, we face increased competition from financial technology firms that offer their solutions online and/or through the use of mobile phone apps and other technological means, which are increasingly preferred by younger consumers of financial services. If we are unable to compete effectively with those banking or other financial services businesses, we could find it more difficult to attract new and retain existing clients and our net interest margins, net interest income and investment management fees could decline, which could materially adversely affect our business, results of operations and prospects, and could cause us to incur losses in the future.

***We continually encounter technological change, and we may have fewer resources than many of our competitors to invest in technological improvements.***

The financial services industry is undergoing rapid technological changes with frequent introductions of new technology-driven products and services. The effective use of technology increases efficiency and enables financial institutions to better serve clients and to reduce costs. Our future success will depend, in part, upon our ability to address the needs of our clients by using technology to provide products and services that will satisfy client demands for convenience, as well as to create additional efficiencies in our operations. Many national vendors provide turn-key services that allow smaller banks to compete with institutions that have substantially greater resources to invest in technological improvements. However, these technology services may not be as sophisticated or adoptable as some of our larger competitors and we may be subject to long-term contracts that impede our ability to change vendors to adapt to a changing technology marketplace. Thus, we may not be able to effectively implement new technology-driven products and services or be successful in marketing these products and services to our clients.

***We depend on third party systems, so a systems failure could significantly disrupt our business. These and other operational risks may disrupt our business, result in regulatory action against us, or limit our growth.***

Our business depends highly on our ability to process, on a daily basis, a large number of transactions across numerous and diverse markets, and the transactions we process have become increasingly complex.

Consequently, we rely heavily on our communications and financial, accounting, and other data processing systems, including systems provided by our clearing brokers and service providers. We face operational risk arising from mistakes made in the confirmation or settlement of transactions or from transactions not being properly recorded, evaluated, or accounted.

If any of these systems do not operate properly or are disabled, we could suffer financial loss, a disruption of our business, liability to clients, regulatory intervention, or reputational damage. Any failure or interruption of our systems, the systems of our clearing brokers or custodians, or third party trading systems could cause delays or other problems in our securities trading activities, which could have a material adverse effect on our operating results. In addition, our clearing brokers and custodians provide our principal disaster recovery system. We cannot provide assurance that we or our clearing brokers or custodians will not suffer any systems failures or interruption, including ones caused by earthquake, fire, other natural disasters, power or telecommunications failure, act of God, act of war, terrorism, or otherwise, or that our or our clearing brokers' back-up procedures and capabilities in the event of any such failure or interruption will be adequate. The inability of our or our clearing brokers' or custodians' systems to accommodate an increasing volume of transactions could also constrain our ability to expand our business.

***We are exposed to cybersecurity risks associated with our internet-based systems and online commerce security, and our information systems could experience an interruption, failure, breach in security, or cyber-attack.***

The Company relies heavily on public utilities infrastructures, internal information and operating systems, and cloud-based solutions and storage to conduct its business, and these systems could fail in a variety of ways. In addition, the use of network, cloud-based, or third-party hosted systems expose the Company to the increased sophistication and activity of cyber-criminals, both domestic and international. A cyber incident is considered to be any adverse event that threatens the confidentiality, integrity, or availability of the information resources of the Company. These incidents may be an intentional attack or an unintentional event and could involve blocking the Company from accessing its own systems or remote servers in exchange for a ransom payment, gaining unauthorized access directly to our information systems, or indirectly through our vendors and customers systems or servers, for purposes of misappropriating assets, stealing confidential corporate information or customers' Personally Identifiable Information, corrupting data, denying access or causing operational disruption. The Company's independent third-party service providers or their subcontractors may also have access to customers' personal information and therefore also expose the Company to cybersecurity risk. Additionally, vendors' and customers' home, business or mobile information systems and the servers they rely on, are at risk of fraudulent corporate account takeovers which the Company may not be able to detect. There is no guarantee the Company's counteractions will be successful or that the Company will have the resources or technical expertise to anticipate, detect or prevent rapidly evolving types of cyber-attacks.

Third party or internal systems and networks may fail to operate properly or become disabled due to deliberate attacks or unintentional events. Our operations are vulnerable to disruptions from human error, natural disasters, power loss, computer viruses, spam attacks, denial of service attacks, unauthorized access and other unforeseen events. Undiscovered data corruption could render our customer information inaccurate. These events may obstruct our ability to provide services and process transactions. While we believe we are in compliance with all applicable privacy and data security laws, an incident could put our customer confidential information at risk. Although we have not experienced a cyber-incident which has compromised our data or systems, we can never be certain that all of our systems are entirely free from vulnerability to breaches of security or other technological difficulties or failures. We monitor and modify, as necessary, our protective measures in response to the perpetual evolution of cyber threats.

The occurrence of any failures or disruptions of infrastructure, or breakdown, breach, failures or interruptions of the Company's information systems, access points, or those hosted by third-party service providers and customers, or in the cloud, or the Company's inability to detect, respond, disclose and correct such occurrence or compromise in a timely manner, could result in an interruption in our ability to conduct transactions for an indeterminable length of time, could expose customers' personal and confidential information to unauthorized parties, increase the risk of fraud or theft, subject the Company to increased operational costs to detect and rectify the situation, damage the Company's reputation and deter customers from using the Company's services, and increase the Company insurance cost or the ability to obtain adequate cyber insurance coverage. In addition, as a result of any breach, we could incur higher costs to conduct our business, to increase protection or related to remediation. Furthermore, our customers could terminate their accounts with us because of a cyber-incident which occurred on their own system or with that of an unrelated third party, which is outside of our control. In addition, a security breach could also subject us to additional regulatory scrutiny and expose us to civil litigation and possible financial liability.

***We are subject to certain operating risks related to employee error and customer, employee and third party misconduct and fraudulent activity, which could harm our reputation and business.***

Employee error or employee and customer misconduct or fraudulent activity could subject us to financial losses or regulatory sanctions and harm our reputation. Misconduct by our employees could include hiding unauthorized activities from us, improper or unauthorized activities on behalf of our customers or improper use of confidential information, and misconduct or fraud by our customers could include check “kiting” or fraud, wire fraud or other dishonest activities. It is not always possible to prevent employee error or misconduct, and the precautions we take to prevent and detect this activity may not always be effective. Because the nature of the financial services business involves a high volume of transactions, certain errors may be repeated or compounded before they are discovered and rectified. Our necessary dependence upon processing systems to record and process transactions and our large transaction volume may further increase the risk that employee errors, tampering or manipulation of those systems will result in losses that are difficult to detect. Employee error or misconduct could also subject us to financial claims. If our internal control systems fail to prevent or detect an occurrence, or if any resulting loss is not insured, exceeds applicable insurance limits or if insurance coverage is denied or not available, it could have a material adverse effect on our business, financial condition and results of operations.

***Factoring products offered by the Bank’s Integra factoring division may expose us to an increased risk of fraud.***

We rely on the structural features embedded in the factoring products offered by the Bank’s Integra factoring division to mitigate the credit risk associated with such products. With respect to our factoring products, we purchase the underlying invoices of our customers and become the direct payee under such invoices, thus transferring the credit risk in such transactions from our customers to the underlying account debtors on such invoices. In the event one or more of our customers fraudulently represents the existence or validity of an invoice we purchase in the case of a factoring transaction, we may advance more funds to such customer than we otherwise would and lose the benefit of the structural protections of our products with respect to such advances. In such event we could be exposed to material additional losses with respect to such factoring products. Although we believe we have controls in place to monitor and detect fraud with respect to our factoring products, there is no guarantee such controls will be effective. Losses from such fraudulent activity could have a material impact on our business, financial condition and results of operations.

***We rely on client and counterparty information, which subjects us to risks if that information is not accurate or is incomplete.***

When deciding whether to extend credit or enter into other transactions with clients or counterparties, we may rely on information provided by or on behalf of those clients and counterparties, including audited financial statements and other financial information. We may also rely on representations made by clients and counterparties that the information they provide is accurate and complete. We conduct appropriate due diligence on such client information and, where practical and economical, we engage valuation and other experts or sources of information to assist with assessing collateral and other client risks. Our financial results could be adversely affected if the financial statements, collateral value or other financial information provided by clients or counterparties are incorrect.

***Climate change and related legislative and regulatory initiatives may materially affect the Company’s business and results of operations.***

The effects of climate change continue to create an alarming level of concern for the state of the global environment. As a result, the global business community has increased its political and social awareness surrounding the issue. Further, the U.S. Congress, state legislatures and federal and state regulatory agencies continue to propose numerous initiatives to supplement the global effort to combat climate change. Similar and even more expansive initiatives are expected under the current administration, including potentially increasing supervisory expectations with respect to banks’ risk management practices, accounting for the effects of climate change in stress testing scenarios and systemic risk assessments, revising expectations for credit portfolio concentrations based on climate-related factors and encouraging investment by banks in climate-related initiatives and lending to communities disproportionately impacted by the effects of climate change. The lack of empirical data surrounding the credit and other financial risks posed by climate change render it impossible to predict how specifically climate change may impact our financial condition and results of operations; however, the physical effects of climate change may also directly impact us. Specifically, unpredictable and more frequent weather disasters may adversely impact the value of real property securing the loans in our portfolios. Additionally, if insurance obtained by our borrowers is insufficient to cover any losses sustained to the collateral, or if insurance coverage is otherwise unavailable to our borrowers, the collateral securing our loans may be negatively impacted by climate change, which could impact our financial condition and results of operations. Further, the effects of climate change may negatively impact regional and local economic activity, which could lead to an adverse effect on our customers and impact the communities in which we operate. Overall, climate change, its effects and the resulting, unknown impact could have a material adverse effect on our financial condition and results of operations.

***A natural disaster could harm our business.***

We have clients across the United States, but concentrations in California (subject to earthquakes and wildfires), Florida (hurricanes) and Texas (hurricanes, tornadoes, wildfires and flooding). The nature and level of natural disasters cannot be predicted. These natural disasters could harm our operations through interference with communications, including the interruption or loss of our computer systems, which could prevent or impede us from gathering deposits, originating loans and processing and controlling our flow of business, as well as through the destruction of facilities and our operational, financial and management information systems. Additionally, natural disasters could negatively impact the values of collateral securing our borrowers' loans and interrupt our borrowers' abilities to conduct their business in a manner to support their debt obligations, either of which could result in losses and increased provisions for credit losses for us.

***The costs and effects of litigation, investigations or similar matters, or adverse facts and developments related thereto, could materially affect our business, operating results and financial condition.***

We may be involved from time to time in a variety of litigation, investigations or similar matters arising out of our business. It is inherently difficult to assess the outcome of these matters, and we may not prevail in proceedings or litigation. Our insurance may not cover all claims that may be asserted against us and indemnification rights to which we are entitled may not be honored, and any claims asserted against us, regardless of merit or eventual outcome, may harm our reputation. Should the ultimate judgments or settlements in any litigation or investigation significantly exceed our insurance coverage, they could have a material adverse effect on our business, financial condition and results of operations. In addition, premiums for insurance covering the financial and banking sectors are rising. We may not be able to obtain appropriate types or levels of insurance in the future, nor may we be able to obtain adequate replacement policies with acceptable terms or at historic rates, if at all.

***The Company is subject to environmental risks associated with owning real estate or collateral.***

The cost of cleaning up or paying damages and penalties associated with environmental problems could increase the Company's operating expenses and result in a decline in the underlying collateral. When a borrower defaults on a loan secured by real property, the Company may purchase the property in foreclosure or accept a deed to the property surrendered by the borrower. The Company may also take over the management of commercial properties whose owners have defaulted on loans. The Company also owns and leases premises where banking and other facilities are located. While the Company's lending, foreclosure and facilities policies and guidelines are intended to exclude properties with an unreasonable risk of contamination, hazardous substances could exist on some of the properties that the Company may own, acquire, manage or occupy. Environmental laws could force the Company to clean up the properties at the Company's expense. It may cost much more to clean a property than the property is worth and it may be difficult or impossible to sell contaminated properties. The Company could also be liable for pollution generated by a borrower's operations if the Company takes a role in managing those operations after a default.

**Risks Related to Our Regulatory Environment**

***We are subject to extensive government regulation and supervision, which could constrain our growth and profitability.***

We are subject to extensive regulation, supervision and legal requirements that govern almost all aspects of our operations. These laws and regulations are not intended to protect our shareholders. Rather, these laws and regulations are intended to protect customers, depositors, the DIF and the overall financial stability of the banking system in the United States. These laws and regulations, among other matters, prescribe minimum capital requirements, impose limitations on the business activities in which we can engage, limit the dividend or distributions that the Bank can pay to us, restrict the ability of institutions to guarantee any debt we may issue and impose certain specific accounting requirements on us that may be more restrictive and may result in greater or earlier charges to earnings or reductions in our capital than generally accepted accounting principles would require. Compliance with laws and regulations can be difficult and costly, and changes to laws and regulations often impose additional compliance costs. Our failure to comply with these laws and regulations, even if the failure follows good faith effort or reflects a difference in interpretation, could subject us to restrictions on our business activities, fines and other penalties, any of which could adversely affect our results of operations, capital base and the price of our securities. Further, any new laws, rules and regulations could make compliance more difficult or expensive or otherwise adversely affect our business, financial condition and results of operations. The banking industry remains heavily regulated. Compliance with such regulations may increase our costs and limit our ability to pursue business opportunities.

See "Supervision and Regulation" for additional information regarding the supervisory and regulatory issues facing the Company.

***Recent bank failures and the related negative impact on customer confidence in the safety and soundness of the banking industry may adversely affect our business, earnings and financial condition.***

The Company is exposed to a number of risks when other financial institutions experience financial difficulties, which could result in an adverse impact on the regional banking industry, generally, and the business environment in which the Company operates. Recent bank failures during 2023 have resulted in significant market volatility among publicly traded bank holding companies and has caused uncertainty in the investor community and bank customers, generally. While the Company does not believe that the circumstances of the bank failures in 2023 are indicators of broader issues within the banking industry, bank failures may negatively impact customer confidence in the safety and soundness of regional banks and, as a result, customers may choose to maintain deposits with larger financial institutions or invest in higher yielding short-term fixed income securities, all of which could materially adversely impact our liquidity, cost of funding, loan funding capacity, net interest margin, capital and results of operations.

Moreover, the FDIC's sale of one of the institutions resulted in \$20 billion in projected losses to the DIF. More losses may result from this institution or others. The resultant losses to the DIF will likely result in higher premiums for depository insurance and increased regulatory scrutiny, which will result in higher compliance costs and likely greater regulation. Each of these results will reduce the profitability and increase the regulatory costs of the Company. Management continues to monitor the ongoing events concerning the 2023 bank failures as well as any volatility within the financial services industry generally, together with any responsive measures taken by the banking regulators to mitigate or manage potential turmoil in the financial services industry.

***We are subject to stringent capital requirements that may limit our operations and potential growth.***

We are subject to various regulatory capital requirements on a consolidated basis, and at both the Bank and Sanders Morris separately. Failure to meet minimum capital requirements can initiate certain mandatory, and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on our financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of our assets, liabilities and certain off-balance sheet commitments as calculated under these regulations. The failure to meet the established capital requirements under the prompt corrective action framework could result in one or more of our regulators placing limitations or conditions on our activities, including our growth initiatives, or restricting the commencement of new activities, and such failure could subject us to a variety of enforcement remedies available to the federal regulatory authorities, including limiting our ability to pay dividends, issuing a directive to increase our capital and terminating the Bank's FDIC deposit insurance. FDIC deposit insurance is critical to the continued operation of the Bank. In addition, an inability to meet the capital requirements under the Basel III regulatory capital reforms, would prevent us from being able to pay certain discretionary bonuses to our executive officers and dividends to our shareholders.

Many factors affect the calculation of our risk-based assets and our ability to maintain the level of capital required to achieve acceptable capital ratios. For example, changes in risk weightings of assets relative to capital and other factors may combine to increase the amount of risk-weighted assets in the Tier 1 risk-based capital ratio and the total risk-based capital ratio. Any increases in our risk-weighted assets will require a corresponding increase in our capital to maintain the applicable ratios. In addition, recognized credit losses in excess of amounts reserved for such losses, loan impairments and other factors will decrease our capital, thereby reducing the level of the applicable ratios.

Our failure to remain well-capitalized for bank regulatory purposes, either under the Basel III regime or the community bank leverage ratio framework, could affect client and investor confidence, our ability to grow, our costs of funds, our ability to pay competitive rates to attract and retain deposits, FDIC insurance costs, our ability to pay dividends on preferred and common stock, our ability to make acquisitions, and our business, results of operations and financial condition. In addition, if we cease to be a well-capitalized institution for bank regulatory purposes, the interest rates that we pay on deposits and our ability to accept brokered deposits may be restricted.

***Federal banking agencies periodically conduct examinations of our banking business, including compliance with laws and regulations, and our failure to comply with any supervisory actions which we are, or may become, subject to as a result of such examinations may adversely affect us.***

The OCC, the Federal Reserve and the FDIC may conduct examinations of our business, including for compliance with applicable laws and regulations. As a result of an examination, regulatory agencies may determine that the financial condition, capital resources, asset quality, asset concentrations, earnings prospects, management, liquidity, sensitivity to market risk, or other aspects of any of our operations are unsatisfactory, or that we or our management are in violation of any law, regulation or guideline in effect from time to time. Regulatory agencies may take a number of different remedial actions, including the power to enjoin “unsafe or unsound” practices, to require affirmative actions to correct any conditions resulting from any violation or practice, to issue an administrative order that can be judicially enforced, to direct an increase in our capital, to restrict our growth, to change the composition of our concentrations in portfolio or balance sheet assets, to assess civil monetary penalties against officers or directors, to remove officers and directors and, if such conditions cannot be corrected or there is an imminent risk of loss to depositors, the FDIC may terminate our deposit insurance. A regulatory action against us could have a material adverse effect on our business, results of operations, financial condition and prospects.

***We are subject to numerous laws designed to protect consumers, including the CRA and fair lending laws, and failure to comply with these laws could lead to a wide variety of sanctions.***

The CRA, the Equal Credit Opportunity Act, the Fair Housing Act and other fair lending laws and regulations impose nondiscriminatory lending requirements on financial institutions. The U.S. Department of Justice, the CFPB, and other federal agencies are responsible for enforcing these laws and regulations. A successful regulatory challenge to an institution’s performance under the CRA or fair lending laws and regulations could result in a wide variety of sanctions, including damages and civil money penalties, injunctive relief, restrictions on mergers and acquisitions activity, restrictions on expansion, and restrictions on entering new business lines. Private parties may also have the ability to challenge an institution’s performance under fair lending laws in private class action litigation. Any such actions could have a material adverse effect on our business, financial condition, results of operations and prospects.

***We face a risk of noncompliance and enforcement action with the BSA and other anti-money laundering statutes and regulations.***

The BSA, as amended by the USA PATRIOT Act, and as further amended by the National Defense Authorization Act, and other laws and regulations require financial institutions, among other duties, to institute and maintain effective anti-money laundering programs and file suspicious activity and currency transaction reports as appropriate. FinCEN, established by the U.S. Department of the Treasury to administer the BSA, is authorized to impose significant civil money penalties for violations of those requirements and has recently engaged in coordinated enforcement efforts with the individual federal banking regulators, as well as the U.S. Department of Justice, Drug Enforcement Administration and Internal Revenue Service (the “IRS”). There is also increased scrutiny of compliance with the sanctions rules enforced by OFAC. If our policies, procedures and systems are deemed deficient or the policies, procedures and systems of any financial institutions that we may acquire in the future are deemed deficient, we could be subject to liability, including fines and regulatory actions such as restrictions on our ability to pay dividends and the necessity to obtain regulatory approvals to proceed with certain aspects of our business plan, which could negatively impact our business, financial condition and results of operations. Although we have not been subject to fines or other penalties, or suffered business or reputational harm, as a result of money laundering activities, failure to maintain and implement adequate programs to combat money laundering and terrorist financing could also have serious reputational consequences for us. Any of these results could materially and adversely affect our business, financial condition, results of operations and prospects.



***Additional regulations and rule making impacting the transportation industry may have a disproportionate impact on the small-to-mid-sized trucking businesses that comprise our primary transportation factoring clients and adversely affect the factoring business conducted by the Bank's Integra factoring division.***

Our primary transportation factoring clients are small-sized owner-operators and trucking fleets. Recently implemented federal regulations, and regulations proposed to be implemented in the future, may significantly increase the costs and expenses or reduce the ability to generate revenue associated with owning or operating a trucking fleet. These regulations include rule making proposed by the Federal Motor Carrier Safety Administration of the United States Department of Transportation ("FMCSA") under the Compliance, Safety, Accountability ("CSA") initiative, maximum hours of service limitations imposed by the FMCSA, electronic log requirements, and regulations proposed by the federal Food and Drug Administration ("FDA") requiring increased labeling and monitoring by carriers of any commodity transported that is regulated by the FDA. The costs and burdens of compliance with these requirements will have a disproportionate impact on the small-to-mid-sized trucking businesses that comprise our client base and may force some or all of these businesses out of the market. Such an occurrence could impact the returns we realize on the factoring activity conducted by the Bank's Integra factoring division or result in a decrease in the overall amount of factoring activity conducted by the Bank's Integra factoring division and could have an adverse effect on our business, financial condition and results of operations.

***Sanders Morris and Tectonic Advisors are subject to substantial regulation. If we fail to comply with applicable requirements, our business will be adversely affected.***

Tectonic Advisors and Sanders Morris are subject to extensive regulation under both federal and state laws. Sanders Morris is registered as a broker-dealer with the SEC and FINRA; Tectonic Advisors and Sanders Morris are registered with the SEC as investment advisors. The SEC is the federal agency responsible for the administration of federal securities laws. In addition, SROs, principally FINRA and the securities exchanges, are actively involved in the regulation of broker-dealers. Tectonic Advisors and Sanders Morris are also subject to regulation by state securities commissions in those states in which we do business. The principal purpose of regulation and discipline of broker-dealers is the protection of clients and the securities markets rather than protection of creditors and shareholders of broker-dealers. Broker-dealers are subject to regulations that cover all aspects of the securities business, including sales methods, trade practices among broker-dealers, use and safekeeping of clients' funds and securities, capital structure of securities firms, record-keeping, and the conduct of directors, officers, and employees.

As investment advisors, Sanders Morris and Tectonic Advisors are subject to the Advisers Act. The Advisers Act imposes numerous obligations on registered investment advisers, including fiduciary, record keeping, operational and disclosure obligations. Moreover, the Advisers Act grants broad administrative powers to regulatory agencies such as the SEC to regulate investment advisory businesses. Sanders Morris and Tectonic Advisors are also subject to the provisions and regulations of ERISA to the extent that they act as a "fiduciary" under ERISA with respect to certain of their clients. ERISA and the applicable provisions of the federal tax laws impose a number of duties on persons who are fiduciaries under ERISA and prohibit certain transactions involving the assets of each ERISA plan which is a client, as well as certain transactions by the fiduciaries (and certain other related parties) to such plans. Additionally, like other investment advisory and broker-dealer companies, Sanders Morris and Tectonic Advisors face the risks of lawsuits by clients. The outcome of regulatory proceedings and lawsuits is uncertain and difficult to predict. An adverse resolution of any regulatory proceeding or lawsuit could result in substantial costs or reputational harm to Sanders Morris or Tectonic Advisors and, therefore, could have an adverse effect on the ability to retain key relationship and wealth managers, and to retain existing clients or attract new clients, any of which could have a material adverse effect on our business, financial condition, results of operations and prospects.

Sanders Morris is subject to periodic examinations by the SEC and FINRA and Tectonic Advisors by the SEC. In these examinations, personnel from FINRA or the SEC (as applicable) make a visit to the office(s) of Sanders Morris or Tectonic Advisors and review the files, business practices and personnel. These reviews are often based on a pre-examination checklist or areas of interest, often based on the risks associated with Sanders Morris' or Tectonic Advisors' business. The examiners consult with their home office and, at the end of the examination, often issue a letter setting forth areas requiring attention. However, under certain circumstances, a poor examination or a violation brought to the SEC's or FINRA's attention can result in an administrative proceeding.

The SEC, FINRA, and state securities commissions may conduct administrative proceedings that can result in:

- censure, fines, or civil penalties;
- issuance of cease-and-desist orders;
- deregistration, suspension, or expulsion of a broker-dealer or investment advisor;
- suspension or disqualification of the broker-dealer's officers or employees;
- prohibition against engaging in certain lines of business; and
- other adverse consequences.

In the last five years, neither Tectonic Advisors nor Sanders Morris has received what either believes is a poor examination by any of their federal or state regulators, been subject to any material administrative proceeding or been found to be in material violation by their federal or state regulators or experienced an imposition of any material penalties, censure, fines or cease-and-desist orders by such regulators. The imposition of any penalties or orders on us could have a material adverse effect on our business, financial condition, and results of operations. The investment banking and brokerage industries have recently come under scrutiny at both the state and federal levels, and the cost of compliance and the potential liability for noncompliance has increased as a result.

Our ability to comply with laws and regulations relating to our financial services businesses depends in large part upon maintaining a system to monitor compliance and our ability to attract and retain qualified compliance personnel. Although we believe we are in material compliance with all applicable laws and regulations, we may not be able to comply in the future. Any noncompliance could have a material adverse effect on our business, financial condition, and results of operations.

***Regulations relating to privacy, information security and data protection could increase our costs, affect or limit how we collect and use personal information and adversely affect our business opportunities.***

We are subject to various privacy, information security and data protection laws, including requirements concerning security breach notification, and we could be negatively impacted by these laws. For example, our business is subject to the GLBA, which, among other things: (i) imposes certain limitations on our ability to share non-public personal information about our clients with non-affiliated third parties; (ii) requires that we provide certain disclosures to clients about our information collection, sharing and security practices and afford clients the right to "opt out" of any information sharing by us with non-affiliated third parties (with certain exceptions); and (iii) requires we develop, implement and maintain a written comprehensive information security program containing safeguards appropriate based on our size and complexity, the nature and scope of our activities, and the sensitivity of client information we process, as well as plans for responding to data security breaches. Various state and federal banking regulators and states and foreign countries have also enacted data security breach notification requirements with varying levels of individual, consumer, regulatory or law enforcement notification in certain circumstances in the event of a security breach. Moreover, legislators and regulators in the United States and other countries are increasingly adopting or revising privacy, information security and data protection laws that potentially could have a significant impact on our current and planned privacy, data protection and information security-related practices, our collection, use, sharing, retention and safeguarding of consumer or employee information, and some of our current or planned business activities. This could also increase our costs of compliance and business operations and could reduce income from certain business initiatives. This includes increased privacy-related enforcement activity at the federal level, by the Federal Trade Commission, as well as at the state level, such as with regard to mobile applications.

Compliance with current or future privacy, data protection and information security laws (including those regarding security breach notification) affecting client or employee data to which we are subject could result in higher compliance and technology costs and could restrict our ability to provide certain products and services, which could have a material adverse effect on our business, financial condition or results of operations. Our failure to comply with privacy, data protection and information security laws could result in potentially significant regulatory or governmental investigations or actions, litigation, fines, sanctions and damage to our reputation, which could have a material adverse effect on our business, financial condition or results of operations.

***We can be subject to legal and regulatory proceedings, investigations and inquiries related to conduct risk.***

U.S. authorities have been increasingly focused on “conduct risk,” a term that is used to describe the risks associated with behavior by employees and agents, including third-party vendors, that could harm clients, consumers, investors or the markets, such as failures to safeguard consumers’ and investors’ personal information, failures to identify and manage conflicts of interest and improperly creating, selling and marketing products and services. In addition to increasing compliance risks, this focus on conduct risk could lead to more regulatory or other enforcement proceedings and litigation, including for practices which historically were acceptable but are now receiving greater scrutiny. Further, while we take numerous steps to prevent and detect conduct by employees and agents that could potentially harm clients, investors or the markets, such behavior may not always be deterred or prevented. Banking regulators have also focused on the overall culture of financial services firms. In addition to regulatory restrictions or structural changes that could result from perceived deficiencies in our culture, such focus could also lead to additional regulatory proceedings. Although we have not been subject to any material conduct risk investigations or inquiries in the past eight years, the occurrence of such proceedings, investigations or inquiries could damage our reputation, disrupt our business, increase our costs and causes losses in the future.

**Risks Related to an Investment in the Series B Preferred Stock**

***The Series B preferred stock is an equity security and is subordinate to our existing and future indebtedness, which could adversely impact our ability to pay dividends on the Series B preferred stock.***

The shares of Series B preferred stock are equity interests and do not constitute indebtedness of ours. This means that the Series B preferred stock ranks junior to all our existing and future indebtedness and our other non-equity claims with respect to assets available to satisfy claims against us, including claims in the event of our liquidation.

As of December 31, 2023, our total liabilities were approximately \$570.5 million, and we may incur additional indebtedness in the future to increase our capital resources or fund strategic acquisitions or other business efforts. Additionally, if our capital ratios or the capital ratios of the Bank fall below minimum ratios required by the Federal Reserve, we or the Bank could be required to raise additional capital by making additional offerings of debt securities, including senior or subordinated notes, or other applicable securities that could rank senior to the Series B preferred stock. The Series B preferred stock places no restrictions on our business or operations or on our ability to incur indebtedness or engage in any transactions, subject only to the limited voting rights referred to below. In addition, dividends on the Series B preferred stock are payable only when, as, and if declared by our board of directors out of assets legally available therefor. In the event of our liquidation, dissolution or winding-up of our affairs, our assets will be available to pay obligations on the Series B preferred stock only after all of our indebtedness and other liabilities have been paid. Accordingly, our existing and future indebtedness may restrict the payment of dividends on the Series B preferred stock. Further, if we are unable to or do not pay dividends on the Series B preferred stock, the market price of the Series B preferred stock may decline.

***The Series B preferred stock may be junior in rights and preferences to our future preferred stock.***

The Series B preferred stock may rank junior to preferred stock issued in the future that by its terms is expressly senior in rights and preferences to the Series B preferred stock, although the affirmative vote or consent of the holders of at least 66⅔% of all outstanding shares of the Series B preferred stock is required to authorize or issue any shares of stock senior in rights and preferences to the Series B preferred stock. The terms of any future preferred stock expressly senior to the Series B preferred stock may restrict dividend payments on the Series B preferred stock.

***Additional issuances of preferred stock or securities convertible into preferred stock may further dilute existing holders of the Series B preferred stock.***

We may determine that it is advisable, or we may encounter circumstances where we determine it is necessary, to issue additional shares of preferred stock, securities convertible into, exchangeable for or that represent an interest in preferred stock, or preferred stock-equivalent securities to fund strategic initiatives or other business needs or to build additional capital. Our board of directors is authorized to cause us to issue one or more classes or series of preferred stock from time to time without any action on the part of the shareholders, including issuing additional shares of Series B preferred stock. Our board of directors also has the power, without shareholder approval, to set the terms of any such classes or series of preferred stock that may be issued, including voting rights, dividend rights and preferences over the Series B preferred stock with respect to dividends or upon our dissolution, winding-up and liquidation and other terms.

Although the affirmative vote or consent of the holders of at least 66 2/3% of all outstanding shares of the Series B preferred stock is required to authorize or issue any shares of capital stock senior in rights and preferences to the Series B preferred stock, if we issue preferred stock in the future with voting rights that dilute the voting power of the Series B preferred stock, the rights of holders of the Series B preferred stock or the market price of the Series B preferred stock could be adversely affected. The market price of the Series B preferred stock could decline as a result of these other offerings, as well as other sales of a large block of Series B preferred stock or similar securities in the market thereafter, or the perception that such sales could occur. Holders of the Series B preferred stock are not entitled to preemptive rights or other protections against dilution.

***Payment of dividends by the Company on its common stock, corporate spin-offs or other corporate actions may diminish the amount of capital and/or earning power of the Company to pay dividends on, or redeem, its Series B preferred stock.***

Subject to regulatory requirements and the terms of the Series B preferred stock, the Company may: (a) and currently intends to, pay dividends on its common stock and any such payment reduces the capital of the Company available to the Series B preferred stock and (b) undertake certain corporate actions, including, without limitation, spinning off subsidiaries and/or businesses to its stockholders, selling businesses to third parties, (c) making acquisitions using capital from the Company and (d) borrowing and/or investing its capital to make acquisitions and/or for other purposes (hiring key personnel, etc.). In each of these cases, the holders of the Series B preferred stock may not have the ability to block certain of such actions and, in such case, the capital base and/or earnings of the Company may be negatively impacted. In such case, the ability of the Company to pay dividends on and/or redeem the Series B preferred stock may be negatively impacted.

***Dividends on the Series B preferred stock are discretionary and non-cumulative, and our future ability to pay dividends is subject to restrictions.***

Although we intend to continue to pay dividends on the Series B preferred stock, dividends on the Series B preferred stock are discretionary and are not mandatory or cumulative. If our board of directors does not declare a dividend on the Series B preferred stock or if our board of directors authorizes and we declare less than a full dividend in respect of a Dividend Period, the holders of the Series B preferred stock will have no right to receive any dividend or a full dividend, as the case may be, for the Dividend Period, and we will have no obligation to pay a partial or full dividends for that Dividend Period at any time, whether or not our board of directors declares a dividend on the Series B preferred stock or any other class or series of our capital stock for any future Dividend Period. Any declaration and payment of dividends on the Series B preferred stock depends upon, among other factors, our earnings and financial condition, liquidity and capital requirements, the general economic and regulatory climate, our ability to service any equity or debt obligations senior to the Series B preferred stock, dividend restrictions contained in any credit agreements and other factors deemed relevant by our board of directors.

The Bank and Sanders Morris are subject to capital ratios. In addition, the Company is subject to consolidated capital ratios, which take into account its underlying subsidiaries' capital position and the capital position of the Company. To the extent that Sanders Morris and/or the Bank suffer losses (including, without limitation, credit losses at the Bank), they may fail to meet their minimum capital requirements necessary for them to pay dividends to the Company, which would impact the Company's ability to pay dividends on the preferred stock. In addition, to the extent that the Company and/or its underlying subsidiaries (including the Bank) suffer losses that cause the Company to be less than "well capitalized", then the Company, even if it has cash available to it, would not be permitted to pay dividends on the preferred stock without regulatory approval, which may not be granted. Accordingly, any losses suffered by the Company or any of its subsidiaries, particularly credit losses at the Bank, might have a material adverse effect on the Company, including on the ability of the Company to pay dividends on the preferred stock.

The Federal Reserve has indicated that bank holding companies should carefully review their dividend policy in relation to the organization's overall asset quality, current and prospective earnings and level, composition and quality of capital. The guidance provides that we inform and consult with the Federal Reserve prior to declaring and paying a dividend that exceeds earnings for the period for which the dividend is being paid or that could result in an adverse change to our capital structure, including interest on any debt obligations.

In addition, the Company is a separate and distinct legal entity from its subsidiaries. It receives substantially all of its revenue from dividends paid by or distributions made from its subsidiaries. These dividends and distributions are the principal source of funds to pay dividends on our preferred stock and common stock and interest and principal on our debt. Various federal and/or state laws and regulations limit the amount of dividends or distributions that our bank and nonbank subsidiaries may pay to the Company. In the event our subsidiaries are unable to pay dividends or make distributions to the Company, the Company may not be able to service debt or pay dividends on the Series B preferred stock. The inability to receive dividends and distributions from our subsidiaries could have a material adverse effect on the Company's business, financial condition, results of operations and liquidity.

**The replacement of the London Inter-bank Offered Rate (“LIBOR”) on our Series B preferred stock could increase our interest payments, may adversely affect the value of the Series B preferred stock and could adversely impact our business, financial condition and results of operations.**

In March 2021, the United Kingdom’s Financing Conduct Authority and the Intercontinental Exchange Benchmark Administration, the administrator for LIBOR, concurrently announced that certain settings of LIBOR would no longer be published on a representative basis after December 31, 2021, and the most commonly used U.S. dollar LIBOR settings would no longer be published on a representative basis after June 30, 2023. The Federal Reserve Board and the Federal Reserve Bank of New York organized the Alternative Reference Rates Committee, which identified SOFR as its preferred alternative to LIBOR in derivatives and other financial contracts. With the transition from LIBOR to SOFR as the preferred alternative to LIBOR, we have transitioned and amended our contracts and financial instruments, including the Series B preferred stock, to reference the SOFR rate where required.

SOFR has a very limited history, and its historical performance is not indicative of future performance. The Federal Reserve began to publish SOFR in April 2018; therefore, SOFR has limited performance history and no actual investment based on the performance of SOFR was possible before April 2018. The level of SOFR during the floating rate period for our Series B preferred stock may bear little or no relation to the historical level of SOFR. Furthermore, the future performance of SOFR is impossible to predict and, as a result, no future performance of SOFR or our Series B preferred stock may be inferred from any historical performance data. Changes in the levels of SOFR may affect the return on, and trading price of, our Series B preferred stock, but it is impossible to predict whether such levels will rise or fall. Since the initial publication of SOFR, daily changes in the rate have, on occasion, been more volatile than daily changes in other benchmark or market rates, such as U.S. dollar LIBOR, during corresponding periods.

The composition and characteristics of SOFR are not the same as those of U.S. dollar LIBOR and any failure of SOFR to gain market acceptance could adversely affect the Series B preferred stock. SOFR was developed for use in certain U.S. dollar derivatives and other financial contracts as an alternative to the U.S. dollar LIBOR in part because it is considered representative of general funding conditions in the overnight Treasury repo market. However, as a rate based on transactions secured by U.S. Treasury securities, it does not measure bank-specific credit risk and, as a result, is less likely to correlate with the unsecured short-term funding costs of banks. In addition, SOFR is an overnight rate, while U.S. dollar LIBOR represents interbank funding over different maturities. As a result, there can be no assurance that SOFR will perform in the same way as U.S. dollar LIBOR would have at any time, including, without limitation, as a result of changes in interest and yield rates in the market, market volatility, or global or regional economic, financial, political, regulatory, judicial or other events. The differences between SOFR and U.S. dollar LIBOR may mean that market participants would not consider SOFR a suitable substitute or successor for all of the purposes for which U.S. dollar LIBOR historically has been used, which may, in turn, lessen market acceptance of SOFR. If SOFR does not prove to be widely used in securities that are similar or comparable to the Series B preferred stock, the trading price of those securities may be adversely affected.

***Dividends on the Series B preferred stock will vary beginning on May 15, 2024 and any dividends declared may be less than the initial fixed annual rate in effect prior to May 15, 2024.***

As described in further detail in the description of the Series B preferred stock attached to this Form 10-K, the annual dividend rate on the Series B preferred stock commencing on May 15, 2024 will equal three-month CME Term SOFR, plus a spread of 672 basis points per annum. Notwithstanding the foregoing, in the event that three-month CME Term SOFR is less than zero, three-month CME Term SOFR shall be deemed to be zero. Therefore, any dividends declared on or after May 15, 2024 may vary from period to period and could be more or less than the fixed rate for the initial period. We have no control over a number of factors that may affect market interest rates, including geopolitical conditions and economic, financial, political, regulatory, judicial or other events that affect the markets generally and that are important in determining the existence, magnitude and longevity of market rate risk.

***The Series B preferred stock may be redeemed at our option, and you may not be able to reinvest the redemption price you receive in a similar security.***

Subject to the approval of the Federal Reserve (if then required), at our option, we may redeem the Series B preferred stock at any time, either in whole or in part, for cash, on any dividend payment date on or after May 15, 2024. We may also redeem the Series B preferred stock at our option, subject to the approval of the Federal Reserve (if then required), at any time, in whole, but not in part, within 90 days following the occurrence of a Regulatory Capital Treatment Event (as defined in the description of the Series B preferred stock attached to this Form 10-K), such as a proposed change in law or regulation with respect to whether the Series B preferred stock qualifies as an “additional Tier 1 capital” instrument.

Although the terms of the Series B preferred stock were established at issuance to satisfy the criteria for “additional Tier 1 capital” instruments consistent with Basel III as set forth in the joint final rulemaking issued in July 2013 by the Federal Reserve, the FDIC and the OCC, it is possible that the Series B preferred stock may not satisfy the criteria set forth in future rulemakings or interpretations. As a result, a Regulatory Capital Treatment Event could occur whereby we would have the right, subject to prior approval of the Federal Reserve (if then required), to redeem the Series B preferred stock in accordance with its terms prior to May 15, 2024, or any date thereafter.

If we redeem the Series B preferred stock for any reason, you may not be able to reinvest the redemption proceeds you receive in a similar security or earn similar rate of return on any investment. See the description of the Series B preferred stock attached to this Form 10-K for more information on redemption of the Series B preferred stock.

***Investors should not expect us to redeem the Series B preferred stock on the date it becomes redeemable or on any particular date after it becomes redeemable.***

The Series B preferred stock is a perpetual equity security. This means that it has no maturity or mandatory redemption date and is not redeemable at the option of the holders of the Series B preferred stock. The Series B preferred stock may be redeemed by us at our option, either in whole or in part, for cash, on any dividend payment date on or after May 15, 2024, or in whole, but not in part, at any time within 90 days following a Regulatory Capital Treatment Event. Any decision we may make at any time to propose a redemption of the Series B preferred stock will depend upon, among other things, our evaluation of our capital position, the composition of our shareholders’ equity and general market conditions at that time.

In addition, our right to redeem the Series B preferred stock is subject to limitations. Under the Federal Reserve’s current risk-based capital guidelines applicable to bank holding companies, any redemption of the Series B preferred stock is subject to prior approval of the Federal Reserve. We cannot assure you that the Federal Reserve will approve any redemption of the Series B preferred stock that we may propose. There also can be no assurance that, if we propose to redeem the Series B preferred stock without replacing such capital with common equity Tier 1 capital or additional Tier 1 capital instruments, the Federal Reserve will authorize such redemption. We understand that the factors that the Federal Reserve will consider in evaluating a proposed redemption, or a request that we be permitted to redeem the Series B preferred stock without replacing it with common equity Tier 1 capital or additional Tier 1 capital instruments, include its evaluation of the overall level and quality of our capital components, considered in light of our risk exposures, earnings and growth strategy, and other supervisory considerations, although the Federal Reserve may change these factors at any time.

***Holders of the Series B preferred stock have limited voting rights.***

Holders of the Series B preferred stock have no voting rights with respect to matters that generally require the approval of our common shareholders. Holders of the Series B preferred stock have voting rights only with respect to (i) authorizing, creating or issuing any capital stock ranking senior to the Series B preferred stock as to dividends and rights (including redemption payments) upon liquidation, dissolution or winding up, or reclassifying any authorized capital stock into any such shares of such capital stock or issuing any obligation or security convertible into or evidencing the right to purchase any such shares of capital stock, (ii) amending, altering or repealing any provision of our certificate of formation or the designation, including by merger, consolidation or otherwise, so as to adversely affect the rights, powers or preferences of the Series B preferred stock, (iii) the election of two directors, if dividends have not been declared or paid in an aggregate amount equal to the equivalent of at least six or more quarterly Dividend Periods, whether or not consecutive, (voting as a class with holders of shares of any other series of preferred stock ranking equally as to the payment of dividends and having equivalent voting rights), and (iv) as otherwise required by applicable law. See the description of the Series B preferred stock attached to this Form 10-K for more information.

***An active, liquid market for the Series B preferred stock may not be sustained, which may impair your ability to sell your shares.***

The Series B preferred stock is currently traded on the NASDAQ Global Market, but an active, liquid trading market for the Series B preferred stock may not exist or, if it exists, may not be sustained over time. A public trading market having the desired characteristics of depth, liquidity and orderliness depends upon the presence in the marketplace and independent decisions of willing buyers and sellers of the Series B preferred stock, over which we have no control. Without an active, liquid trading market for the Series B preferred stock, shareholders may not be able to sell their shares at the volume, prices and times desired. Moreover, the lack of an established market could materially and adversely affect the value of the Series B preferred stock. The market price of the Series B preferred stock could decline significantly due to failure to pay dividends, actual or anticipated issuances or sales of the Series B preferred stock or other securities in the future.

***The market price of the Series B preferred stock may become subject to substantial fluctuations, which may make it difficult for you to sell your shares at the volume, prices and times desired.***

The market price of the Series B preferred stock may become highly volatile. There are many factors that may affect the market price and trading volume of the Series B preferred stock, including, without limitation:

- actual or anticipated fluctuations in our operating results, financial condition or asset quality;
- changes in economic or business conditions;
- the effects of, and changes in, trade, monetary and fiscal policies, including the interest rate policies of the Federal Reserve;
- recommendations by securities analysts;
- operating and stock price performance of companies that investors deemed comparable to us;
- additional or anticipated sales of the Series B preferred stock or other securities by us or our existing shareholders;
- additions or departures of key personnel;
- perceptions in the marketplace regarding our competitors or us;
- significant acquisitions or business combinations, strategic partnerships, joint ventures or capital commitments by or involving our competitors or us;
- other economic, competitive, governmental, regulatory and technological factors affecting our operations, pricing, products and services; and
- other news, announcements or disclosures (whether by us or others) related to us, our competitors, our primary markets or the financial services industry.

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

***Securities analysts may not continue coverage on us, or may publish an unfavorable report.***

The trading market for the Series B preferred stock depends, in part, on the research and reports that securities analysts publish about us and our business. We do not have any control over these securities analysts. If one or more of these analysts cease to cover us or fail to publish regular reports on us, we could lose visibility in the financial markets, which could cause the price or trading volume of the Series B preferred stock to decline. If we are the subject of an unfavorable report, the price of the Series B preferred stock may decline.

***The Series B preferred stock is not rated.***

The Series B preferred stock is not rated by any rating agency. Unrated securities usually trade at a discount to similar, rated securities. As a result, there is a risk that the Series B preferred stock may trade at a price that is lower than they might otherwise trade if rated by a rating agency. It is possible, however, that one or more rating agencies might independently determine to assign a rating to the Series B preferred stock. In addition, we may elect to issue other securities for which we may seek to obtain a rating. If any ratings are assigned to the Series B preferred stock 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, could adversely affect the market for or the market value of the Series B preferred stock.



***Our management and board of directors have significant control over our business.***

As of March 27, 2024, our directors, executive officers and affiliates (including partners of Cain Watters) beneficially owned an aggregate of 5,099,935 shares, or approximately 71.17% of our outstanding shares of common stock. Consequently, our management and board of directors may be able to significantly affect our affairs and policies, including the outcome of the election of directors and the potential outcome of other matters submitted to a vote of our shareholders, such as mergers, the sale of substantially all of our assets and other extraordinary corporate matters. This influence may also have the effect of delaying or preventing changes of control or changes in management or limiting the ability of our other shareholders to approve transactions that they may deem to be in the best interests of our Company. The interests of these insiders could conflict with the interests of our other shareholders, including you.

***We are a “controlled company” within the meaning of the rules of NASDAQ, and as such, we qualify for exemptions from certain corporate governance requirements. As a result, you may not have the same protections afforded to shareholders of companies that are subject to such requirements.***

We are a “controlled company” under NASDAQ’s corporate governance listing standards, meaning that more than 50% of the voting power for the election of our board of directors is held by a single person, entity or group. As a controlled company, we are exempt from the obligation to comply with certain corporate governance requirements, including the requirements:

- that a majority of our board of directors consists of “independent directors,” as defined under NASDAQ rules;
- that director nominations are selected, or recommended for the board of directors’ selection, by either (i) the independent directors constituting a majority of the board of directors’ independent directors in a vote in which only independent directors participate, or (ii) a nominating and corporate governance committee that is composed entirely of independent directors; and
- that we have a compensation committee that is composed entirely of independent directors. We intend to avail ourselves of certain of these other exemptions for as long as we remain a “controlled company.” Accordingly, our shareholders may not have the same protections afforded to shareholders of companies that are subject to all of NASDAQ’s corporate governance requirements, which could make our stock less attractive to investors or otherwise harm our stock price.

***We are controlled by the majority shareholders, whose interests may not coincide with yours and with whose decisions you may disagree.***

A. Haag Sherman, George L. Ball, Darrell W. Cain, Steven B. Clapp, Thomas Sanders, Daniel C. Wicker, other members of management and partners of Cain Watters, and certain other existing shareholders (collectively, the “Majority Shareholders”) currently own more than 50% of our outstanding shares of common stock. So long as the Majority Shareholders continue to control more than 50% of our outstanding shares of common stock, they will have the ability, if they vote in the same manner, to determine the outcome of certain matters requiring only common shareholder approval, including the election of directors and certain amendments to our certificate of formation, bylaws and other corporate governance documents. In addition, this concentration of ownership may delay or prevent a change in control of our Company and make some transactions more difficult or impossible without the support of the Majority Shareholders. In any of these matters, the interests of the Majority Shareholders may differ from or conflict with our interests as a company or the interests of other shareholders. Accordingly, the Majority Shareholders could influence us to enter into transactions or agreements that other shareholders would not approve or make decisions with which other shareholders may disagree.

***Our corporate organizational documents and provisions of federal and state law to which we are subject contain certain provisions that could have an anti-takeover effect and may delay, make more difficult or prevent an attempted acquisition that you may favor or an attempted replacement of our board of directors or management.***

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

- subject to the rights of the holders of the Series B preferred stock, empower our board of directors, without shareholder approval, to issue our preferred stock, the terms of which, including voting power, are to be set by our board of directors;
- eliminate cumulative voting in elections of directors;
- subject to certain exceptions, permit our board of directors to alter, amend or repeal our amended and restated bylaws or to adopt new bylaws;

- require shareholders that wish to bring business before annual or special meetings of shareholders, or to nominate candidates for election as directors at our annual meeting of shareholders, to provide timely notice of their intent in writing; and
- enable our board of directors to increase, between annual meetings, the number of persons serving as directors and to fill the vacancies created as a result of the increase by a majority vote of the directors present at a meeting of directors at which there is a quorum.

Banking laws also impose notice, approval, and ongoing regulatory requirements on any shareholder or other party that seeks to acquire direct or indirect “control” of an FDIC-insured depository institution or its holding company. These laws include the BHC Act and the CIBCA. These laws could delay or prevent an acquisition.

Furthermore, our bylaws provide that the state or federal courts located in Dallas County, Texas, the county in which the city of Dallas is located, will be the exclusive forum for: (i) any actual or purported derivative action or proceeding brought on our behalf; (ii) any action asserting a claim of breach of fiduciary duty by any of our current or former directors or officers; (iii) any action asserting a claim against us or our current or former directors or officers arising pursuant to the TBOC, our certificate of formation, or our bylaws; or (iv) any action asserting a claim against us or our current or former officers or directors that is governed by the internal affairs doctrine, in each case subject to said courts having personal jurisdiction over the indispensable parties named as defendants therein. Any person purchasing or otherwise acquiring any interest in any shares of our capital stock will be deemed to have notice of and to have consented to this provision of our certificate of formation. The exclusive forum provision may limit a shareholder’s ability to bring a claim in a judicial forum that it finds favorable for disputes with us or our directors, officers or other employees, which may discourage such lawsuits. Alternatively, if a court were to find the exclusive forum provision to be inapplicable or unenforceable in an action, we may incur additional costs associated with resolving such action in other jurisdictions, which could have a material adverse effect on our business, financial condition, results of operations and growth prospects.

***The obligations associated with being a public company require significant resources and management attention, which increase our costs of operations and may divert focus from our business operations.***

We incur substantial legal, accounting, administrative and other costs and expenses related to operating as a public company, and these costs may be higher when we no longer qualify as an “emerging growth company,” as defined in the Jumpstart Our Business Startups Act (the “JOBS Act”). We are subject to the reporting requirements of the Exchange Act, which requires that we file annual, quarterly and current reports with respect to our business and financial condition and proxy and other information statements, and the rules and regulations implemented by the SEC, the Sarbanes-Oxley Act, the Dodd-Frank Act, the Public Company Accounting Oversight Board (“PCAOB”) and NASDAQ, each of which imposes additional reporting and other obligations on public companies. As a public company, compliance with these reporting requirements and other SEC and NASDAQ rules make certain operating activities more time-consuming, and we also incur significant legal, accounting, insurance and other expenses. Additionally, any failure by us to file our periodic reports with the SEC in a timely manner could, among other things, harm our reputation, cause our investors and potential investors to lose confidence in us, restrict trading in or reduce the market price of the Series B preferred stock, and potentially limit our ability to access the capital markets. Furthermore, the corporate infrastructure demanded of a public company may divert management’s attention from implementing our operating strategy, which could prevent us from successfully implementing our strategic initiatives and improving our results of operations. We incur expenses to maintain our internal control and procedures for financial reporting and accounting systems to meet our reporting obligations as a public company. We cannot predict or estimate the amount of additional costs we may incur in the future in order to continue to comply with these requirements, and these costs may materially increase our general and administrative expenses over time, and such increases would reduce our profitability.

***We are an “emerging growth company,” and the reduced reporting requirements applicable to emerging growth companies may make the Series B preferred stock less attractive to investors.***

We are an “emerging growth company,” as defined in the JOBS Act. For as long as we continue to be an emerging growth company, we may take advantage of reduced regulatory and reporting requirements that are otherwise generally applicable to public companies. These include, without limitation, not being required to comply with the auditor attestation requirements of Section 404(b) of the Sarbanes-Oxley Act, reduced financial reporting requirements, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements and exemptions from the requirements of holding non-binding advisory votes on executive compensation and shareholder approval of any golden parachute payments not previously approved. The JOBS Act also permits an “emerging growth company” such as us to take advantage of an extended transition period to comply with new or revised accounting standards applicable to public companies. We have elected to, and expect to continue to, take advantage of certain of these and other exemptions until we are no longer an emerging growth company. Further, the JOBS Act allows us 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 this Form 10-K.

We may take advantage of these provisions for up to five years from the date of our initial offering date in May 2019, unless we earlier cease to be an emerging growth company, which would occur if our annual gross revenues exceed \$1.07 billion, if we issue more than \$1.0 billion in non-convertible debt in a three-year period or if we become a “large accelerated filer,” in which case we would no longer be an emerging growth company as of the following December 31. We cannot predict if investors find the Series B preferred stock less attractive because we rely on these exemptions, or if we choose to rely on additional exemptions in the future. If some investors find the Series B preferred stock less attractive as a result, there may be a less active trading market for the Series B preferred stock and our share price may be more volatile.

***An investment in the Series B preferred stock is not an insured deposit and is subject to risk of loss.***

The Series B preferred stock is not a savings account, deposit or other obligation of any of our bank or nonbank subsidiaries and is not insured or guaranteed by the FDIC or any other government agency. Your investment is subject to investment risk, and you must be capable of affording the loss of your entire investment.

**Item 1B. Unresolved Staff Comments.**

Not applicable.

**Item 1C. Cybersecurity.**

**Cybersecurity Risk Management**

Cybersecurity is critical to supporting our business and protecting our customers in an increasingly complex environment. We face a variety of cybersecurity threats including attacks that are common to most industries, such as ransomware and denial-of-service, as well as attacks from advanced and highly organized adversaries targeting financial services companies. Our information systems have from time to time experienced such attacks despite our best efforts to prevent them. Our customers, suppliers, and other third parties also face similar cybersecurity threats, and a cybersecurity incident impacting any party could have a material impact on our operations, performance, or operating results. None of these threats or incidents have to date materially affected our business strategy, results of operations, or financial condition. However, we cannot assure that any future security breaches will not occur or that any such events that have occurred or may occur in the future will not result in material harm to our business, operations, reputation or profitability. These threats and related risks highlight the importance of allocating resources to protect the Company and our customers. For more information on how cybersecurity risk may materially affect the Company’s business strategy, results of operations or financial condition, please refer to Item 1A, Risk Factors, of this Form 10-K.

The Company maintains a formal Information Security Program that includes risk assessments regularly conducted by internal resources as well as third-party experts. These assessments are used to evaluate potential security threats that may have a negative impact on the organization, detect potential vulnerabilities and mitigate any identified security risks. Our program leverages industry standards and frameworks and is designed to protect the confidentiality, integrity, and availability of our information assets and systems.

The Information Security Program is led by the Chief Information Security Officer (“CISO”), who reports to the Chief Executive Officer. The CISO has oversight of the Company’s risk management framework, which includes the Information Security Program. The CISO provides program oversight and direction, including adjustments in response to changes in technology, threats, business processes, and regulatory or statutory requirements. The CISO works collaboratively with information technology staff, operational management, counterparts at third-party vendors and functional stakeholders to implement a program designed to protect our information systems from cybersecurity threats and promptly respond to potential cybersecurity incidents. The CISO has over 20 years of experience in the fields of information technology and cybersecurity and maintains multiple professional cybersecurity certifications.

Our Information Security Program consists of several elements including:

- **Incident Monitoring and Response.** We have 24x7 security cybersecurity monitoring, which utilizes both third-party cybersecurity experts and leading tools to monitor activity in our information systems. We also maintain an incident response plan and playbooks that define our response to a cybersecurity incident, including a cross-functional incident response process that includes key stakeholders such as senior leaders and legal, and leverages our technological resources and third-party service providers. Through ongoing communication with these teams, the CISO monitors the prevention, detection, mitigation, and remediation of cybersecurity incidents in real time, and reports such incidents to leadership when appropriate pursuant to internal guidelines governing the reporting of such events.

- *Threat and Vulnerability Management.* We maintain a threat and vulnerability management program that leverages multiple data sources to proactively identify, assess, and mitigate changing cybersecurity risks. This program incorporates vulnerability scanning and threat intelligence capabilities, which are in place to help safeguard information assets. We also share and receive threat intelligence with government agencies, the Financial Services Information Sharing and Analysis Center ("FS-ISAC") and cybersecurity vendors and leaders in the cybersecurity industry.
- *Infrastructure and Data Protection.* We have technical and organizational safeguards that are designed to protect our networks, systems, and data from cybersecurity threats, including: firewalls, intrusion prevention and detection systems, network and endpoint anti-malware protections, and access controls such as privileged access management. Our information security and information technology teams collaborate regularly to assess the security of current and future infrastructure changes.
- *Third-Party Risk Management.* We run a third-party risk management program designed to identify and manage risks, including cybersecurity risks, involving our third-party providers. This includes performing due diligence and assessment of each provider's cybersecurity posture as well as periodic re-assessments.
- *Security Training and Awareness.* We provide ongoing education and training to employees regarding cybersecurity threats and the role they play in helping prevent and detect these threats. This includes regular phishing simulations, with training provided for any failures, as well as periodic communications via the internal company portal concerning threats, best practices, and technology changes to improve security. We also work with the Company marketing department to periodically publish articles on our website to raise security awareness with our customers.

While we maintain teams that specialize in cybersecurity and information technology, we also leverage third-party experts to provide objective feedback on our program and posture. These are accomplished via penetration tests, security posture assessments, and technology consulting. These independent evaluations help validate existing controls, identify potential focus areas, and aid in securely deploying technology in an increasingly complex environment.

Our Information Security Program is evaluated regularly by both the internal audit function as well as third-party audit firms. These audits help ensure our program is appropriate to address the changing threat landscape and aligns to industry standards such as the National Institute of Standards and Technology Cybersecurity Framework, as well as other legal and regulatory guidance including the Federal Financial Institutions Examination Council Cybersecurity Assessment Tool, the Bankers Electronic Crimes Taskforce Ransomware Self-Assessment Tool, and the Gramm-Leach-Bliley Act. Controls are reviewed for adequacy and design at least annually, and both internal and third-party audits aid in identifying areas for continued focus, providing assurance that controls are appropriately designed and operating effectively. Additionally, we meet regularly with examiners from the Office of the Comptroller of the Currency to review our cybersecurity program and discuss the changing threat landscape.

Our cybersecurity personnel maintain current knowledge through training, obtaining professional certifications, and participation in industry groups such as FS-ISAC, American Bankers Association, and the Texas Bankers Association. Company cybersecurity personnel expand and test their knowledge of cyber threats and countermeasures through additional on-the-job training and periodic simulated exercises to practice their response to real-life threats. We maintain a training budget, and personnel are encouraged to obtain formal training and industry-approved certifications as appropriate for their roles and responsibilities.

The Technology Committee of our board of directors is responsible for overseeing our information security and technology programs, including management's actions to identify, assess, mitigate, and remediate or prevent material cybersecurity issues and risks. Our Chief Information Security Officer provides quarterly reports to the Technology Committee of our board of directors regarding the information security program and the technology program, key enterprise cybersecurity initiatives, and other matters relating to cybersecurity processes. The Technology Committee of our board of directors reviews and approves our information security and technology budgets and strategies at least annually. Additionally, the Technology Committee of our board of directors reviews our cyber security risk profile on at least an annual basis.

**Item 2. Properties.**

Our main office is located in a two-story, approximately 33,000 square foot commercial office building located at 16200 Dallas Parkway, Dallas, Texas 75248, which is owned by the Bank. The Bank occupies approximately 36% of the building and leases out the remainder to other tenants.

We also lease space at: (a) 600 Travis, Houston, Texas 77002, comprising 14,402 square feet (expires in April 2026) for offices of Sanders Morris, Tectonic Advisors and HWG, (b) 17 Cowboys Way, Frisco, Texas 75034, comprising 2,141 square feet (expires in January 2034) for offices of Tectonic Advisors and HWG, (c) 5950 Sherry Lane, Suite 470, Dallas, Texas 75225, comprising 2,508 square feet, which lease expires in August 2029 for offices of Sanders Morris's Dallas branch, (d) 8900 Indian Creek Parkway, Overland Park, Kansas 66210, comprising 4,947 square feet, which lease expires in May 2027 for offices of the Bank's Nolan division, and (e) 6300 Ridglea Place, Fort Worth, Texas 76116, comprising 4,139 square feet, which lease expires in January 2027 for offices of the Bank's Integra factoring division. Management believes that the principal terms of the leases are consistent with prevailing market terms and conditions and that these facilities are in good condition and adequate to meet our current needs.

**Item 3. Legal Proceedings.**

We are involved, from time to time, as plaintiff or defendant in various legal actions arising in the normal course of its business. Based on the information presently available, management believes that the ultimate outcome in such proceedings, in the aggregate, will not have a material adverse effect on the business's financial condition or results of operations of the Company on a consolidated basis. However, changes in circumstances or additional information could result in additional accruals or resolution of these matters in excess of established accruals, which could adversely affect our financial condition, results of operations or cash flows, potentially materially.

**Item 4. Mine Safety Disclosures.**

Not applicable.

## PART II

### Item 5. Market for Registrant’s Common Equity and Related Shareholder Matters and Issuer Purchases of Equity Securities.

#### Market Information

There is no established public trading market for our common stock. Our Series B preferred stock is quoted on the NASDAQ Global Market under the symbol “TECTP”.

#### Holders of Record

As of March 27, 2024, we had 100 holders of record of our common stock.

#### Dividends

Although we intend to pay dividends on the Series B preferred stock, dividends on the Series B preferred stock are not cumulative or mandatory. If our board of directors does not declare a dividend on the Series B preferred stock or if our board of directors authorizes and we declare less than a full dividend in respect of any dividend period, the holders of the Series B preferred stock will have no right to receive any dividend or a full dividend and we will have no obligation to pay a dividend or to pay full dividends for that dividend period at any time, whether or not dividends on the Series B preferred stock or any other class or series of our preferred stock or common stock are declared for any future dividend period.

It is the policy of our board of directors to reinvest earnings for such period of time as is necessary to ensure our successful operations. During the year ended 2023, and after declaring and paying dividends on our Series B preferred stock, our board of directors declared and paid certain quarterly dividends on our common stock, which is not registered with the SEC, and does not trade publicly. As a financial holding company, our ability to pay cash dividends is dependent upon the ability of our bank and non-bank subsidiaries to pay cash dividends. Future dividends will depend on our consolidated earnings, capital and regulatory requirements, financial condition, and other factors considered relevant by our board of directors. In addition, we are subject to regulatory restrictions on our payment of dividends. For more information regarding the Company’s ability to pay dividends, please refer to the “*Supervision and Regulation*” section under Item 1 of this Form 10-K.

#### Securities Authorized for Issuance Under Equity Compensation Plans

Information regarding stock-based compensation awards outstanding and available for future grants as of December 31, 2023, segregated between stock-based compensation plans approved by shareholders and stock-based compensation plans not approved by shareholders, is presented in the table below.

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants, and rights (a)	Weighted average exercise price of outstanding options, warrants, and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in (a))
Equity compensation plans approved by security holders:			
2017 Equity Incentive Plan	337,500	\$ 5.51	340,000

### Item 6. [RESERVED]

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

*This management's discussion and analysis of financial condition and results of operations contains forward-looking statements that involve risks and uncertainties. Please see "Cautionary Statement Regarding Forward-Looking Statements" for a discussion of the uncertainties, risks and assumptions associated with these statements. The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and accompanying notes included elsewhere in this Annual Report on Form 10-K. Our actual results could differ significantly from those anticipated in these estimates and in the forward-looking statements as a result of certain factors, including those discussed in the section of this Form 10-K captioned "Risk Factors," and elsewhere in this Form 10-K.*

**Company Overview**

We are a financial holding company headquartered in Dallas, Texas. We provide a wide array of financial products and services including banking, trust, investment advisory, securities brokerage, factoring, third-party administration, qualified plan recordkeeping and insurance services to individuals, small businesses and institutions across the United States.

We operate through four main direct and indirect subsidiaries: (i) T Bancshares, Inc. which was incorporated under the laws of the State of Texas on December 23, 2002 to serve as the bank holding company for the Bank, (ii) Sanders Morris, a registered broker-dealer with FINRA, and registered investment advisor with the SEC, (iii) Tectonic Advisors a registered investment advisor registered with the SEC focused generally on managing money for relatively large, affiliated institutions and investment advisors, as well as for their clients, and (iv) HWG, an insurance agency registered with the TDI.

The Bank offers a broad range of commercial and consumer banking and trust services primarily to small- to medium-sized businesses and their employees, and other institutions. The Bank's traditional fiduciary services clients primarily consist of clients of Cain Watters. The Bank also offers lending services, including commercial loans to small-to medium-sized businesses and professional concerns, as well as consumers, Nolan, operating from its office in Overland Park, Kansas as a division within the Bank, offers third party administration ("TPA") services, and Integra, operating from its Fort Worth, Texas office as a division within the Bank, offers factoring services.

The Bank's technological capabilities, including worldwide free ATM withdrawals, sophisticated on-line banking capabilities, electronic funds transfer capabilities, and economical remote deposit solutions, allow most customers to be served regardless of their geographic location. The Bank serves its local geographic market which includes Dallas, Tarrant, Denton, Collin and Rockwall counties which encompass an area commonly referred to as the Dallas/Fort Worth Metroplex. The Bank also provides focused services to the dental and other health professional industries through a centralized loan and deposit platform that operates out of its main office in Dallas, Texas. In addition, the Bank serves the small business community by offering loans guaranteed by the SBA and the USDA.

Sanders Morris provides brokerage, advisory, and wealth management services to high and ultra-high net worth individuals in a broad geographic area that includes Texas, with a concentration of clients in the Houston, Texas metroplex area, as well as clients across the United States. Tectonic Advisors provides advisory and wealth management services primarily to affiliated institutions and their clients, including the Bank, Cain Watters, and their clients, under long-standing advisory and due diligence agreements.

We have three operating segments: Banking, Other Financial Services and HoldCo. Our banking operating segment encompasses both commercial and consumer banking services, as well as factoring services. Our Other Financial Services segment includes the activities of Tectonic Advisors, Sanders Morris, the Bank's Trust Division, which includes Nolan, and HWG. Our HoldCo operating segment includes the Bank's immediate parent, T Bancshares, and related subordinated debt, as well as operations of the financial holding company that serves as parent for the group overall. See the section entitled Segment Reporting, below, for more information.

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries, T Bancshares, the Bank, Tectonic Advisors, Sanders Morris, and through Sanders Morris, HWG. All intercompany transactions and balances are eliminated in consolidation.



## Critical Accounting Policies and Estimates

We prepare consolidated financial statements based on GAAP and customary practices within the financial services industry. These policies, in certain areas, require management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. While we base estimates on historical experience, current information and other factors deemed to be relevant, actual results could differ from those estimates.

We consider accounting estimates to be critical to reported financial results if (i) the accounting estimate requires management to make assumptions about matters that are highly uncertain at the time we make the accounting estimate and (ii) different estimates that management reasonably could have used for the accounting estimate in the current period, or changes in the accounting estimate that are reasonably likely to occur from period to period, could have a material impact on the financial statements.

As discussed in Note 1 – Summary of Significant Accounting Policies, the Company adopted ASU 2016-13, *Financial Instruments - Credit Losses (Topic 326) (ASC 326): Measurement of Credit Losses on Financial Instruments*, effective on January 1, 2023, pursuant to the delayed adoption allowable for smaller reporting companies, replacing allowance allocations calculated in accordance with ASC Topic 310, *Receivables*, and allowance allocations calculated in accordance with FASB ASC Topic 450, *Contingencies* discussed in the 2022 Form 10-K. Upon adoption of the current expected credit loss (“CECL”) methodology, the Company recorded an increase of \$1.4 million to the allowance for credit losses for loans and \$237,505 to the allowance for credit losses for unfunded commitments. In addition, the Company recognized a cumulative effect reduction to retained earnings totaling \$1.3 million, net of a recorded deferred tax asset of \$341,662. In the case of loans, the allowance for credit losses is a contra-asset valuation account, calculated in accordance with ASC 326, that is deducted from the amortized cost basis of loans to present the net amount expected to be collected. In the case of off-balance-sheet credit exposures, the allowance for credit losses is a liability account, calculated in accordance with ASC 326, reported as a component of other liabilities in our consolidated balance sheets. The amount of each allowance account represents management's best estimate of current expected credit losses on these financial instruments considering available information, from internal and external sources, relevant to assessing exposure to credit loss over the contractual term of the instrument. Relevant available information includes historical credit loss experience, current conditions and reasonable and supportable forecasts. While historical credit loss experience provides the basis for the estimation of expected credit losses, adjustments to historical loss information may be made for differences in current portfolio-specific risk characteristics, environmental conditions or other relevant factors. While management utilizes its best judgment and information available, the ultimate adequacy of our allowance accounts is dependent upon a variety of factors beyond our control, including the performance of our portfolios, the economy, changes in interest rates and the view of the regulatory authorities toward classification of assets. See the section captioned “Allowance for Credit Losses” elsewhere in this discussion as well as Note 1 – Summary of Significant Accounting Policies and Note 3 - Loans and Allowance for Credit Losses for more details on the impact of the Company’s adoption of the CECL methodology, including related accounting policies.

## Performance Summary

Net income available to common shareholders decreased by \$1.8 million, or 11.6%, to \$13.7 million for the year ended December 31, 2023 from \$15.5 million for the year ended December 31, 2022. Earnings per diluted common share were \$1.87 and \$2.11 for the years ended December 31, 2023 and 2022, respectively. The decrease in net income for 2023 over 2022 included a \$120,000 decrease in net interest income, a \$236,000 decrease in non-interest income, a \$2.0 million increase in non-interest expense, and a \$24,000 increase in the provision for credit losses, partly offset by a \$586,000 decrease in income tax expense. Net interest income before provision for credit losses was lower in the current year mainly due to increased funding costs on our deposit products due to federal funds rate increases over the last year offset to a lesser extent by increased earnings on interest earning assets, primarily loans and interest-bearing deposits held at the FRB. For the year ended December 31, 2023, annual return on average assets was 2.38%, compared to 2.89% for the prior year, and annual return on average equity was 15.04%, compared to 18.88% for the prior year.

Our accounting and reporting policies conform to GAAP and the prevailing practices in the banking industry. However, this Form 10-K contains financial information determined by methods other than in accordance with GAAP, which includes return on average tangible common equity. We calculate return on average tangible common equity as net income available to common shareholders (net income less dividends paid on preferred stock) divided by average tangible common equity. The most directly comparable GAAP financial measure for tangible common equity is average total shareholders’ equity. We believe these non-GAAP measures and ratios, when taken together with the corresponding GAAP measures and ratios, provide meaningful supplemental information regarding our performance. We believe investors benefit from referring to these non-GAAP measures and ratios in assessing our operating results and related trends, and when planning and forecasting future periods. However, these non-GAAP measures and ratios should be considered in addition to, and not as a substitute for or preferable to, measures and ratios prepared in accordance with GAAP.

The following table reconciles net income to income available to common shareholders and presents the calculation of return on average tangible common equity:

(In thousands, except percentages)	As of and for the Year Ended December 31, 2023	As of and for the Year Ended December 31, 2022
Income available to common shareholders	\$ 13,667	\$ 15,478
Average shareholders' equity	\$ 101,176	\$ 90,194
Less: average goodwill	21,440	21,440
Less: average core deposit intangible	472	681
Less: average preferred stock	17,250	17,250
Average tangible common equity	<u>\$ 62,014</u>	<u>\$ 50,823</u>
Return on average tangible common equity	22.04%	30.45%

Total assets grew by \$64.8 million, or 10.6%, to \$677.3 million as of December 31, 2023, from \$612.5 million as of December 31, 2022. This increase was primarily due to increases of \$49.0 million in loans held for investment, \$16.6 million in cash and cash equivalents and \$3.9 million in investments, partly offset by a decrease of \$7.3 million in loans held for sale.

Shareholders' equity increased \$10.4 million, or 10.8%, to \$106.9 million as of December 31, 2023, from \$96.5 million as of December 31, 2022. See analysis of shareholders' equity in the section captioned "Capital Resources and Regulatory Capital Requirements" included elsewhere in this discussion.

## Results of Operations

Details of the changes in the various components of net income are discussed below.

### Net Interest Income

Net interest income is the difference between interest income on interest-earning assets, such as loans, investment securities, and interest-bearing cash, and interest expense on interest-bearing liabilities, such as deposits and borrowings. Changes in net interest income result from changes in volume and spread, and are reflected in the net interest margin, as well as changes in average interest rates. Volume refers to the average dollar level of interest-earning assets and interest-bearing liabilities. Spread refers to the difference between the average yield on interest-earning assets and the average rate paid on interest-bearing liabilities. Margin refers to net interest income divided by average interest-earning assets, and is influenced by the level and relative mix of interest-earning assets and interest-bearing liabilities.

The Federal Reserve influences the general market rates of interest, including the deposit and loan rates offered by many financial institutions. Interest rates are highly sensitive to many factors that are beyond the control of the Company, including changes in the expected rate of inflation, the influence of general and local economic conditions and the monetary and fiscal policies of the United States government, its agencies and various other governmental regulatory authorities. As of December 31, 2023, the target range for the federal funds rate was 5.25% to 5.50%.

The following table presents the changes in net interest income and identifies the changes due to differences in the average volume of interest-earning assets and interest-bearing liabilities and the changes due to changes in the average interest rate on those assets and liabilities. The changes in net interest income due to changes in both average volume and average interest rate have been allocated to the average volume change or the average interest rate change in proportion to the absolute amounts of the change in each.

(In thousands)	2023 vs 2022		
	Increase (Decrease) Due to Change in		
	Rate	Average Volume	Total
Interest-bearing deposits and federal funds sold	\$ 1,256	\$ 895	\$ 2,151
Securities	27	177	204
Loans, net of unearned discount <sup>(1)</sup>	7,978	2,749	10,727
Total earning assets	9,261	3,821	13,082
Savings and interest-bearing demand	27	(20)	7
Money market deposit accounts	4,398	116	4,514
Time deposits	5,803	2,485	8,288
FHLB and other borrowings	423	(315)	108
Subordinated notes	285	-	285
Total interest-bearing liabilities	10,936	2,266	13,202
Changes in net interest income	\$ (1,675)	\$ 1,555	\$ (120)

(1) Include non-accrual loans.

Net interest income decreased \$120,000, or 0.4% from \$27.5 million for the year ended December 31, 2022, to \$27.4 million for year ended December 31, 2023. Net interest margin for the year ended December 31, 2023 and 2022 was 4.58% and 5.06%, respectively, a decrease of 48 basis points. The decrease in net interest income was primarily due to an increase in the average interest rate paid on interest-bearing liabilities as a result of the continued interest rate increases, and increases in the average volume of time deposits, partly offset by an increase in the average yield and average volume of loans and interest-bearing deposits (primarily amounts held in an interest-bearing account at the FRB), and to a lesser extent an increase in the average volume of securities.

The average volume of interest-earning assets increased \$54.5 million, or 10.0%, from \$542.6 million for the year ended December 31, 2022, to \$597.1 million for the year ended December 31, 2023. The increase during 2023 included a \$32.5 million, or 7.1%, increase in the average volume of loans, a \$17.7 million, or 47.9%, increase in average volume interest-bearing deposits (primarily amounts held in an interest-bearing account at the Federal Reserve), and a \$4.3 million, or 9.2%, increase in the average volume of securities.

The average yield on interest-earning assets increased 163 basis points from 6.15% for the year ended December 31, 2022, to 7.78% for the year ended December 31, 2023, due to the increasing rate environment, and changes in the mix of interest-earning assets. The average yield for loans increased 174 basis points from 6.73% for the year ended December 31, 2022, to 8.47% for the year ended December 31, 2023. The average yield on interest-bearing deposits increased 339 basis points from 1.66% for the year ended December 31, 2022, to 5.05% for the year ended December 31, 2023. The average yield on securities increased 6 basis points from 4.05% for the year ended December 31, 2022, to 4.11% for the year ended December 31, 2023.

The average volume of interest-bearing liabilities increased \$51.8 million, or 13.5%, from \$383.2 million for the year ended December 31, 2022, to \$435.0 million for the year ended December 31, 2023. The increase during 2023 included a \$57.6 million, or 15.9%, increase in average volume of interest-bearing deposits, partly offset by a \$5.8 million, or 66.2%, decrease in average volume of FHLB and other borrowings. The average interest rate paid on interest-bearing liabilities increased 285 basis points from 1.54% for the year ended December 31, 2022, to 4.39% for the year ended December 31, 2023. The average interest rate paid on interest-bearing deposits increased 287 basis points from 1.36% for the year ended December 31, 2022, to 4.23% for the year ended December 31, 2023. The average cost of FHLB and other borrowings increased 485 basis points from 0.61% for the year ended December 31, 2022, to 5.46% for the year ended December 31, 2023, and the average cost of subordinated notes increased 238 basis points from 7.59% for the year ended December 31, 2022, to 9.97% for the year ended December 31, 2023, due to the aforementioned significant increases in the market interest rates.

The following table sets forth our average balances of assets, liabilities and shareholders' equity, in addition to the major components of net interest income and our net interest margin, for the years ended December 31, 2023 and 2022.

(In thousands, except percentages)	Year Ended December 31,					
	2023			2022		
	Average Balance	Interest	Average Yield	Average Balance	Interest	Average Yield
<b>Assets</b>						
Interest-bearing deposits and federal funds sold	\$ 54,770	\$ 2,764	5.05%	\$ 37,032	\$ 613	1.66%
Securities	50,874	2,091	4.11	46,576	1,887	4.05
Loans, net of unearned discount (1)	491,448	41,612	8.47	458,980	30,885	6.73
Total earning assets	597,092	46,467	7.78	542,588	33,385	6.15
Cash and other assets	48,320			49,995		
Allowance for credit losses	(5,743)			(4,192)		
Total assets	\$ 639,669			\$ 588,391		
<b>Liabilities and Shareholders' Equity</b>						
Savings and interest-bearing demand	\$ 12,041	56	0.47%	\$ 16,287	49	0.30%
Money market deposit accounts	132,471	6,153	4.64	129,972	1,639	1.26
Time deposits	275,540	11,540	4.19	216,196	3,252	1.50
Total interest-bearing deposits	420,052	17,749	4.23	362,455	4,940	1.36
FHLB and other borrowings	2,951	161	5.46	8,730	53	0.61
Subordinated notes	12,000	1,196	9.97	12,000	911	7.59
Total interest-bearing liabilities	435,003	19,106	4.39	383,185	5,904	1.54
Non-interest-bearing deposits	92,230			104,170		
Other liabilities	11,260			10,842		
Total liabilities	538,493			498,197		
Shareholders' equity	101,176			90,194		
Total liabilities and shareholders' equity	\$ 639,669			\$ 588,391		
Net interest income		\$ 27,361			\$ 27,481	
Net interest spread			3.39%			4.61%
Net interest margin			4.58%			5.06%

(1) Includes non-accrual loans.

### Provision for Credit Losses

As discussed in Note 1 – Summary of Significant Accounting Policies in the accompanying notes to consolidated financial statements, the Company adopted the CECL accounting standard effective on January 1, 2023. The measurement of expected credit losses under the CECL methodology is applicable to financial assets measured at amortized cost, including loans and held-to-maturity debt securities, as well as off-balance sheet credit exposures. Provision for credit losses is determined by management as the amount to be added to the allowance for credit loss accounts for various types of financial instruments to bring the allowance to a level deemed appropriate by management to absorb expected credit losses over the lives of the respective financial instruments. Management actively monitors the Company's asset quality and provides appropriate provisions based on such factors as historical loss experience, current conditions and reasonable and supportable forecasts.

Financial instruments are charged-off against the allowance for credit losses when appropriate. Although management believes it uses the best information available to make determinations with respect to the provision for credit losses, forecasted economic conditions continue to remain uncertain due to the rising interest rate environment and persistent high inflation levels in the United States. Accordingly, future adjustments may be necessary if economic conditions differ from the assumptions used in making the determination.

The following table presents the components of provision for credit losses:

(In thousands)	Year Ended December 31,	
	2023	2022
Provision for credit losses related to:		
Loans	\$ 1,333	\$ 1,264
Held to maturity securities	-	-
Off-balance sheet credit exposures	(45)	-
Total	\$ 1,288	\$ 1,264

Provision expense for loans is generally reflective of change in loan volume and mix as well as charge-offs or specific reserves taken during the respective period. Provision expense is also impacted by the economic outlook and changes in macroeconomic variables. The provision expense recorded for the year ended December 31, 2023 and 2022 driven by the loss rate and charge-offs. See “Allowance for Credit Losses” elsewhere in this discussion for further analysis of our provision for credit losses related to loans.

Changes in the allowance for off-balance sheet credit exposures are generally driven by the remaining unfunded loan commitments expected to fund loans and to changes in the assumptions to project loss rates. The credit provision for the year ended December 31, 2023 was due to decreased outstanding loan commitments to fund.

## Non-Interest Income

The components of non-interest income were as follows:

(In thousands)	Year Ended December 31,	
	2023	2022
Trust income	\$ 6,442	\$ 6,098
Gain on sale of loans	581	-
Advisory income	14,910	13,549
Brokerage income	7,527	11,754
Service fees and other income	10,037	8,293
Rental income	307	346
Total	<u>\$ 39,804</u>	<u>\$ 40,040</u>

Total non-interest income for the year ended December 31, 2023, decreased \$236,000, or 0.6%, as compared to the year ended December 31, 2022. Changes in the various components of non-interest income are discussed below.

*Trust Income.* Trust income is earned from trust services provided by the Bank on the value of managed and non-managed assets held in custody. Changes in asset values and the volatility of the bond and equity markets impact the market value of trust assets and the related fees. Trust income for the year ended December 31, 2023, increased \$344,000, or 5.6%, compared to the year ended December 31, 2022. The fee income increased between the two years due to an increase in the average market value of the trust assets over the year ended December 31, 2023, from an increase in asset values of \$326.2 million between the two periods from net asset inflows to the Bank’s Trust Division of \$71.8 million and asset appreciation of \$254.4 million.

*Gain on sale of loans.* The gain on sale of loans primarily reflects the gain from the sale of the guaranteed portion of SBA 7(a) and USDA loans originated by the Bank’s SBA lending group. Gain on sale of loans increased \$581,000 during the year ended December 31, 2023, during which there was a gain on sale of loans resulting from the sale of \$5.8 million of USDA loans.

*Advisory income.* Advisory fees are typically based on a percentage of the underlying average asset value for a given period, where each percentage point represents 100 basis points. These revenues are of a recurring nature but are directly affected by increases and decreases in the values of the underlying assets. In addition to fees based on a percentage of underlying assets, payments under certain advisory agreements at Sanders Morris are based on the performance of the respective account, measured as a percentage of the increase achieved in the asset values in the respective account. Performance-based fees, though the agreements may remain in place from year to year, are far less predictable, given the uncertainty of the ability to achieve an increase of the same level as in prior periods, or at all. For the year ended December 31, 2023, advisory income increased \$1.4 million, or 10%, compared to the year ended December 31, 2022. This increase during the year ended December 31, 2023, was primarily due an increase in advisory fees based on a percentage of the underlying assets at Tectonic Advisors totaling \$1.1 million and an increase in advisory fees based on a percentage of underlying assets at Sanders Morris totaling \$261,000.

*Brokerage income.* Brokerage revenues are generally based on a per share fee or commission to trade a share of a particular stock, bond or other security. In addition, brokerage revenues in this context include private placements, participation in syndication of public offerings, and certain other brokerage revenues, including interest earned on margin lending. Brokerage revenue is dependent on the volume of trading, cash held in brokerage accounts which funds margin lending, and on private placement and syndication activity during the period. Brokerage income for the year ended December 31, 2023, decreased \$4.2 million, or 36.0%, compared to the year ended December 31, 2022. This decrease is primarily due to a decrease in private placement activity of \$3.1 million, offset by a slight increase in syndicate deals of \$292,000, and a decline in traditional brokerage activity of \$1.6 million. In addition, revenue from margin lending declined \$468,000 and insurance commissions fell by \$104,000. These decreases were offset by an increase in federated rebates of \$819,000.

The table below reflects a rollforward of our client assets, which includes both advisory and brokerage assets, as of December 31, 2023 and 2022, and the inflows and outflows and market appreciation during the years then ended. Our brokerage and advisory assets experienced an increase of approximately \$1.7 billion, or 33.5%, and an increase of \$409.8 million, or 7.3%, during the years ended December 31, 2023 and 2022, respectively. The increase for the year ended December 31, 2023 was related to market appreciation of \$821 million, or 15.8%, and positive net flows of \$869 million, or 16.7%.

(In thousands)	Tectonic Advisors	Sanders Morris	Total
<b>As of January 1, 2022</b>	<b>\$ 2,852,980</b>	<b>\$ 2,756,332</b>	<b>\$ 5,609,312</b>
Client inflows	857,461	1,545,368	2,402,829
Client outflows	(492,064)	(1,350,240)	(1,842,304)
Net flows	365,397	195,128	560,525
Market appreciation/(depreciation)	(494,912)	(475,454)	(970,366)
<b>As of December 31, 2022</b>	<b>2,723,465</b>	<b>\$ 2,476,006</b>	<b>\$ 5,199,471</b>
Client inflows	956,123	1,459,223	2,415,346
Client outflows	(477,325)	(1,068,957)	(1,546,282)
Net flows	478,798	390,266	869,064
Market appreciation	446,142	375,015	821,157
<b>As of December 31, 2023</b>	<b>\$ 3,648,405</b>	<b>\$ 3,241,287</b>	<b>\$ 6,889,692</b>

*Service fees and other income.* Service fees include fees for deposit-related services and third-party administrative fees from the Bank's Nolan division. Service fees and other income for the year ended December 31, 2023, increased \$1.7 million, or 21.0%, compared to the year ended December 31, 2022. The increase was primarily the result of increases in pension administration fees of \$1.4 million and an increase in other income from the recovery of unclaimed funds at Sanders Morris of \$264,000, and other material fluctuations netting to an increase of \$59,000. The increases in pension administration fees are the result of increases in plans administration clients in 2023 and an increase in fees related to plan terminations, for which two years of administration must be prepared. In addition, loan service fees increased \$165,000 and bank service fees increased \$121,000. These increases were offset by a loss on the disposition of not readily marketable securities of \$100,000 in our HoldCo segment, and by an allowance of \$217,000 related to not readily marketable securities in our Other Financial Services segment.

*Rental income.* The Company receives monthly rental income from tenants leasing space in the bank building. Rental income for the year ended December 31, 2023, decreased \$39,000, or 11.3%, compared to the year ended December 31, 2022, due to a decrease in occupancy in 2023 compared to 2022.

#### Non-Interest Expense

The components of non-interest expense were as follows:

(In thousands)	Year Ended December 31,	
	2023	2022
Salaries and employee benefits	\$ 31,288	\$ 31,093
Occupancy and equipment	1,984	1,707
Trust expenses	2,265	2,243
Brokerage and advisory direct costs	1,936	2,015
Professional fees	1,813	1,480
Data processing	941	794
Other expense	6,594	5,473
Total	<u>\$ 46,821</u>	<u>\$ 44,805</u>

Total non-interest expense for the year ended December 31, 2023, increased \$2.0 million, or 4.5%, compared to the year ended December 31, 2022. Changes in the various components of non-interest income are discussed below.

*Salaries and employee benefits.* Salaries and employee benefits include employee salaries and related payroll expense, incentive compensation, health insurance, benefit plans and payroll taxes. Salaries and employee benefits for the year ended December 31, 2023, increased \$195,000, or 0.6%, compared to the year ended December 31, 2022. In our Other Financial Services segment, salaries and employee benefits decreased \$2.2 million. The decrease was primarily from a decrease in incentive bonuses at Sanders Morris related to decreases in traditional brokerage, private placement, and syndicated offerings activity of \$2.4 million, offset by an increase in commission salaries of \$64,000, and an increase in salaries, payroll taxes, and other benefits of \$196,000. Salaries, bonuses and payroll taxes at Tectonic Advisors decreased \$614,000, due to the move of the technology and accounting staff to the HoldCo segment, where salaries, bonuses and payroll taxes increased \$1.4 million. Salaries, bonuses and payroll taxes at the Bank's Nolan division increased \$347,000 related to staff increases and overtime pay to accommodate the increase in the number of plans administered and merit increases. Salaries, taxes and other benefits in our trust group within our Other Financial Services segment increased \$222,000 related to staffing additions to accommodate additional recordkeeping clients and duplication of personnel during staff changes as well as retention bonuses. Salaries and employee benefits in our Banking segment increased \$947,000, primarily driven by increases in staff and merit increases of \$1.6 million, \$571,000 of which was within the Bank's Integra division. These increases were partially offset by a decrease in bonuses of \$697,000, which decrease was primarily related to a decrease in lending activity in the Bank's SBA team.

*Occupancy and equipment expense.* Occupancy and equipment expenses include building, furniture, fixtures and equipment depreciation and maintenance costs. Occupancy and equipment expenses for the year ended December 31, 2023, increased \$277,000, or 16.2%, compared to the year ended December 31, 2022. The increase is primarily due to an increase in occupancy and equipment expense in our Other Financial Services and HoldCo segments of \$222,000 led by an increase in rent of \$219,000 from Sanders Morris' and Tectonic Advisors' new lease agreements. Occupancy and equipment expense in our Banking segment increased \$55,000, primarily from an increase of \$43,000 in facilities expense at the bank facility, offset by a decrease in rent expense of \$14,000 at Integra. Depreciation expense increased \$19,000, due to increases in furniture, fixtures and equipment and building improvements across all segments. The remaining variances in our occupancy and equipment expense were individually immaterial.

*Trust expenses.* Trust expenses are incurred in our Other Financial Services segment, and include advisory fees paid on the common trust funds managed by the Company based on the value of the assets held in custody. Changes in asset values and the volatility of the bond and equity markets impacts the market value of trust assets and the related expenses. The monthly advisory fees are assessed based on the market value of assets at month-end. Trust expenses for the year ended December 31, 2023, increased by \$22,000, or 1.0%, compared to the year ended December 31, 2022, based on increases in asset values of the Bank's common trust funds.

*Brokerage and advisory direct costs.* Brokerage and advisory direct costs for the year ended December 31, 2023, decreased \$79,000, or 3.9%, compared to the year ended December 31, 2022. Brokerage and advisory direct costs are incurred primarily in our Other Financial Services segment and include the cost of clearing firm services and fees on advisory assets from custodians and certain referral fees, as well as information services related to our advisory and trading activity. The decrease is primarily due to a decrease in brokerage and advisory direct costs at Sanders Morris and HWG of \$73,000, related to a decrease in exchange clearing fees, advisory clearing fees and referral fees of \$177,000, offset by an increase in clearing firm service fees, execution charges, information services and service fees of \$104,000. Tectonic Advisors' brokerage and advisory direct costs decreased \$7,000, due to decreases in service and referral fees of \$14,000, offset by an increase in information services of \$7,000.

*Professional fees.* Professional fees, which include legal, consulting, audit and tax fees, for the year ended December 31, 2023, increased \$333,000, or 22.5%, compared to the year ended December 31, 2022. The increase was the result of increases in our HoldCo segment of \$210,000, primarily due to professional consulting fees for projects involving robotic process automation, and increases in professional fees in our Banking segment of \$152,000, primarily related to collections efforts on past due loans and various other matters, including our regulatory filings. These increases were offset by a decrease in our Other Financial Services segment of \$29,000, due to a decrease in professional fees at Sanders Morris, and in consulting, actuarial, and auditing fees at the Bank's Nolan division and other individually immaterial fluctuations elsewhere in this segment.

*Data processing.* Data processing includes costs related to the Company's operating systems. Data processing expenses for the year ended December 31, 2023, increased \$147,000, or 18.5%, compared to the year ended December 31, 2022. The increase was due to increases in data processing expenses within the Banking segment of \$125,000 and an increase of \$22,000 in our Other Financial Services segment. The increase in our Banking segment was related to discounts the Bank was receiving from the core system vendor from the conversion in 2021 that were exhausted during 2023, along with general increases in other data processing services. The increase in our Other Financial Services segment was related to an increase in costs at the Bank's Trust Division of \$18,000 and immaterial increases at the Bank's Nolan division.



*Other expense.* Other expenses include costs for insurance, FDIC and OCC assessments, director fees, and regulatory filing fees related to our brokerage business, business travel, management fees, and other operational expenses. Other expenses for the year ended December 31, 2023, increased \$1.1 million, or 20.5%, compared to the year ended December 31, 2022. The increase includes increases in software costs and licensing of \$518,000 primarily at our Banking and HoldCo segments, increases in employee recruitment of \$371,000, which were primarily at our Banking segment, where costs increased by \$326,000 related to hiring of additional business development officers in the Bank's SBA and Integra divisions, increases in loan and other real estate operating costs at the Bank of \$133,000, advertising and marketing expense across all segments of the Company of \$46,000, and other individually immaterial increases. These increases were offset by decreases in office expense of \$142,000, primarily in our Other Financial Services segment, related to the reversal of an accrual recorded during the year ended December 31, 2022, related to one of our syndicated offerings undertaken of \$61,000, along with decreases in our technology costs for e-signature services, a decrease in client entertainment, travel, and other client related expenses of \$69,000, and other individually immaterial decreases.

## Income Taxes

Income tax expense was \$3.8 million, for an effective tax rate of 20.1%, for the year ended December 31, 2023, compared to \$4.4 million, for an effective tax rate of 20.6%, for the year ended December 31, 2022. The effective income tax rates differed from the U.S. statutory federal income tax rate of 21% during 2023 and 2022 primarily due to the effect of the income tax effects associated with stock-based compensation, among other things, and their relative proportion to total pre-tax net income.

## Segment Reporting

We have three operating segments: Banking, Other Financial Services and HoldCo. Our primary operating segments are Banking and Other Financial Services.

Our Banking operating segment includes both commercial and consumer banking services, which includes Integra. Commercial banking services are provided primarily to small- to medium-sized businesses and their employees, which includes a wide array of lending and cash management products. Consumer banking services include lending and depository services.

Our Other Financial Services segment includes Tectonic Advisors, Sanders Morris, the Bank's Trust Division, which includes a TPA services unit, and HWG. Through these business divisions, we offer investment advisory and brokerage services to individuals and businesses, private trust services, and financial management services, including personal wealth management, retirement plan design and administrative services, and insurance brokerage services.

A third operating segment, HoldCo, includes the Bank's immediate parent and related subordinated debt, as well as operations of the financial holding company that serves as parent for the group overall. Our principal source of revenue is dividends from our subsidiaries.

The following table presents key metrics related to our segments:

	Year Ended December 31, 2023			
	Banking	Other Financial Services	HoldCo	Consolidated
(In thousands)				
Revenue(1)	\$ 30,608	\$ 37,854	\$ (1,297)	\$ 67,165
Net income (loss) before taxes	\$ 11,920	\$ 12,273	\$ (5,137)	\$ 19,056
	Year Ended December 31, 2022			
	Banking	Other Financial Services	HoldCo	Consolidated
(In thousands)				
Revenue(1)	\$ 29,630	\$ 38,788	\$ (897)	\$ 67,521
Net income (loss) before taxes	\$ 13,106	\$ 11,164	\$ (2,818)	\$ 21,452

(1) Net interest income plus non-interest income

## *Banking*

Income before taxes for the year ended December 31, 2023, decreased \$1.2 million, or 9.0%, compared to the year ended December 31, 2022. The decrease was primarily the result of a \$2.1 million increase in non-interest expense and a \$24,000 increase in the provision for credit losses, partly offset by a \$166,000 increase in net interest income and an \$812,000 increase in non-interest income.

Net interest income for the year ended December 31, 2023, increased \$166,000, or 0.6%, compared to the year ended December 31, 2022. The increase in net interest income was primarily due to an increase in the average yield and average volume on total earning assets, partly offset by an increase in the average rate paid on interest-bearing deposit accounts and an increase in the average volume of deposits. The average yield on interest earning assets and average rate paid on deposits were impacted by changes in market interest rates and changes in the mix of interest-earning assets. See the analysis of net interest income included in the section captioned “Net Interest Income” included elsewhere in this discussion.

The provision for credit losses for the year ended December 31, 2023, increased \$24,000, or 1.9%, compared to the year ended December 31, 2022. See “Provision for Credit Losses” and “Allowance for Credit Losses” included elsewhere in this discussion for further analysis of credit loss provision related to loans and off-balance sheet commitments.

Non-interest income for the year ended December 31, 2023, increased \$812,000, or 65.6%, compared to the year ended December 31, 2022. The increase was primarily due to a \$581,000 gain on sale of a USDA loan during 2023, \$165,000 increase for loan servicing fees, and a \$121,000 increase in deposit service fees and other, partly offset by a \$39,000 decrease in rental income due to abatements given to tenants during the first two quarters of 2023 and a \$16,000 decrease in other miscellaneous income. See the analysis of non-interest income included in the section captioned “Non-Interest Income” included elsewhere in this discussion.

Non-interest expense for the year ended December 31, 2023, increased \$2.1 million, or 14.0%, compared to the year ended December 31, 2022. Salaries and employee benefits increased \$947,000 including \$1.6 million for annual merit increases and increases in staff, partly offset by a \$697,000 decrease in incentive bonuses. Other increases include a \$55,000 increase in occupancy and equipment expense for increase in facilities repairs and maintenance, a \$152,000 increase in professional fees, including \$89,000 for legal fees related to increases in loan collections and various other matters, and \$88,000 for audit fees, partly offset by \$26,000 decrease in consulting fees, a \$125,000 increase in data processing primarily as a result of discounts provided by the Bank’s core system vendor, related to the change in core system in March 2021, ending during 2023, and an \$861,000 increase in other expenses which included increases of \$314,000 for software development primarily in our lending and Integra divisions, \$326,000 for employee recruitment fees primarily attributable to our lending and Integra divisions, and \$122,000 for FDIC insurance premiums related to increase in the base rate during the second quarter of 2023, and \$42,000 for loan related costs, and other various fluctuations which net increased other expenses by \$57,000 for the year ended December 31, 2023. See the analysis of non-interest expense included in the section captioned “Non-Interest Expense” included elsewhere in this discussion.

## *Other Financial Services*

Income before taxes for the year ended December 31, 2023, increased \$1.1 million, or 9.9%, compared to the year ended December 31, 2022. The increase was primarily the result of a \$934,000 decrease in non-interest income which was offset by a \$2.0 million decrease in non-interest expense.

Non-interest income for the year ended December 31, 2023 decreased \$934,000, or 2.4%, compared to the year ended December 31, 2022. The decrease was due to a decrease in brokerage income of \$4.2 million, primarily due to a decrease in private placement and syndicated offering activity of \$2.8 million and a decline in traditional brokerage activity of \$1.6 million. Revenue from margin lending declined \$468,000 and insurance commissions fell by \$104,000. These decreases were offset by an increase in federated rebates of \$819,000. The decrease in brokerage income was partially offset by increases in trust and advisory income of \$1.7 million from net inflows and appreciation, and an increase in service fees and other income of \$1.6 million, primarily from increased plan administration revenue at the Bank’s Nolan division. See the analysis of non-interest income included in the section captioned “Non-Interest Income” above in this discussion.

Non-interest expense for the year ended December 31, 2023, decreased \$2.0 million, or 7.4%, compared to the year ended December 31, 2022. The decrease was primarily from a decrease in salaries and employee benefits of \$2.2 million. In addition, brokerage and advisory direct costs decreased \$79,000, and professional fees decreased \$29,000. These decreases were offset by increases in occupancy and equipment costs of \$143,000, other operating expenses of \$75,000, trust expense of \$22,000, and data processing expense of \$22,000. The decrease in salaries and employee benefits expense was primarily from a decrease in incentive and earnout bonuses at Sanders Morris related to traditional brokerage, private placement, and syndicated offerings activity of \$2.1 million. Salaries and benefits expense at Tectonic Advisors fell by \$614,000 related to the movement of technology and accounting personnel to our HoldCo division. The decrease at Tectonic Advisors was offset by increases at the Bank's Trust Division in the amount of \$222,000 related to staffing additions to accommodate additional recordkeeping clients and duplication of personnel during staff changes and at the Bank's Nolan division of \$347,000 related to staff increases and overtime pay to accommodate the increase in the number of plans administered and merit increases.

The decrease in brokerage and advisory direct costs related to decreases at Sanders Morris and HWG of \$73,000, related to a decrease in exchange clearing fees, advisory clearing fees and referral fees of \$177,000, offset by an increase in clearing firm service fees, execution charges, information services and service fees of \$104,000. The decrease in professional services related primarily to a decrease in professional fees at Sanders Morris and the Nolan division, offset by increases in professional fees at Tectonic Advisors related to technology consulting costs.

The offsetting increases within the segment's non-interest expense, which were primarily in occupancy and equipment costs, included \$110,000 related to leases renewed at Sanders Morris for both the Houston and Dallas, Texas offices and increases in parking costs at these offices, and \$33,000 related to Tectonic Advisors' new office space in Frisco, Texas and related buildout costs. The increase in other operating costs was primarily related to an increase in employee recruitment costs, software licensing costs and advertising and marketing expense across our advisory, brokerage, and third party administration businesses totaling \$263,000, which were offset by decreases in office expense of \$146,000, and decreases in travel, entertainment, and other client promotional costs of \$92,000, and other individually immaterial fluctuations. The increase in trust expense of \$22,000 related to fluctuations in asset values during the year ended December 31, 2023, and the increase in data processing expense was due to an increase in costs at the Bank's Trust Division of \$18,000 and immaterial increases at the Bank's Nolan division. See also the analysis of non-interest expense included in the section captioned "Non-Interest Expense" included elsewhere in this discussion.

#### *HoldCo*

The net loss before taxes at the HoldCo operating segment increased by \$2.3 million, or 82.3%, during the year ended December 31, 2023, compared to the year ended December 31, 2022. Non-interest income decreased \$114,000 which was primarily due to a loss on the disposition of not readily marketable securities of \$100,000. Non-interest expense increased \$2.0 million, which included an increase in salaries and employee benefits of \$1.4 million, primarily related to the movement of accounting and technology staff from Tectonic Advisors to Tectonic Financial, Inc., to allow for more accurate allocation of costs given that these personnel frequently work on matters across the business. In addition, professional fees increased \$210,000 related primarily to website development of \$75,000, and technology and software costs related to the work done by our technology team, particularly consulting around process automation, which is now reported within our HoldCo segment. Other expense increased \$185,000, primarily from increases in software licenses of \$153,000 related to the work done within our technology team, and occupancy and equipment costs increased \$79,000, related to lease renewals in our Houston office, where our technology and certain management personnel office, and the new Frisco office, where our accounting staff primarily office., See also the analysis of non-interest expense included in the section captioned "Non-Interest Expense" included elsewhere in this discussion.

#### **Financial Condition**

##### *Investment Securities*

The primary purpose of the Company's investment portfolio is to provide a source of earnings for liquidity management purposes, to provide collateral to pledge against borrowings, and to control interest rate risk. In managing the portfolio, the Company seeks to attain the objectives of safety of principal, liquidity, diversification, and maximized return on investment. Securities are classified as available for sale when we intend to hold for an indefinite period of time but might be sold before maturity. Securities available for sale are carried at fair value, with unrealized holding gains and losses reported as a separate component of stockholders' equity as other comprehensive income (loss), net of tax. Securities are classified as held to maturity and carried at amortized cost when management has the positive intent and ability to hold them to maturity.

As of December 31, 2023 and 2022, securities available for sale consisted of U.S. Treasuries, U.S. government agency securities and mortgage-backed securities guaranteed by U.S. government agencies. Securities held to maturity consist of PACE and PID/TIRZ investments. These investment contracts or bonds located in Texas, California and Florida, originate under a contractual obligation between the property owners, the local county or city administration, and a TPA and sponsor. PACE assessments are created to fund the purchase and installation of energy saving improvements to the property such as solar panels. PID/TIRZ assessments are used to pay for the development costs of a residential subdivision. Generally, as a property assessment, the total assessment is repaid in installments over a period of 5 to 32 years by the then current property owner(s). Each installment is collected by the County or City Tax Collector where the property is located. The assessments are an obligation of the property.

Restricted securities consisted of FRB stock, having an amortized cost and fair value of \$2.2 million as of December 31, 2023 and 2022, and FHLB stock, having an amortized cost and fair value of \$2.0 million and \$1.3 million as of December 31, 2023 and 2022, respectively.

Securities not readily marketable consists of an income interest in a private investment. The private investment was dissolved during the last quarter of 2023 and the Company held no income interest as of December 31, 2023. For the year ended December 31, 2023, the Company recorded a \$100,000 loss on the sale of securities not readily marketable.

The following presents the amortized cost and fair values of the securities portfolio as of the dates indicated:

	As of December 31, 2023		As of December 31, 2022	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
<b>(In thousands)</b>				
<b>Securities available for sale:</b>				
U.S. Treasuries	\$ 3,906	\$ 3,894	\$ 1,990	\$ 1,953
U.S. government agencies	15,644	13,627	15,715	13,088
Mortgage-backed securities	5,731	5,456	5,925	5,592
Total securities available for sale	<u>\$ 25,281</u>	<u>\$ 22,977</u>	<u>\$ 23,630</u>	<u>\$ 20,633</u>
<b>Securities held to maturity:</b>				
Property assessed clean energy	\$ 1,326	\$ 1,254	\$ 1,596	\$ 1,722
Public improvement district/TIRZ	22,868	22,595	23,666	24,760
Total securities held to maturity	<u>\$ 24,194</u>	<u>\$ 23,849</u>	<u>\$ 25,262</u>	<u>\$ 26,482</u>
<b>Securities, restricted:</b>				
Other	<u>\$ 4,176</u>	<u>\$ 4,176</u>	<u>\$ 3,496</u>	<u>\$ 3,496</u>
<b>Securities not readily marketable</b>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 100</u>	<u>\$ 100</u>

The following table summarizes the maturity distribution schedule with corresponding weighted-average yields of securities available for sale and securities held to maturity as of December 31, 2023. Yields are calculated based on amortized cost. Mortgage-backed securities are included in maturity categories based on their stated maturity date. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations. Other securities classified as restricted include stock in the FRB and the FHLB, which have no maturity date. These securities have been included in the total column only and are not included in the total yield.

(In thousands, except percentages)	Maturing									
	One Year or Less		After One Year Through Five Years		After Five Years Through Ten Years		After Ten Years		Total	
	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
<b>Securities available for sale:</b>										
U.S. Treasuries	\$ 3,906	4.02%	\$ -	-%	\$ -	-%	\$ -	-%	\$ 3,906	4.02%
U.S. government agencies	-	-	11,997	0.95	86	3.62	3,561	0.84	15,644	0.93
Mortgage-backed securities	15	4.08	2,497	3.75	1,224	2.68	1,995	3.65	5,731	3.48
<b>Total</b>	<b>\$ 3,921</b>	<b>4.02%</b>	<b>\$ 14,494</b>	<b>1.43%</b>	<b>\$ 1,310</b>	<b>2.74%</b>	<b>\$ 5,556</b>	<b>1.84%</b>	<b>\$ 25,281</b>	<b>1.99%</b>
<b>Securities held to maturity:</b>										
PACE	\$ -	-%	\$ -	-%	\$ 366	6.87%	\$ 960	7.24%	\$ 1,326	7.14%
PID/TIRZ	-	-	1,432	4.12	-	-	21,436	6.27	22,868	6.13
<b>Total</b>	<b>\$ -</b>	<b>-%</b>	<b>\$ 1,432</b>	<b>4.12%</b>	<b>\$ 366</b>	<b>6.87%</b>	<b>\$ 22,396</b>	<b>6.31%</b>	<b>\$ 24,194</b>	<b>6.19%</b>
<b>Securities, restricted:</b>										
Other	\$ -	-%	\$ -	-%	\$ -	-%	\$ -	-%	\$ 4,176	-%

### Loan Portfolio Composition

Total loans excluding allowance for credit losses, increased \$50.8 million, or 11.3%, to \$501.1 million at December 31, 2023, compared to \$450.3 million at December 31, 2022. The increase includes \$10.6 million for SBA loans, \$48.3 million for real estate loans and \$2.6 million increase in factored receivables. The increases were partly offset by a \$10.5 million decrease in commercial and industrial loans. SBA loans comprise the largest group of loans in our portfolio totaling \$268.9 million, or 53.7% of the total loans at December 31, 2023, compared to \$258.3 million, or 57.4%, of the total loans at December 31, 2022. Commercial and industrial loans totaled \$82.5 million, or 16.5%, of the total loans at December 31, 2023, compared to \$92.9 million, or 20.6%, of the total loans at December 31, 2022. Commercial and construction real estate loans totaled \$113.5 million, or 22.6%, of the total loans at December 31, 2023, compared to \$67.8 million, or 15.1%, of the total loans at December 31, 2022.

The following table sets forth the composition of our loans held for investment as of the dates indicated:

(In thousands, except percentages)	December 31,			
	2023		2022	
	Amount	Percent	Amount	Percent
Commercial and industrial	\$ 82,483	16.5%	\$ 92,946	20.6%
Consumer installment	900	0.2	1,058	0.2
Real estate – residential	8,181	1.6	5,566	1.2
Real estate – commercial	68,792	13.7	63,924	14.2
Real estate – construction and land	44,663	8.9	3,873	0.9
SBA 7(a) guaranteed	162,144	32.4	149,374	33.2
SBA 7(a) unguaranteed	64,858	12.9	56,268	12.5
SBA 504	41,906	8.4	52,668	11.7
USDA	2,124	0.4	2,235	0.5
Factored Receivables	25,044	5.0	22,420	5.0
<b>Total Loans</b>	<b>\$ 501,095</b>	<b>100.0%</b>	<b>\$ 450,332</b>	<b>100.0%</b>

The Company initially records the guaranteed portion of the SBA 7(a) and USDA loans as held for sale at the lower of cost or fair value. Loans held for sale totaled \$26.6 million and \$33.9 million at December 31, 2023 and 2022, respectively. During the year ended December 31, 2023, the Company elected to reclassify \$52.6 million of the SBA loans held for sale to held for investment. The Company determined that holding these loans provides better long-term risk adjusted returns than selling the loans.

*Loan Origination/Risk Management.* The Company has certain lending policies and procedures in place that are designed to maximize loan income with an acceptable level of risk. Management reviews and approves these policies and procedures on an annual basis and makes changes as appropriate. Management receives and reviews monthly reports related to loan originations, loan quality, concentrations of credit, loan delinquencies and nonperforming and potential problem loans. Diversification in the loan portfolio is a means of managing risk associated with fluctuations in economic conditions, both by type of loan and geographic location.

Commercial and industrial loans, which are predominantly loans to dentists, are underwritten based on historical and projected income of the business and individual borrowers and guarantors. The Company utilizes a comprehensive global debt service coverage analysis to determine debt service coverage ratios. This analysis compares global cash flow of the borrowers and guarantors on an individual credit to existing and proposed debt after consideration of personal and business related other expenses. Collateral is generally a lien on all available assets of the business borrower including intangible assets. Credit worthiness of individual borrowers and guarantors is established through the use of credit reports and credit scores.

Consumer loans are evaluated on the basis of credit worthiness as established through the use of credit reports and credit scores. Additional credit quality indicators include borrower debt to income ratios based on verifiable income sources.

Real estate mortgage loans are evaluated based on collateral value as well as global debt service coverage ratios based on historical and projected income from all related sources including the collateral property, the borrower, and all guarantors where applicable.

The Company originates SBA loans which are sometimes sold into the secondary market. The Company continues to service these loans after sale and is required under the SBA programs to retain specified amounts. The two primary SBA loan programs that the Company offers are the basic SBA 7(a) loan guaranty program and the SBA 504 loan program in conjunction with junior lien financing from a Certified Development Company ("CDC").

The SBA 7(a) program serves as the SBA's primary business loan program to help qualified small businesses obtain financing when they might not be eligible for business loans through normal lending channels. Loan proceeds under this program can be used for most business purposes including working capital, machinery and equipment, furniture and fixtures, land and building (including purchase, renovation and new construction), leasehold improvements and debt refinancing. Loan maturity is generally up to 10 years for non-real estate collateral and up to 25 years for real estate collateral. The SBA 7(a) loan is approved and funded by a qualified lender, partially guaranteed by the SBA and subject to applicable regulations. In general, the SBA guarantees up to 75% of the loan amount depending on loan size. The Company is required by the SBA to service the loan and retain a contractual minimum of 5% on all SBA 7(a) loans, but generally retains 25% (the unguaranteed portion). The servicing spread is 1% of the guaranteed portion of the loan that is sold in the secondary market.

The SBA 504 program is an economic development-financing program providing long-term, low down payment loans to businesses. Typically, an SBA 504 project includes a loan secured from a private-sector lender with a senior lien, a loan secured from a CDC (funded by a 100% SBA-guaranteed debenture) with a junior lien covering up to 40% of the total cost, and a contribution of at least 10% equity from the borrower. Debenture limits are \$5.0 million for regular 504 loans and \$5.5 million for those SBA 504 loans that meet a public policy goal.

The SBA has designated the Bank as a "Preferred Lender". As a Preferred Lender, the Bank has been delegated loan approval, closing and most servicing and liquidation authority from the SBA.

The Company also offers Business & Industry ("B&I") program loans through the USDA. These loans are similar to the SBA product, except they are guaranteed by the USDA. The guaranteed amount is generally 80%. B&I loans are made to businesses in designated rural areas and are generally larger loans to larger businesses than the SBA 7(a) loans. Similar to the SBA 7(a) product, they can be sold into the secondary market. These loans can be utilized for rural commercial real estate and equipment. The loans can have maturities up to 30 years and the rates can be fixed or variable.

Construction and land development loans are evaluated based on the borrower's and guarantor's credit worthiness, past experience in the industry, track record and experience with the type of project being considered, and other factors. Collateral value is determined generally by independent appraisal utilizing multiple approaches to determine value based on property type.

For all loan types, the Company establishes guidelines for its underwriting criteria including collateral coverage ratios, global debt service coverage ratios, and maximum amortization or loan maturity terms.

Loan concentrations are considered to exist when there are amounts loaned to multiple borrowers engaged in similar activities that would cause them to be similarly impacted by economic or other conditions. As of December 31, 2023, our loan portfolio included \$78.2 million of loans, approximately 15.6% of our total funded loans to the dental industry, as compared to \$83.9 million of loans, approximately 18.6% of our total funded loans December 31, 2022. We believe that these loans are to credit worthy borrowers and are diversified geographically.

As of December 31, 2023, 65.8% of the loan portfolio, or \$329.5 million, matured or re-priced within one year or less. The following table presents the contractual maturity ranges for loans outstanding as of December 31, 2023, and also presents portion of loans that have fixed interest rates or floating adjustable interest rates over the life of the loan in accordance with changes in the interest rate environment:

	Maturity Distribution of Loan Portfolio				
	One Year or Less	Over One Year Through Five Years	Over Five Years Through Fifteen Years	Over Fifteen Years	Total Loans Receivable
(In thousands)					
Commercial and industrial	\$ 5,786	\$ 12,405	\$ 64,292	\$ -	\$ 82,483
Consumer installment	350	550	-	-	900
Real estate – residential	203	7,847	-	131	8,181
Real estate – commercial	28,924	34,821	3,461	1,586	68,792
Real estate – construction and land	43,533	1,130	-	-	44,663
SBA 7(a) guaranteed	142,799	17,147	1,318	880	162,144
SBA 7(a) unguaranteed	56,722	7,276	324	536	64,858
SBA 504	24,042	15,361	2,503	-	41,906
USDA	2,124	-	-	-	2,124
Factored Receivables	25,044	-	-	-	25,044
Total	<u>\$ 329,527</u>	<u>\$ 96,537</u>	<u>\$ 71,898</u>	<u>\$ 3,133</u>	<u>\$ 501,095</u>

	Loans Due After One Year		
	Fixed Rate	Floating or Adjustable Rate	Total
(In thousands)			
Commercial and industrial	\$ 74,196	\$ 2,501	\$ 76,697
Consumer installment	550	-	550
Real estate – residential	6,512	1,466	7,978
Real estate – commercial	7,471	32,397	39,868
Real estate – construction and land	922	208	1,130
SBA 7(a) guaranteed	4,164	15,181	19,345
SBA 7(a) unguaranteed	1,635	6,501	8,136
SBA 504	-	17,864	17,864
USDA	-	-	-
Factored Receivables	-	-	-
Total	<u>\$ 95,450</u>	<u>\$ 76,118</u>	<u>\$ 171,568</u>

Scheduled contractual principal repayments of loans do not reflect the actual life of such assets. The average life of loans is less than their average contractual terms due to prepayments.

Loans acquired in acquisitions are initially recorded at fair value with no carryover of the related allowance for credit losses. The fair value of the loans is determined using market participant assumptions in estimating the amount and timing of principal and interest cash flows initially expected to be collected on the loans and discounting those cash flows at an appropriate market rate of interest. Under the accounting model for acquired loans, the excess of cash flows expected to be collected over the carrying amount of the loans, referred to as the “accretable yield,” is accreted into interest income over the life of the loans.



### Non-performing Assets

Our primary business segments are banking and other financial services, and as outlined above, the banking segment's primary business is lending. That activity entails potential credit losses, the magnitude of which depends on a variety of economic factors affecting borrowers which are beyond our control. While we have instituted underwriting guidelines and policies and credit review procedures to protect us from avoidable credit losses, some losses will inevitably occur.

Non-performing assets include non-accrual loans, loans 90 days or more past due and still accruing, and foreclosed assets. Non-performing assets totaled \$2.6 million as of December 31, 2023, compared to \$2.8 million as of December 31, 2022. As of December 31, 2023, non-performing assets consisted of SBA non-accrual loans totaling \$2.4 million, of which all except \$251,000 was guaranteed by the SBA, and commercial real estate loans totaling \$221,000.

Loans are considered past due when principal and interest payments have not been received as of the date such payments are contractually due. Loans are placed on non-accrual status when management has concerns relating to the ability to collect the loan interest and generally when such loans are 90 days or more past due. Accrued interest is charged off and no further interest is accrued. Subsequent payments received on non-accrual loans are recorded as reductions of principal, and interest income is recorded only after principal recovery is reasonably assured. A loan is considered impaired when it is probable that not all principal and interest amounts will be collected according to the original loan contract. Loans past due 90 days or more and still accruing interest totaled \$147,000 in factored receivables as of December 31, 2023, compared to \$206,000 in residential real estate and \$132,000 in factored receivables as of December 31, 2022.

Foreclosed assets represent property acquired as the result of borrower defaults on loans. Foreclosed assets are recorded at estimated fair value, less estimated selling costs, at the time of foreclosure. Write-downs occurring at foreclosure are charged against the allowance for possible credit losses. On an ongoing basis, properties are appraised as required by market indications and applicable regulations. Write-downs are provided for subsequent declines in value and are included in other non-interest expense along with other expenses related to maintaining the properties. There were no foreclosed assets as of December 31, 2023, and 2022.

The following table sets forth certain information regarding non-performing assets by type, including ratios of such loans to total assets as of the dates indicated:

(In thousands, except percentages)	December 31,	
	2023	2022
Non-accrual loans:		
Commercial and industrial	\$ 93	\$ -
Real estate – commercial	128	138
SBA guaranteed	1,951	2,221
SBA unguaranteed	251	107
Total non-accrual loans	2,423	2,466
Real estate – residential past due 90 days	-	206
Factored receivables past due 90 days	147	132
Foreclosed assets	-	-
Total non-performing assets	\$ 2,570	\$ 2,804
As a % of total loans	0.51%	0.65%
As a % of total assets	0.38	0.48

### ***Allowance for Credit Losses***

As discussed in Note 1 – Summary of Significant Accounting Policies in the accompanying notes to consolidated financial statements, our policies and procedures related to accounting for credit losses changed on January 1, 2023, in connection with the adoption of the CECL methodology as codified in ASC 326. In the case of loans and securities, allowances for credit losses are contra-asset valuation accounts, calculated in accordance with ASC 326, that are deducted from the amortized cost basis of these assets to present the net amount expected to be collected. When management deems all or a portion of a loan to be uncollectible, the appropriate amount is charged-off against the allowance. Subsequent recoveries, if any, are credited to the allowance. In the case of off-balance-sheet credit exposures, the allowance for credit losses is a liability account, calculated in accordance with ASC 326, reported as a component of other liabilities in our consolidated balance sheets. The amount of each allowance account represents management’s best estimate of CECL on these financial instruments considering available information, from internal and external sources, relevant to assessing exposure to credit loss over the contractual term of the instrument. Relevant available information includes historical credit loss experience, current conditions and reasonable and supportable forecasts. While historical credit loss experience provides the basis for the estimation of expected credit losses, adjustments to historical loss information may be made for differences in current portfolio-specific risk characteristics, environmental conditions or other relevant factors. While management utilizes its best judgment and information available, the ultimate adequacy of our allowance accounts is dependent upon a variety of factors beyond our control, including the performance of our portfolios, the economy, changes in interest rates and the view of the regulatory authorities toward classification of assets. For additional information regarding critical accounting policies, refer to Note 1 – Summary of Significant Accounting Policies and Note 3 - Loans and Allowance for Credit Losses in the accompanying notes to the consolidated financial statements.

The Company uses the open pool life method to estimate expected losses for all of the Company’s loan pools. The loan portfolio pools were selected in order to generally align with the loan categories specified in the quarterly call reports required to be filed with the Federal Financial Institutions Examination Council, except that the dental, SBA and USDA loans, are segregated in separate pools. For dental and SBA 7(a) loans, the Company adjusts the pool life for expected prepayment speeds.

For all loan pools, management has determined two years represents a reasonable and supportable forecast period and reverts to a historical loss rate over two years on a straight-line basis. Management leverages economic projections from a reputable and independent third party to inform its loss driver forecasts over the two year forecast period. Other internal and external indicators of economic forecasts are also considered by management when developing the forecast metrics.

Management estimates the allowance balance using relevant available information, from internal and external sources, relating to past events, current conditions, and reasonable and supportable forecasts. Historical credit loss experience provides the basis for the estimation of expected credit losses. Adjustments to historical loss information are made for differences in current loan-specific risk characteristics. See the discussion of Q-Factors described below.

The allowance for credit losses is measured based on call report segment as these types of loans exhibit similar risk characteristics. The allowance for credit losses for each segment is measured through the use of the open pool method. Loans that do not share risk characteristics are evaluated on an individual basis. Loans evaluated individually are not also included in the collective evaluation. For those loans that are classified as impaired, an allowance is established when the discounted cash flows, collateral value or observable market price of the impaired loan is lower than the carrying value of that loan.

Expected credit losses are estimated over the contractual term of the loans, adjusted for expected prepayments when appropriate. The contractual term excludes expected extensions, renewals and modifications unless management has a reasonable expectation at the reporting date that troubled debt restructuring will be executed with an individual borrower or the extension or renewal options are included in the original or modified contract at the reporting date and are not unconditionally cancellable by the Company.

Management qualitatively adjusts model results for risk factors (“Q-Factor”) that are not considered within our modeling processes but are nonetheless relevant in assessing the expected credit losses within our loan pools. These Q-Factors and other qualitative adjustments may increase or decrease management’s estimate of expected credit losses by a calculated percentage or amount based upon the estimated level of risk. The various risks that may be considered in making Q-Factor and other qualitative adjustments include, among other things, the impact of (i) changes in lending policies, procedures and strategies; (ii) staff experience; (iii) changes in volume and trends in classified loans, delinquencies and nonaccruals; (iv) concentration risk; (v) trends in underlying collateral values; (vi) external factors such as competition, legal and regulatory environment; and (vii) economic conditions.

Upon the adoption of ASC 326 effective on January 1, 2023, the total amount of the allowance for credit losses for loans estimated using the CECL methodology increased \$1.4 million compared to the total amount of the allowance for credit losses for loans estimated as of December 31, 2022 using the prior incurred loss model under GAAP.

The following table sets forth the allocation of the allowance for credit losses, the percentage of loans in each category to total gross loans and the ratio of allowance allocated to loans in each category as of the date indicated:

(In thousands, except percentages)	December 31, 2023			December 31, 2022		
	Allocated Allowance	% of Loan Portfolio	ACL to Loans	Allocated Allowance	% of Loan Portfolio	ACL to Loans
Commercial and industrial	\$ 2,495	16.5%	3.0%	\$ 1,301	20.6%	1.4%
Consumer installment	18	0.2	2.0	14	0.2	1.3
Real estate – residential	71	1.6	0.9	79	1.2	1.4
Real estate – commercial	616	13.7	0.9	899	14.2	1.4
Real estate – construction and land	143	8.9	0.3	55	0.9	1.4
SBA	2,484	53.7	0.9	1,505	57.4	0.6
USDA	19	0.4	0.9	52	0.5	2.3
Factored receivables	462	5.0	1.8	608	5.0	2.7
Total Loans	<u>\$ 6,308</u>	<u>100.0%</u>	<u>1.3%</u>	<u>\$ 4,513</u>	<u>100.0%</u>	<u>1.0%</u>

The table below presents a summary of the Company's net loan credit experience and provisions to the allowance for credit losses for the period indicated:

(In thousands, except percentages)	As of and for the Year Ended December 31	
	2023	2022
Average loans outstanding	\$ 491,448	\$ 458,980
Gross loans held for investment outstanding at end of period	\$ 501,095	\$ 450,332
Allowance for credit losses at beginning of period	\$ 4,513	\$ 4,152
Impact of adopting ASC 326	1,390	-
Provision for credit losses	1,333	1,264
Charge offs:		
Commercial and industrial	(214)	(337)
SBA 7(a)	(329)	(43)
Factored Receivables	(637)	(617)
Total charge-offs	(1,180)	(997)
Recoveries:		
Commercial and industrial	14	31
SBA 7(a)	69	22
Factored Receivables	169	41
Total recoveries	252	94
Net charge-offs	(928)	(903)
Allowance for credit losses at end of period	<u>\$ 6,308</u>	<u>\$ 4,513</u>
Ratio of allowance to end of period loans	1.26%	1.00%
Ratio of net charge-offs to average loans	0.19%	0.20%

## Deposits

Deposits are attracted principally from our primary geographic market area with the exception of time deposits, which, due to the Company's attractive rates, are attracted from across the nation. The Company offers a broad selection of deposit products, including demand deposit accounts, NOW accounts, money market accounts, regular savings accounts, term certificates of deposit and retirement savings plans (such as IRAs). Deposit account terms vary, with the primary differences being the minimum balance required, the time period the funds must remain on deposit, and the associated interest rates. Management sets the deposit interest rates periodically based on a review of deposit flows and a survey of rates among competitors and other financial institutions. The Company relies on customer service and long-standing relationships with customers to attract and retain deposits, and also on CD listing services.

The Company participates in the One-Way Buy Insured Cash Sweep (“ICS”) service, which provides for one-way buy transactions among banks for the purpose of purchasing cost-effective floating-rate funding without collateralization or stock purchase requirements. Management believes these sources represent a reliable and cost-efficient alternative funding source for the Company. However, to the extent that our condition or reputation deteriorates, or to the extent that there are significant changes in market interest rates which we do not elect to match, we may experience an outflow of brokered deposits. In that event we would be required to obtain alternate sources for funding. As of December 31, 2023, total deposits included \$50.0 million of ICS brokered deposits.

Total deposits increased \$33.9 million, or 10.7%, to \$526.9 million as of December 31, 2023, from \$493.0 million as of December 31, 2022. The following table sets forth our average deposit account balances, the percentage of each type of deposit to total deposits, and average cost of funds for each category of deposits for the periods indicated:

	Year Ended December 31, 2023			Year Ended December 31, 2022		
	Average Balance	Percent of Deposits	Average Rate	Average Balance	Percent of Deposits	Average Rate
(In thousands, except percentages)						
Non-interest-bearing deposits	\$ 92,230	18.0%	0.00%	\$ 104,170	22.3%	0.00%
Savings and interest-bearing demand	12,041	2.3	0.47	16,287	3.5	0.30
Money market accounts	132,471	25.9	4.64	129,972	27.9	1.26
Time deposits	275,540	53.8	4.19	216,196	46.3	1.50
Total deposits	<u>\$ 512,282</u>	<u>100.0%</u>	<u>3.46%</u>	<u>\$ 466,625</u>	<u>100.0%</u>	<u>1.06%</u>

The following table provides information on the maturity distribution of the time deposits exceeding the FDIC insurance limit of \$250,000 as of December 31, 2023:

(In thousands, except percentages)		
Maturing		
Three months or less	\$ 21,027	29.3%
Over three months to six months	18,010	25.0
Over six months to 12 months	22,629	31.5
Over 12 months	10,229	14.2
Total	<u>\$ 71,895</u>	<u>100.0%</u>

The estimated amount of uninsured total deposits is approximately \$59.3 million (11.3% of total deposits) and \$68.0 million (13.8% of total deposits) as of December 31, 2023 and 2022, respectively.

## Borrowings

The table below presents balances of each of the borrowing facilities as of the dates indicated:

(In thousands)	December 31,	
	2023	2022
Borrowings:		
FHLB borrowings	\$ -	\$ -
FRB borrowings (BTFP)	21,000	-
Subordinated notes	12,000	12,000
	<u>\$ 33,000</u>	<u>\$ 12,000</u>

The Company has a credit line with the FHLB with borrowing capacity of \$56.8 million secured by commercial loans. The Company determines its borrowing needs and renews the advances accordingly at varying terms. The Company had no borrowings with FHLB as of December 31, 2023 and 2022.

The Company also has a credit line with the FRB with borrowing capacity of \$43.5 million, which is secured by commercial loans. The company had no borrowings from the FRB at December 31, 2023 and 2022 under this credit line. During 2023, the FRB offered loans of up to one year in length under the BTFP to banks and other eligible depository institutions pledging U.S. treasuries, agency debt and mortgage-backed securities, and other qualifying assets as collateral, which are assessed at par value. The Bank pledged available for sale securities with par value of \$23.3 million to provide additional liquidity to meet the needs of depositors as of December 31, 2023. The Company had \$21.0 million of borrowings related to the BTFP as of December 31, 2023.

As of December 31, 2023 and 2022, T Bancshares had subordinated notes totaling \$12.0 million, consisting of \$8.0 million issued in 2017 bearing an interest rate of three month LIBOR plus 5.125%, with interest payable quarterly and maturing on July 20, 2027, at which all principal is due, and \$4.0 million issued in 2018 bearing interest rate of 7.125% payable semi-annually up to July 17, 2023, after which it converted to three month LIBOR plus 5.125%, with interest payable quarterly and maturing on March 31, 2028, at which all principal is due. The subordinated notes are unsecured and subordinated in right of payment to the payment of our existing and future senior indebtedness and structurally subordinated to all existing and future indebtedness of our subsidiaries. Beginning July 1, 2023, in accordance with the Adjustable Interest Rate (LIBOR) Act and the rules promulgated by the Federal Reserve thereunder, T Bancshares' outstanding subordinated notes transitioned to SOFR index.

### Capital Resources and Regulatory Capital Requirements

Shareholders' equity increased \$10.4 million, or 10.7%, to \$106.9 million as of December 31, 2023, from \$96.5 million as of December 31, 2022. The increase included net income of \$15.2 million, \$302,000 related to stock compensation expense, \$548,000 net after-tax other comprehensive income, along with \$250,000 related to the reduction in note receivable utilized to exercise stock options. The increases were partly offset by the repurchase of common stock in the amount of \$1.1 million and dividends paid on the Series B preferred stock and on the common stock in the amounts of \$1.6 million and \$2.0 million, respectively, and a \$1.3 million reduction in retained earnings related to the adoption of ASC326 on January 1, 2023.

Together with the Bank, the Company is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Bank's and, accordingly, the Company's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company must meet specific capital guidelines that involve quantitative measures of the Company's assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. The Company's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors. As of December 31, 2023, the Company and the Bank met all capital adequacy requirements to which they were subject. As of December 31, 2023, the Bank qualified as "well capitalized" under the prompt corrective action regulations of Basel III and the OCC.

Quantitative measures established by regulations to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets (as defined in the regulations), common equity Tier 1 capital (as defined in the regulations) to risk-weighted assets, and of Tier 1 capital (as defined in the regulations) to average assets (as defined in the regulations).

The following table presents our regulatory capital ratios, as well as those of the Bank, as of the dates indicated:

(In thousands)	December 31, 2023		December 31, 2022	
	Amount	Ratio	Amount	Ratio
<b>Tectonic Financial, Inc.</b>				
Tier 1 Capital (to Average Assets)	\$ 86,847	13.97%	\$ 76,805	13.27%
Common Equity Tier 1 (to Risk Weighted Assets)	69,597	15.74	59,555	14.80
Tier 1 Capital (to Risk Weighted Assets)	86,847	19.65	76,805	19.09
Total Capital (to Risk Weighted Assets)	92,385	20.90	81,317	20.21
<b>T Bank, N.A.</b>				
Tier 1 Capital (to Average Assets)	\$ 87,488	13.97%	\$ 76,767	13.47%
Common Equity Tier 1 (to Risk Weighted Assets)	87,488	20.04	76,767	19.29
Tier 1 Capital (to Risk Weighted Assets)	87,488	20.04	76,767	19.29
Total Capital (to Risk Weighted Assets)	92,957	21.29	81,279	20.42

In addition to the regulatory requirements of the federal banking agencies, Sanders Morris is subject to the regulatory framework applicable to registered investment advisors under the SEC's Division of Investment Management. Sanders Morris is also regulated by FINRA, which, among other requirements, imposes minimums on its net regulatory capital. As of December 31, 2023, Sanders Morris is in compliance with FINRA's net regulatory capital requirements.

## **Liquidity**

Our liquidity relates to our ability to maintain a steady flow of funds to support our ongoing operating, investing and financing activities. Our board of directors establishes policies and analyzes and manages liquidity to ensure that adequate funds are available to meet normal operating requirements in addition to unexpected customer demands for funds, such as high levels of deposit withdrawals or loan demand, in a timely and cost-effective manner. The most important factor in the preservation of liquidity is maintaining public confidence that facilitates the retention and growth of a large, stable supply of core deposits and funds. Ultimately, public confidence is generated through profitable operations, sound credit quality and a strong capital position. Liquidity management is viewed from a long-term and a short-term perspective as well as from an asset and liability perspective. We monitor liquidity through a regular review of loan and deposit maturities and forecasts, incorporating this information into a detailed projected cash flow model.

The Bank's liquidity is monitored by its management, the Asset-Liability Committee and its board of directors who review historical funding requirements, current liquidity position, sources and stability of funding, marketability of assets, options for attracting additional funds, and anticipated future funding needs, including the level of unfunded commitments.

The Company's primary sources of funds are retail, small business, custodial, commercial deposits, loan repayments, maturity of investment securities, other short-term borrowings, and other funds provided by operations. Our liquidity position is enhanced by our ability to raise additional funds as needed in the wholesale markets. While scheduled loan repayments and maturing investments are relatively predictable, deposit flows and loan prepayments are more influenced by interest rates, general economic conditions, and competition. The Company will maintain investments in liquid assets based upon management's assessment of (1) the need for funds, (2) expected deposit flows, (3) yields available on short-term liquid assets, and (4) objectives of the asset/liability management program.

The Company had cash and cash equivalents of \$58.8 million, or 8.7% of total assets, as of December 31, 2023. In addition to the on balance sheet liquidity available, the Company has lines of credit with the FHLB and the FRB, which provide the Company with a source of off-balance sheet liquidity. As of December 31, 2023, the Company's borrowing capacity with the FHLB was \$56.8 million, or 8.4% of assets, none of which was utilized, and borrowing capacity with the FRB was \$43.5 million, or 6.4% of assets. During March 2023, the Federal Reserve created the BTFP, which was made available to banks in response to liquidity concerns in the United States banking system. The BTFP allows the whole par value of available for sale securities to be included as the collateral value. As of December 31, 2023, securities with a par value of \$23.3 million were pledged to the Federal Reserve under this program, of which \$21.0 million was borrowed against. In addition, as of December 31, 2023, the Company had approximately \$160.3 million of SBA guaranteed loans held for investment that could be sold to investors.

### **Off-Balance Sheet Arrangements and Contractual Obligations**

We are a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of our customers. These financial instruments include commitments to extend credit and standby letters of credit. These instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the accompanying balance sheets. Our exposure to credit loss in the event of non-performance by the other party to the financial instruments for commitments to extend credit and standby letters of credit is represented by the contractual amount of those instruments. We follow the same credit policies in making commitments and conditional obligations as we do for on-balance sheet instruments.

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

Standby letters of credit are conditional commitments issued by us to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loans to customers.

The following table presents future contractual obligations to make future payments, excluding interest, for the periods indicated:

	As of December 31, 2023				
	Less than One Year	One to Three Years	Over Three to Five Years	Over Five Years	Total
(In thousands)					
FHLB borrowings	\$ -	\$ -	\$ -	\$ -	\$ -
FRB borrowings	21,000	-	-	-	21,000
Subordinated notes	-	-	-	12,000	12,000
Time deposits	250,876	54,287	3,272	-	308,435
Minimum lease payments	682	1,278	407	524	2,891
Total	<u>\$ 272,558</u>	<u>\$ 55,565</u>	<u>\$ 3,679</u>	<u>\$ 12,524</u>	<u>\$ 344,326</u>

The following table presents contractual financial commitments for the periods indicated, however some of these commitments may expire unused or only partially used, so the total amounts do not necessarily reflect future cash requirements.

	As of December 31, 2023				
	Less than One Year	One to Three Years	Over Three to Five Years	Over Five Years	Total
(In thousands)					
Undisbursed loan commitments	\$ 8,411	\$ 2,041	\$ 111	\$ 35,180	\$ 45,743
Standby letters of credit	162	-	-	-	162

*Allowance For Credit Losses - Off-Balance-Sheet Credit Exposures* The allowance for credit losses for off-balance sheet credit exposures is calculated under the CECL model, representing expected credit losses over the contractual period for which the Company is exposed to credit risk resulting from a contractual obligation to extend credit. Off-balance sheet credit exposures primarily consist of amounts available under outstanding commitments to extend credit and letters of credit detailed above. The allowance for credit losses for off-balance sheet credit exposures is estimated by loan segment at each balance sheet date using the same methodologies as portfolio loans, taking into consideration the likelihood that funding will occur based on historical utilization rates. Upon adoption of ASC 326 on January 1, 2023, the impact of adoption was \$238,000 to the allowance for credit losses for off-balance-sheet credit exposure, and subsequent to adoption we recognized a credit loss benefit related to off-balance-sheet credit exposures totaling \$45,000 for the year ended December 31, 2023, leaving a balance of \$193,000 in the allowance for credit losses for off-balance sheet credit exposures as of December 31, 2023. Further information regarding our policies and methodology used to estimate the allowance for credit losses for off-balance-sheet credit exposures is presented in Note 12 – Commitments and Contingencies in the accompanying notes to consolidated financial statements.

#### Item 7A. Quantitative and Qualitative Disclosures about Market Risk.

##### *Interest Rate Sensitivity and Market Risk*

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

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

We manage exposure to interest rates by structuring the balance sheet in the ordinary course of business. We use no off-balance-sheet financial instruments to manage interest rate risk.

Our exposure to interest rate risk is managed by the Bank's Asset Liability Committee in accordance with policies approved by the Bank's board of directors. The committee formulates strategies based on appropriate levels of interest rate risk. In determining the appropriate level of interest rate risk, the committee considers the impact on earnings and capital of the current outlook on interest rates, potential changes in interest rates, liquidity, business strategies and other factors.



The Asset Liability Committee meets regularly to review, among other things, the sensitivity of assets and liabilities to interest rate changes, the book and market values of assets and liabilities, unrealized gains and losses, purchase and sale activities, commitments to originate loans and the maturities of investments and borrowings. Additionally, the committee reviews liquidity, cash flow flexibility, maturities of deposits and consumer and commercial deposit activity. We employ methodologies to manage interest rate risk which include an analysis of relationships between interest-earning assets and interest-bearing liabilities, and an interest rate shock simulation model.

We use interest rate risk simulation models and shock analysis to test the interest rate sensitivity of net interest income and the impact of changes in interest rates on other financial metrics. The assumptions used are inherently uncertain and, as a result, the model cannot precisely measure future net interest income or precisely predict the impact of fluctuations in market interest rates on net interest income. Actual results will differ from the model's simulated results due to timing, magnitude and frequency of interest rate changes as well as changes in market conditions and the application and timing of various management strategies.

On at least an annual basis, we run various stress tests to measure the impact on net interest income from changes in market interest rates under various scenarios. Under the static model, rates are shocked instantaneously and ramped rates change over a twelve-month horizon based upon parallel yield curve shifts. Parallel shock scenarios assume instantaneous parallel movements in the yield curve compared to a flat yield curve scenario. Additionally, we run non-parallel simulation involving analysis of interest income and expense under various changes in the shape of the yield curve.

The Company's asset liability management model indicated that it was in an asset sensitive position in terms of its income simulation as of December 31, 2023. The following table summarizes the impact of an instantaneous, sustained simulated change in net interest income over a 12-month horizon as of December 31, 2023:

<b>Change in Interest Rates (basis points)</b>	<b>% Change in Net Interest Income</b>
+200	20.71
+100	15.97
-100	6.83
-200	2.82

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

**Item 8. Financial Statements and Supplementary Data**

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and Shareholders of  
Tectonic Financial, Inc.

**Opinion on the Consolidated Financial Statements**

We have audited the accompanying consolidated balance sheets of Tectonic Financial, Inc. (the “Company”) as of December 31, 2023, and 2022, and the related consolidated statements of income, comprehensive income, changes in shareholders’ equity, and cash flows for the years then ended, and the related notes (collectively referred to as the “financial statements”). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2023, and 2022, and the results of their operations and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

**Basis for Opinion**

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

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits we are required to obtain an understanding of internal control over financial reporting, but not for the purpose of expressing an opinion on the effectiveness of the entity’s internal control over financial reporting. Accordingly, we express no such opinion.

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

/s/ Whitley Penn LLP

We have served as the Company’s auditor since 2018.

Plano, Texas  
April 1, 2024

**TECTONIC FINANCIAL, INC.**  
**CONSOLIDATED BALANCE SHEETS**

	<u>December 31,</u> <u>2023</u>	<u>December 31,</u> <u>2022</u>
<b>(In thousands, except share amounts)</b>		
<b>ASSETS</b>		
Cash and due from banks	\$ 5,016	\$ 8,549
Interest-bearing deposits	52,481	32,562
Federal funds sold	1,270	1,044
Total cash and cash equivalents	58,767	42,155
Securities available for sale	22,977	20,633
Securities held to maturity	24,194	25,262
Securities, restricted at cost	4,176	3,496
Securities, not readily marketable	-	100
Loans held for sale	26,573	33,902
Loans, net of allowance for credit losses of \$6,308 and \$4,513, respectively	494,787	445,819
Bank premises and equipment, net	4,758	4,629
Core deposit intangible, net	359	569
Goodwill	21,440	21,440
Deferred tax asset	889	636
Other assets	18,426	13,895
Total assets	<u>\$ 677,346</u>	<u>\$ 612,536</u>
<b>LIABILITIES</b>		
Demand deposits:		
Non-interest-bearing	\$ 68,433	\$ 94,187
Interest-bearing	150,023	137,148
Time deposits	308,435	261,690
Total deposits	526,891	493,025
Borrowed funds	21,000	-
Subordinated notes	12,000	12,000
Other liabilities	10,598	11,013
Total liabilities	570,489	516,038
Commitments and contingencies (see Note 11)		
<b>SHAREHOLDERS' EQUITY</b>		
Preferred stock, 9.00% fixed to floating rate Series B non-cumulative, perpetual (\$0.01 par value; 1,725,000 shares authorized, issued and outstanding at December 31, 2023 and December 31, 2022)	17	17
Common stock, \$0.01 par value; 40,000,000 shares authorized; 7,186,453 and 7,094,453 shares issued at December 31, 2023 and December 31, 2022, respectively, and 7,102,680 and 7,068,884 shares outstanding at December 31, 2023 and December 31, 2022, respectively	72	71
Additional paid-in capital	51,246	50,695
Treasury stock, at cost; 83,773 shares and 25,569 shares as of December 31, 2023 and December 31, 2022, respectively	(1,575)	(481)
Retained earnings	58,917	48,564
Accumulated other comprehensive loss	(1,820)	(2,368)
Total shareholders' equity	106,857	96,498
Total liabilities and shareholders' equity	<u>\$ 677,346</u>	<u>\$ 612,536</u>

See accompanying notes to consolidated financial statements.

**TECTONIC FINANCIAL, INC.**  
**CONSOLIDATED STATEMENTS OF INCOME**  
**YEARS ENDED DECEMBER 31,**

(In thousands, except per share data and share amounts)

	2023	2022
<b>Interest Income</b>		
Loan, including fees	\$ 41,612	\$ 30,885
Securities	2,091	1,887
Federal funds sold	45	12
Interest-bearing deposits	2,719	601
Total interest income	46,467	33,385
<b>Interest Expense</b>		
Deposits	17,749	4,940
Borrowed funds	1,357	964
Total interest expense	19,106	5,904
Net interest income	27,361	27,481
Provision for credit losses	1,288	1,264
Net interest income after provision for credit losses	26,073	26,217
<b>Non-interest Income</b>		
Trust income	6,442	6,098
Gain on sale of loans	581	-
Advisory income	14,910	13,549
Brokerage income	7,527	11,754
Service fees and other income	10,037	8,293
Rental income	307	346
Total non-interest income	39,804	40,040
<b>Non-interest Expense</b>		
Salaries and employee benefits	31,288	31,093
Occupancy and equipment	1,984	1,707
Trust expenses	2,265	2,243
Brokerage and advisory direct costs	1,936	2,015
Professional fees	1,813	1,480
Data processing	941	794
Other	6,594	5,473
Total non-interest expense	46,821	44,805
<b>Income before Income Taxes</b>	19,056	21,452
Income tax expense	3,836	4,422
<b>Net Income</b>	15,220	17,030
Preferred stock dividends	1,553	1,552
<b>Net income available to common stockholders</b>	\$ 13,667	\$ 15,478
<b>Earnings per common share:</b>		
Basic	\$ 1.94	\$ 2.19
Diluted	1.87	2.11
Weighted average common shares outstanding	7,057,430	7,061,519
Weighted average diluted shares outstanding	7,292,668	7,336,195

See accompanying notes to consolidated financial statements.

**TECTONIC FINANCIAL, INC.**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**  
**YEARS ENDED DECEMBER 31,**

(In thousands)	2023	2022
<b>Net Income</b>	\$ 15,220	\$ 17,030
<b>Other Comprehensive Income (Loss):</b>		
Change in unrealized gain (loss) on investment securities available for sale	693	(2,582)
Tax effect	145	(542)
Other comprehensive income (loss)	548	(2,040)
<b>Comprehensive Income</b>	<u>\$ 15,768</u>	<u>\$ 14,990</u>

See accompanying notes to consolidated financial statements.

**TECTONIC FINANCIAL, INC.**  
**CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY**  
**YEARS ENDED DECEMBER 31,**

(In thousands)	Series B Preferred Stock	Common Stock	Additional Paid-in Capital	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Loss	Total
<b>Balance at January 1, 2022</b>	\$ 17	\$ 71	\$ 50,176	\$ -	\$ 34,851	\$ (328)	\$ 84,787
Issuance of common stock	-	-	97	-	-	-	97
Purchase of treasury stock at cost	-	-	-	(481)	-	-	(481)
Repayments of note receivable utilized to exercise options	-	-	150	-	-	-	150
Dividends paid on common stock	-	-	-	-	(1,765)	-	(1,765)
Dividends paid on Series B preferred stock	-	-	-	-	(1,552)	-	(1,552)
Net income	-	-	-	-	17,030	-	17,030
Other comprehensive loss	-	-	-	-	-	(2,040)	(2,040)
Stock based compensation	-	-	272	-	-	-	272
<b>Balance at December 31, 2022</b>	\$ 17	\$ 71	\$ 50,695	\$ (481)	\$ 48,564	\$ (2,368)	\$ 96,498
Cumulative change in accounting principle (adoption of ASC 326), net of tax	-	-	-	-	(1,286)	-	(1,286)
<b>Balance at January 1, 2023, as adjusted for change in accounting principle (adoption of ASC 326)</b>	17	71	50,695	(481)	47,278	(2,368)	95,212
Issuance of common stock	-	1	(1)	-	-	-	-
Purchase of treasury stock at cost	-	-	-	(1,094)	-	-	(1,094)
Repayments of note receivable utilized to exercise options	-	-	250	-	-	-	250
Dividends paid on common stock	-	-	-	-	(2,028)	-	(2,028)
Dividends paid on Series B preferred stock	-	-	-	-	(1,553)	-	(1,553)
Net income	-	-	-	-	15,220	-	15,220
Other comprehensive income	-	-	-	-	-	548	548
Stock based compensation	-	-	302	-	-	-	302
<b>Balance at December 31, 2023</b>	<u>\$ 17</u>	<u>\$ 72</u>	<u>\$ 51,246</u>	<u>\$ (1,575)</u>	<u>\$ 58,917</u>	<u>\$ (1,820)</u>	<u>\$ 106,857</u>

See accompanying notes to consolidated financial statements.

**TECTONIC FINANCIAL, INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**YEARS ENDED DECEMBER 31,**

(In thousands)	2023	2022
<b>Cash Flows from Operating Activities</b>		
Net income	\$ 15,220	\$ 17,030
Adjustments to reconcile net income to net cash used in operating activities:		
Loss on disposition of securities not readily marketable	100	-
Provision for credit losses	1,288	1,264
Depreciation	247	228
Accretion of discount on loans	(19)	32
Core deposit intangible amortization	210	208
Securities premium amortization, net	(93)	(14)
Origination of loans held for sale	(51,336)	(56,050)
Proceeds from payments and sales of loans held for sale	6,632	509
Gain on sale of loans	(581)	-
Gain on sale of other real estate owned	-	(33)
Stock based compensation	302	272
Deferred income taxes	(56)	311
Servicing assets, net	21	179
Net change in:		
Other assets	(4,513)	(1,203)
Other liabilities	(608)	1,480
Net cash used in operating activities	(33,186)	(35,787)
<b>Cash Flows from Investing Activities</b>		
Purchase of securities held to maturity	-	(7,408)
Purchase of securities available for sale	(405,803)	(381,514)
Principal payments, calls and maturities of securities available for sale	404,198	375,417
Principal payments of securities held to maturity	1,115	1,871
Purchase of securities, restricted	(11,502)	(12,818)
Proceeds from sale of securities, restricted	10,822	11,754
Proceeds from sales of real estate owned	-	1,112
Net change in loans	903	32,880
Purchases of premises and equipment	(376)	(128)
Net cash (used in) provided by investing activities	(643)	21,166
<b>Cash Flows from Financing Activities</b>		
Net change in demand deposits	(12,879)	(5,450)
Net change in time deposits	46,745	54,306
Proceeds from borrowed funds	471,900	387,800
Repayment of borrowed funds	(450,900)	(422,321)
Repayments on note receivable utilized to exercise stock options	250	150
Dividends paid on common stock	(2,028)	(1,765)
Dividends paid on Series B preferred shares	(1,553)	(1,552)
Proceeds from exercise of stock options	-	97
Purchase of treasury stock at cost	(1,094)	(481)
Net cash provided by financing activities	50,441	10,784
<b>Net change in cash and cash equivalents</b>	16,612	(3,837)
Cash and cash equivalents at beginning of period	42,155	45,992
<b>Cash and cash equivalents at end of period</b>	\$ 58,767	\$ 42,155
<b>Non Cash Transactions</b>		
Transfers from loans held for sale to loans held for investment	\$ 52,575	\$ 55,401
Lease liabilities incurred in exchange for right-of-use assets	\$ 72	\$ 143
<b>Supplemental disclosures of cash flow information</b>		
Cash paid during the year for:		
Interest	\$ 18,785	\$ 5,875
Income taxes	\$ 3,350	\$ 4,715

See accompanying notes to consolidated financial statements.



## Notes to Consolidated Financial Statements

### Note 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### Organization and Nature of Operations

Tectonic Financial, Inc. (the “Company,” “we,” “us,” or “our”) is a financial holding company that offers, through its subsidiaries, banking and other financial services including trust, investment advisory, securities brokerage, factoring, third-party administration, qualified plan recordkeeping and insurance services to individuals, small businesses and institutions across the United States.

We operate through four main direct and indirect subsidiaries: (i) T Bancshares, Inc. (“T Bancshares”), which was incorporated under the laws of the State of Texas on December 23, 2002 to serve as the bank holding company for T Bank, N.A., a national association (the “Bank”), (ii) Sanders Morris LLC (“Sanders Morris”), a registered broker-dealer with the Financial Industry Regulatory Authority (“FINRA”), and registered investment advisor with the Securities and Exchange Commission, (“SEC”), (iii) Tectonic Advisors, LLC (“Tectonic Advisors”) a registered investment advisor registered with the SEC focused generally on managing money for relatively large, affiliated institutions as well as for their clients, which include individuals, businesses, and qualified plans and (iv) HWG Insurance Agency LLC (“HWG”), an insurance agency registered with the Texas Department of Insurance (“TDI”).

We are headquartered in Dallas, Texas. The Bank operates through a main office located at 16200 Dallas Parkway, Dallas, Texas. Our other subsidiaries operate from offices in Houston, Dallas, and Plano, Texas. Our Houston office is located at 600 Travis Street, 59<sup>th</sup> Floor, Houston, Texas, and includes the home offices of Sanders Morris and HWG, as well as Tectonic Advisors’ family office services team. Our Dallas office, which is a branch office of Sanders Morris, is at 5950 Sherry Lane, Suite 470, Dallas, Texas. Our main office for Tectonic Advisors is located at 17 Cowboys Way, Suite 250, Frisco, Texas, and also includes a branch office of HWG.

The Bank offers a broad range of commercial and consumer banking and trust services primarily to small- to medium-sized businesses and their employees, and other institutions. The Nolan Company (“Nolan”), operating from its office in Overland Park, Kansas as a division within the bank, offers third party administration (“TPA”) services, and Integra Funding Solutions, LLC (“Integra”), also operating as a division within the Bank from Integra’s office in Fort Worth, Texas, offers factoring services. The Bank’s technological capabilities, including worldwide free ATM withdrawals, sophisticated on-line banking capabilities, electronic funds transfer capabilities, and economical remote deposit solutions, allow most customers to be served regardless of their geographic location. The Bank serves its local geographic market which includes Dallas, Tarrant, Denton, Collin and Rockwall counties in Texas which encompass an area commonly referred to as the Dallas/Fort Worth Metroplex. The Bank also serves the dental and other health professional industries through a centralized loan and deposit platform that operates out of its main office in Dallas, Texas. In addition, the Bank serves the small business community by offering loans guaranteed by the U.S. Small Business Administration (“SBA”) and the U.S. Department of Agriculture (“USDA”).

The Bank offers a wide range of deposit services including demand deposits, regular savings accounts, money market accounts, individual retirement accounts, and certificates of deposit with fixed rates and a range of maturity options. Lending services include commercial loans to small- to medium-sized businesses and professional concerns as well as consumers. The Bank also offers wealth management and trust services. The Bank’s traditional fiduciary services clients primarily consist of clients of Cain Watters & Associates L.L.C. (“Cain Watters”). The Bank, Cain Watters and Tectonic Advisors entered into an advisory services agreement related to the trust operations in April 2006, which has been amended from time to time, most recently in July 2016. See Note 13, *Related Parties*, to these consolidated financial statements for more information. In addition, the Nolan division of the Bank offers TPA services and provides clients with retirement plan design and administrative services, specializing in ministerial recordkeeping, administration, actuarial and design services for retirement plans of small businesses and professional practices. We believe offering TPA services allows us to serve our clients more fully and to attract new clients to our trust platform.

*Basis of Presentation.* The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries, T Bancshares, the Bank, Tectonic Advisors, Sanders Morris, and through Sanders Morris, HWG. All intercompany transactions and balances are eliminated in consolidation.

## **Use of Estimates**

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount of assets, liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expense during the reporting period, as well as the disclosures provided. Changes in assumptions or in market conditions could significantly affect the estimates. The determination of the allowance for credit losses, the fair value of stock options, the fair values of financial instruments and other real estate owned, and the status of contingencies are particularly susceptible to significant change in recorded amounts.

## **Cash and Cash Equivalents**

The Company maintains its cash in bank deposit accounts, which, at times, may exceed federally insured limits. The Company has not experienced any losses in such accounts and does not believe it is exposed to significant credit risk on cash and cash equivalents.

For purposes of the consolidated statements of cash flows, cash and cash equivalents include cash on hand, deposits with other financial institutions, and federal funds sold. Net cash flows are reported for customer loan and deposit transactions.

## **Trust Assets**

Property held for customers in a fiduciary capacity, other than trust cash on deposit at the Bank, is not included in the accompanying consolidated financial statements since such items are not assets of the Company.

## **Securities**

Securities are classified as held to maturity and carried at amortized cost when management has the positive intent and ability to hold them until maturity. Securities to be held for indefinite periods of time are classified as available for sale and carried at fair value, with the unrealized holding gains and losses reported as a component of other comprehensive income, net of tax. Securities held for resale are classified as trading and are carried at fair value, with changes in unrealized holding gains and losses included in income. Management determines the appropriate classification of securities at the time of purchase. Securities with limited marketability, such as stock in the FRB and the FHLB are carried at cost. Securities not readily marketable are carried at cost.

Interest income includes amortization of purchase premiums and accretion of purchase discounts. Premiums and discounts on securities are generally amortized on the interest method with a constant effective yield without anticipating prepayments, except for mortgage-backed securities where prepayments are anticipated. Premiums on callable securities are amortized to their earliest call date. Gains and losses are recorded on the trade date and determined using the basis of the cost of specific securities sold.

## **Factored Receivables**

Integra, operating as a division of the Bank, purchases invoices on completed work from its factoring clients. Integra also makes, from time to time, short-term advances to its clients on transportation contracts for upcoming loads or, to a much lesser extent, makes over-advances on the existing purchased invoices. Funds are advanced to the client based on the applicable advance rate, less fees, as agreed to in each individual factoring agreement. The gross amount (face value) of the invoices purchased are recorded by Integra as factored receivables, and the unadvanced portions of the invoices purchased, less discount and origination fees, are considered deferred client reserves and recorded as other liabilities in the Company's consolidated balance sheets. The deferred client reserves are held to settle any payment disputes or collection short payments, and become reserves due to client when the receivables are collected. Reserves due to client may be used to pay clients' obligations to various third parties as directed by the client, are periodically withdrawn by clients, and are reported as deposits in the Company's consolidated balance sheets.

Unearned factoring fees and unearned net origination fees are deferred revenue and recognized as interest income in the Company's consolidated income statements over the weighted average collection period for the entire portfolio of factored receivables. Subsequent factoring fees are recognized in interest income as incurred by the client and deducted from the clients' reserve balances.

Other factoring-related fees, which include ACH and wire transfer fees, fuel card funding fees, carrier payment fees, fuel advance fees, and other similar fees, are recognized as incurred and are reported by the Company as non-interest income.

## **Loans Held for Sale**

Loans which are originated or purchased and are intended for sale in the secondary market are carried at the lower of cost or estimated fair value determined on an aggregate basis. Valuation adjustments, if any, are recognized through a valuation allowance by charges to non-interest income and direct loan origination costs and fees are deferred at origination of the loan and are recognized in non-interest income upon sale of the loan. Loans held for sale are comprised of the guaranteed portion of SBA and USDA loans. The Company did not incur a lower of cost or market valuation provision in the years ended December 31, 2023 and 2022. The Company elected to reclassify \$52.6 million and \$55.4 million of the SBA 7(a) loans held for sale to loans held for investment during the year ended December 31, 2023 and 2022, respectively.

## **Loans**

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at the principal balance outstanding, net of unearned interest, unearned discount, deferred loan fees, and allowance for credit losses. Interest income is accrued on the unpaid principal balance. Discount on acquired loans and net loan origination fees are deferred and recognized in interest income using the level-yield method without anticipating prepayments.

Interest income on commercial business and commercial real estate loans is discontinued when the loan becomes 90 days delinquent unless the credit is well secured and in process of collection. Unsecured consumer loans are generally charged off when the loan becomes 90 days past due. Consumer loans secured by collateral other than real estate are charged off after a review of all factors affecting the ability to collect on the loan, including the borrower's history, overall financial condition, resources, guarantor support, and the realizable value of any collateral. However, any consumer loan past due 180 days is charged off. Past due status is based on the contractual terms of the loan. In all cases, loans are placed on non-accrual or charged off at an earlier date if collection of principal or interest is considered doubtful.

All interest accrued but not received for loans placed on non-accrual are reversed against interest income. Interest received on such loans is accounted for on a cash-basis or cost-recovery method, until qualifying for return to accrual basis. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

## **New Accounting Pronouncements**

The Company adopted Accounting Standards Update ("ASU") 2016-13, Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments ("ASC 326"), effective on January 1, 2023. The guidance replaces the incurred loss methodology with an expected loss methodology that is referred to as the current expected credit loss ("CECL") methodology. The CECL model requires the measurement of all expected credit losses for financial assets measured at amortized cost and certain off-balance-sheet credit exposures based on historical experience, current conditions, and reasonable and supportable forecasts. ASC 326 requires enhanced disclosures related to the significant estimates and judgments used in estimating credit losses as well as the credit quality and underwriting standards of a company's portfolio. ASU 2016-13 permits the use of estimation techniques that are practical and relevant to the Company's circumstances, as long as they are applied consistently over time and faithfully estimate expected credit losses in accordance with the standard. In addition, ASC 326 made changes to the accounting for available for sale debt securities. One such change is to require credit losses to be presented as an allowance rather than as a write-down on available for sale debt securities management does not intend to sell or believes that it is more likely than not they will be required to sell. Management has made a policy election to exclude accrued interest receivable on available for sale securities from the estimate of credit losses and report accrued interest separately in other assets in the consolidated balance sheets.

The Company adopted ASC 326 using the modified retrospective method for loans and off-balance-sheet ("OBS") credit exposures. Results for reporting periods beginning after January 1, 2023, are presented under ASC 326 while prior period amounts continue to be reported in accordance with previously applicable incurred loss model under GAAP. The Company recorded a one-time cumulative-effect adjustment to the allowance for credit losses of \$1.4 million which was recognized through a \$1.1 million adjustment to retained earnings, net of tax. This adjustment brought the beginning balance of the allowance for credit losses to \$5.9 million as of January 1, 2023. In addition, the Company recorded a \$237,505 reserve on unfunded commitments which is recorded in other liabilities in the Company's consolidated balance sheet, and was recognized through a \$188,000 adjustment to retained earnings, net of tax.

The Company adopted ASC 326 using the prospective transition approach for debt securities for which other-than-temporary impairment had been recognized prior to January 1, 2023. As of December 31, 2022, the Company did not have any other-than-temporarily impaired investment securities. Therefore, upon adoption of ASC 326, the Company determined that an allowance for credit losses for debt securities was not required.

ASU 2022-02, Financial Instruments – Credit Losses (Topic 326): Troubled Debt Restructurings and Vintage Disclosures (“ASU 2022-02”), eliminates the accounting guidance for troubled debt restructurings in ASC Subtopic 310-40, Receivables -Troubled Debt Restructurings by Creditors, while enhancing disclosure requirements for certain loan refinancings and restructurings by creditors when a borrower is experiencing financial difficulty. Additionally, ASU 2022-02 requires entities to disclose current-period gross write-offs by year of origination for financing receivables and net investments in leases within the scope of ASC Subtopic 326-20, Financial Instruments – Credit Losses – Measured at Amortized Cost. The Company adopted ASU 2022-02 on a modified retrospective basis effective on January 1, 2023. The adoption did not have a significant impact on the Company’s consolidated financial statements.

#### **Allowance for Credit Losses**

As further discussed below under “*New Accounting Pronouncements*” the Company adopted Accounting Standards Update (“ASU”) 2016-13, “Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments,” on January 1, 2023. Accounting Standards Codification (“ASC”) Topic 326 (“ASC 326”) replaces the previous “incurred loss” methodology with an “expected loss” methodology which encompasses allowances for losses expected to be incurred over the life of the portfolio. The new current expected credit loss (“CECL”) model requires the measurement of all expected credit losses for financial assets measured at amortized cost and certain off-balance-sheet credit exposures based on historical experience, adjusted for qualitative factors and current conditions, and reasonable and supportable forecasts. The Company adopted ASC 326 using the modified retrospective method for loans and OBS credit exposures.

*Allowance for credit losses – loans:* In accordance with ASC 326, *Measurement of Credit Losses on Financial Instruments*, the allowance for credit losses on loans is a valuation account that is deducted from the amortized cost basis of loans to present management's best estimate of the net amount expected to be collected. Loans, or portions thereof, are charged-off against the allowance for credit losses when management believes that collectability of the principal is unlikely. Subsequent recoveries, if any, are credited to the allowance. The allowance is increased (decreased) by provisions (or reversals of) reported in the income statement as a component of provision for credit losses. Management has made the accounting policy election to exclude accrued interest receivable on loans from the estimate of credit losses and reports accrued interest separately in other assets in the consolidated balance sheets.

The Company adopted ASU 2016-13 effective on January 1, 2023. The guidance replaces the incurred loss methodology with an expected loss methodology that is referred to as the CECL methodology. The new CECL model requires the measurement of all expected credit losses for financial assets measured at amortized cost and certain off-balance-sheet credit exposures based on historical experience, current conditions, and reasonable and supportable forecasts. The Company adopted ASC 326 using the modified retrospective method for loans and OBS credit exposures. Results for reporting periods beginning after January 1, 2023, are presented under ASC 326 while prior period amounts continue to be reported in accordance with the previously applicable incurred loss model under GAAP. The Company recorded a one-time cumulative-effect adjustment to the allowance for credit losses of \$1.4 million which was recognized through a \$1.1 million adjustment to retained earnings, net of tax. This adjustment brought the beginning balance of the allowance for credit losses to \$5.9 million as of January 1, 2023. In addition, the Company recorded a \$237,505 reserve on unfunded commitments which is recorded in other liabilities in the Company’s consolidated balance sheet, and was recognized through a \$188,000 adjustment to retained earnings, net of tax.

*Allowance for credit losses - available for sale securities:* For available for sale securities in an unrealized loss position, the Company first assesses whether it intends to sell or it is more-likely-than-not that it will be required to sell the securities before recovery of the amortized cost basis. If either of these criteria is met, the securities amortized cost basis is written down to fair value as a current period expense. If either of the above criteria is not met, the Company evaluates whether the decline in fair value is the result of credit losses or other factors. In making this assessment, management may consider various factors including the extent to which fair value is less than amortized cost, any changes to the rating of the security by a rating agency, performance of any underlying collateral and adverse conditions specifically related to the security, among other factors. If this assessment indicates that a credit loss exists, the present value of cash flows expected to be collected are compared to the amortized cost basis of the security and any excess of the amortized cost basis over the present value of expected cash flows is recorded as an allowance for credit loss, limited to the amount by which the fair value is less than the amortized cost basis. Any impairment not recorded through an allowance for credit loss is recognized in other comprehensive income as a non credit-related impairment.

The Company evaluates whether the decline in fair value has resulted from credit losses or other factors based upon our analysis of the underlying risk characteristics, including credit ratings, such as bond ratings, and other qualitative factors related to our available for sale securities and in consideration of our historical credit loss experience and internal forecasts. If this assessment indicates that a credit loss exists, the present value of cash flows expected to be collected from the security are compared to the amortized cost basis of the security. If the present value of cash flows expected to be collected is less than the amortized cost basis, a credit loss exists and an allowance for credit losses is recorded for the credit loss, limited by the amount that the fair value is less than the amortized cost basis. Any impairment that has not been recorded through an allowance for credit losses is recognized in other comprehensive income. Changes in the allowance for credit losses are recorded as provision for (or reversal of) credit loss expense. Losses are charged against the allowance when management believes the uncollectability of a security is confirmed or when either of the criteria regarding intent or requirement to sell is met.

Changes in the allowance for credit losses are recorded as provision for (or reversal of) credit losses. Available for sale securities are charged-off against the allowance or, in the absence of any allowance, written down through income when deemed uncollectible by management or when either of the aforementioned criteria regarding intent or requirement to sell is met.

*Allowance for credit losses - held to maturity securities:* The allowance for credit losses on held to maturity securities is a valuation account that is deducted from the amortized cost basis of held to maturity securities to present management's best estimate of the net amount expected to be collected. Held to maturity securities are charged-off against the allowance when deemed uncollectible by management. Adjustments to the allowance are reported in the income statement as a component of provision for credit losses. Management measures expected credit losses on held to maturity securities on a collective basis by major security type with each type sharing similar risk characteristics and considers historical credit loss information that is adjusted for current conditions and reasonable and supportable forecasts along with payment and delinquency history.

Management has made the accounting policy election to exclude accrued interest receivable on available for sale and held to maturity securities from the estimate of credit losses and report accrued interest separately in other assets in the consolidated balance sheet.

Prior to the adoption of ASU 2016-13, declines in the fair value of held-to-maturity and available-for-sale securities below their cost that were deemed to be other than temporary were reflected in earnings as realized losses. In estimating other-than-temporary impairment losses prior to January 1, 2023, management considered, among other things, (i) the length of time and the extent to which the fair value had been less than cost, (ii) the financial condition and near-term prospects of the issuer and (iii) the intent and our ability to retain our investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

*Allowance for credit losses on off-balance sheet credit exposures:* The allowance for credit losses on off-balance sheet credit exposures is a liability account, calculated in accordance with ASC 326, representing expected credit losses over the contractual period for which the Company is exposed to credit risk resulting from a contractual obligation to extend credit. No allowance is recognized if we have the unconditional right to cancel the obligation. The allowance is reported as a component of other liabilities in the consolidated balance sheets. Adjustments to the allowance are reported in the income statement as a component of provision for credit losses. Further information regarding Company policies and methodology used to estimate the allowance for credit losses on off-balance sheet credit exposures is presented in Note 12. Commitments and Contingencies.

## **Premises and Equipment**

Land is carried at cost. Premises and equipment are stated at cost less accumulated depreciation. Buildings and related components are depreciated using the straight-line method with useful lives ranging from 5 to 39 years. Furniture and equipment are depreciated using the straight-line method with useful lives ranging from 3 to 10 years. Land improvements are depreciated using the straight-line method with useful lives ranging from 3 to 10 years. Leasehold improvements are depreciated using the straight-line method over the lease term or estimated life, whichever is shorter. Repair and maintenance costs are expensed as incurred.

We lease certain office facilities and office equipment under operating leases. We also own certain office facilities which we lease to outside parties under operating lessor leases. Under the lease standards, for operating leases other than those considered to be short-term, we recognize lease right-of-use assets and related lease liabilities. Such amounts are reported as components of other assets and other liabilities, respectively, on our accompanying consolidated balance sheet. We do not recognize short-term operating leases on our balance sheet. A short-term operating lease has an original term of 12 months or less and does not have a purchase option that is likely to be exercised.

In recognizing lease right-of-use assets and related lease liabilities, we account for lease and non-lease components (such as taxes, insurance, and common area maintenance costs) separately as such amounts are generally readily determinable under our lease contracts. Lease payments over the expected term are discounted using our incremental borrowing rate referenced to the Federal Home Loan Bank Secure Connect advance rates for borrowings of similar term. We also consider renewal and termination options in the determination of the term of the lease. If it is reasonably certain that a renewal or termination option will be exercised, the effects of such options are included in the determination of the expected lease term. Generally, we cannot be reasonably certain about whether or not we will renew a lease until such time the lease is within the last two years of the existing lease term. However, renewal options related to our regional headquarters facilities or operations centers are evaluated on a case-by-case basis, typically in advance of such time frame. When we are reasonably certain that a renewal option will be exercised, we measure/remeasure the right-of-use asset and related lease liability using the lease payments specified for the renewal period or, if such amounts are unspecified, we generally assume an increase (evaluated on a case-by-case basis in light of prevailing market conditions) in the lease payment over the final period of the existing lease term.

### **Foreclosed Assets**

Assets acquired through or instead of loan foreclosure are held for sale and are initially recorded at fair value less estimated selling costs when acquired, establishing a new cost basis. Costs after acquisition are generally expensed. If the fair value of the asset declines, a write-down is recorded through expense. The valuation of foreclosed assets is subjective in nature and may be adjusted in the future because of changes in economic conditions. The Company had no foreclosed assets at December 31, 2023 and 2022 reported in other real estate in the Company's consolidated balance sheets.

### **Servicing Rights**

The guaranteed portion of certain SBA and USDA loans can be sold into the secondary market. Servicing rights are recognized as separate assets when loans are sold with servicing retained. Servicing rights are amortized in proportion to, and over the period of, estimated future net servicing income. The Company uses industry prepayment statistics in estimating the expected life of the loans. Management evaluates its servicing rights for impairment quarterly. Servicing rights are evaluated for impairment based upon the fair value of the rights as compared to amortized cost. Fair value is determined using discounted future cash flows calculated on a loan-by-loan basis and aggregated by predominant risk characteristics. The initial servicing rights and resulting gain on sale are calculated based on the difference between the actual par and bids on an individual loan basis.

### **Intangible Assets**

Intangible assets consist of goodwill and core deposit intangibles. Goodwill represents the excess purchase price over the fair value of net assets acquired in business acquisitions. The core deposit intangible represents the excess intangible value of acquired deposit customer relationships as determined by valuation specialists. The core deposit intangibles are being amortized over 58 to 100 months on a straight-line basis. Goodwill is not amortized but rather is evaluated for impairment on at least an annual basis or more frequently if management believes indicators of impairment exist. The Company performed its annual impairment test of goodwill and core deposit intangibles during 2023 and 2022, as required by FASB ASC 350, *Intangibles—Goodwill and Other*. The 2023 and 2022 tests indicated no impairment of the Company's goodwill or core deposit intangibles.

### **Stock Based Compensation**

The Company has a share-based employee compensation plan, which is described more fully in Note 11. The Company accounts for its stock-based compensation in accordance with applicable accounting guidance for share-based payments. This guidance requires all share-based payments to be recognized on the consolidated statements of income based on their fair values. Compensation costs for awards with graded vesting are recognized on a straight-line basis over the vesting period.

### **Advertising Costs**

Advertising costs are expensed as incurred. Advertising costs totaled \$558,000 and \$475,000 for the years ended December 31, 2023 and 2022, respectively, and are included in other expense on the consolidated statements of income.

## **Income Taxes**

The Company accounts for income taxes utilizing the asset and liability method. Under this method, deferred tax assets and liabilities are recognized for future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using the enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

The Company accounts for uncertainties in income taxes in accordance with current accounting guidance which prescribes a recognition threshold and a measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. Benefits from tax positions should be recognized in the financial statements only when it is more likely than not that the tax position will be sustained upon examination by the appropriate taxing authority that would have 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 should be recognized in the first subsequent financial reporting period in which that threshold is met. Previously recognized tax positions that no longer meet the more-likely-than-not recognition threshold should be derecognized in the first subsequent financial reporting period in which that threshold is no longer met. No uncertain tax positions have been recognized.

The Company files a consolidated income tax return with our subsidiaries. Federal income tax expense or benefit has been allocated to subsidiaries on a separate return basis.

## **Comprehensive Income**

Comprehensive income consists of net income and other comprehensive income (loss). Other comprehensive income (loss) includes net unrealized gains and losses on available for sale securities, which are recognized as a separate component of equity. Comprehensive income for the years ended December 31, 2023 and 2022 is reported in the accompanying consolidated statements of comprehensive income.

## **Transfer of Financial Assets**

Transfers of financial assets are accounted for as sales when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (i) the assets have been isolated from the Company, (ii) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (iii) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity. Transfer of financial assets are comprised of the guaranteed portion of SBA and USDA loans which have been sold.

## **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.

## **Fair Value of Financial Instruments**

Fair values of financial instruments are estimated using relevant market information and other assumptions, as more fully disclosed in Note 16. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments, and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect the estimates.

## **Revenue Recognition**

The Company recognizes revenue in accordance with FASB ASC 606, *Revenue from Contracts with Customers* ("Topic 606"). Topic 606 establishes principles for reporting information about the nature, amount, timing and uncertainty of revenue and cash flows arising from the entity's contracts to provide goods or services to customers. The core principle requires an entity to recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration that it expects to be entitled to receive in exchange for those goods or services recognized as performance obligations are satisfied.



The Company derives a portion of its revenue from loan and investment income which are specifically excluded from the scope of this standard. Of the Company's remaining sources of income, substantially all sources of banking revenue are recognized either by transaction (ATM, interchange, wire transfer, etc.) or when the Company charges a customer for a service that has already been rendered (monthly service charges, account fees, monthly trust management fees, monthly premise rental income, etc.). Payment for such performance obligations are generally received at the time the performance obligations are satisfied. Other non-interest income primarily includes items such as gains on the sale of loans held for sale and servicing fees, none of which are subject to the requirements of Topic 606.

The scope of ASC 606 focuses on revenue from contracts with customers, which includes fees from asset management services and commission income and fees and commissions from investment banking services, as well as fees earned by the Bank's Nolan division for their third party administration services. These items make up the majority of the non-interest income on our income statement. Under Topic 606, the recognition and measurement of revenue is based on the assessment of individual contract terms. Significant judgment is required to determine whether performance obligations are satisfied at a point in time or over time; how to allocate transaction prices where multiple performance obligations are identified; when to recognize revenue based on the appropriate measure of the Company's progress under the related agreement; and whether constraints on variable consideration should be applied due to uncertain future events.

#### **Advisory Fees**

*Investment advisory fees:* The Company provides investment advisory services on a daily basis. The Company believes the performance obligation for providing advisory services is satisfied over time because the customer is receiving and consuming the benefits as they are provided by the Company. For the majority of accounts, fee arrangements are based on a percentage applied to the customer's assets under management. Fees calculated in this manner are generally received monthly or quarterly and are recognized as revenue ratably over the period as they relate specifically to the services provided in that period, which are distinct from the services provided in other periods.

*Performance fees:* The Company receives fees under certain of its agreements which vary based on specified performance measures, for example, when a separate account exceeds a specified benchmark or contractual hurdle over a contractual performance period. These performance fees may be paid in addition to standard investment advisory fees. Currently, most of the Company's contracts of this nature specify an annual performance period. These fees are earned once account returns have exceeded these specified performance measures for the performance period, and are calculated as a percentage of account returns. These performance fees are considered variable consideration as the uncertainty is dependent on the value of the assets at future points in time as well as meeting a specified hurdle rate, both of which are highly susceptible to factors outside the Company's influence. Revenues are recognized in the last period of the performance period specified in the respective contract since this is the point at which the Company can conclude that a significant reversal will not occur.

*Other advisory fees:* The Company provides general advisory services on an ongoing basis, which may include: operational advice, advice to management on strategic and other initiatives and/or advice on prospective mergers and acquisitions. Revenue is recognized over time for these advisory arrangements, given that under the relevant agreements, the performance obligations are simultaneously provided by the Company and consumed by the customer.

#### **Commissions**

*Brokerage commissions:* The Company buys and sells securities on behalf of its customers through its arrangements with its clearing firm. Each time a customer enters into a buy or sell transaction, the Company charges a commission. Commissions and clearing expenses are recorded each month based upon the trade date, which is the date that the Company fills the trade order by finding and contracting with a counterparty and confirms the trade with the customer. The Company believes that the performance obligation is satisfied on the trade date because that is when the underlying financial instrument or purchaser is identified, the pricing is agreed upon and the risks and rewards of ownership have been transferred to/from the customer.

*Syndication and private placement commissions:* The Company participates in the syndication of public securities offerings and in private placement offerings for business entities that want to raise funds through a sale of securities. With respect to public securities offerings, the Company may make a commitment to acquire securities from the issuer, or the Company may participate in the syndication group on a best efforts, non-committed basis. With respect to private placement offerings, the performance obligation is the consummation of the sale of securities of the issuer, typically on a "best efforts" basis. Revenues are earned from fees arising from these securities offerings, and are recognized when the performance obligation is satisfied, generally the trade date. The Company believes that the trade date is the appropriate point in time to recognize revenue for these securities transactions as there are no significant actions which the Company needs to take subsequent to this date and the issuer obtains the control and benefit of the capital markets offering at that point.

## Accounting Changes, Reclassifications and Restatements

Certain items in prior financial statements have been reclassified to conform to the current presentation but have no effect on the reported results of operations.

## Earnings per Share

Basic earnings per share is computed based on the weighted-average number of shares outstanding during each year. Diluted earnings per share is computed using the weighted-average shares and all potential dilutive shares outstanding during the period. The following table sets forth the computation of basic and diluted earnings per share ("EPS") for the following periods:

(In thousands, except per share data)	Years ended December 31,	
	2023	2022
Net income available to common shareholders	\$ 13,667	\$ 15,478
Weighted average shares outstanding	7,057	7,062
Effect of dilutive shares	236	274
Weighted average diluted shares outstanding	7,293	7,336
Basic earnings per share	\$ 1.94	\$ 2.19
Diluted earnings per share	\$ 1.87	\$ 2.11

As of December 31, 2023, options to purchase 167,500 shares of common stock, with a weighted average exercise price of \$5.51, were included in the computation of diluted net earnings per share. In addition, as of December 31, 2022, 170,000 shares of restricted stock grants with a grant date fair value of \$4.81 per share which vest from 2023 through 2025 were included in the diluted earnings per share calculation.

## Note 2. Securities

A summary of amortized cost and cost and fair value of securities is presented below.

(In thousands)	December 31, 2023			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
<b>Securities available for sale:</b>				
U.S. Treasuries	\$ 3,906	\$ -	\$ 12	\$ 3,894
U.S government agencies	15,644	-	2,017	13,627
Mortgage-backed securities	5,731	-	275	5,456
Total securities available for sale	<u>\$ 25,281</u>	<u>\$ -</u>	<u>\$ 2,304</u>	<u>\$ 22,977</u>
<b>Securities held to maturity:</b>				
Property assessed clean energy	\$ 1,326	\$ -	\$ 72	\$ 1,254
Public improvement district/tax increment reinvestment zone	22,868	592	865	22,595
Total securities held to maturity	<u>\$ 24,194</u>	<u>\$ 592</u>	<u>\$ 937</u>	<u>\$ 23,849</u>
<b>Securities, restricted:</b>				
Other	<u>\$ 4,176</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 4,176</u>

	December 31, 2022			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
<b>(In thousands)</b>				
<b>Securities available for sale:</b>				
U.S. Treasuries	\$ 1,990	\$ -	\$ 37	\$ 1,953
U.S government agencies	15,715	-	2,627	13,088
Mortgage-backed securities	5,925	-	333	5,592
Total securities available for sale	<u>\$ 23,630</u>	<u>\$ -</u>	<u>\$ 2,997</u>	<u>\$ 20,633</u>
<b>Securities held to maturity:</b>				
Property assessed clean energy	\$ 1,596	\$ 126	\$ -	\$ 1,722
Public improvement district/tax increment reinvestment zone	23,666	1,137	43	24,760
Total securities held to maturity	<u>\$ 25,262</u>	<u>\$ 1,263</u>	<u>\$ 43</u>	<u>\$ 26,482</u>
<b>Securities, restricted:</b>				
Other	<u>\$ 3,496</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 3,496</u>
<b>Securities not readily marketable</b>	<u>\$ 100</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 100</u>

Securities available for sale consist of U.S. government agency securities and mortgage-backed securities guaranteed by U.S. government agencies. Securities held to maturity consist of Property Assessed Clean Energy (“PACE”) and Public Improvement District/Tax Increment Reinvestment Zone (“PID/TIRZ”) investments. These investment contracts or bonds located in Texas, California and Florida, originate under a contractual obligation between the property owners, the local county or city administration, and a third-party administrator and sponsor. PACE assessments are created to fund the purchase and installation of energy saving improvements to the property such as solar panels. PID/TIRZ assessments are used to pay for the development costs of a residential subdivision. Generally, as a property assessment, the total assessment is repaid in installments over a period of 5 to 32 years by the then current property owner(s). Each installment is collected by the County or City Tax Collector where the property is located. The assessments are an obligation of the property. Securities, restricted consist of Federal Reserve Bank of Dallas (“FRB”) and Federal Home Loan Bank of Dallas (“FHLB”) stock, which are carried at cost.

As of December 31, 2023 and 2022, securities available for sale with a fair value of \$988,000 and \$94,000, respectively, were pledged against trust deposit balances held at the Bank. During March 2023, the Board of Governors of the Federal Reserve System (the “Federal Reserve”) created the Bank Term Funding Program (“BTFP”), which was made available to banks in response to liquidity concerns in the United States banking system. The BTFP allows the whole par value of available for sale securities to be included as the collateral value. As of December 31, 2023, securities with a par value of \$23.3 million were pledged to the Federal Reserve under the BTFP, which \$21.0 million was borrowed against. As of December 31, 2023 and 2022, there were no securities pledged to secure borrowings at the FHLB.

As of December 31, 2023 and 2022, the Bank held FRB stock in the amount of \$2.2 million. The Bank held FHLB stock in the amount of \$2.0 million and \$1.3 million as of December 31, 2023 and 2022, all of which were classified as restricted securities.

As of December 31, 2022, the Company held an income interest in a private investment, which was not readily marketable, accounted for under the cost less impairment method in the amount \$100,000. The interest terminated under the terms of the private investment during the last quarter of 2023, and the Company recorded a \$100,000 loss on disposition of securities not readily marketable. No allowance for impairment was recorded during 2023 or 2022.

The table below indicates the length of time individual investment securities have been in a continuous loss position as of December 31, 2023:

(In thousands)	December 31, 2023					
	Less than 12 months		12 months or longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
<b>Securities available for sale:</b>						
U.S. Treasuries	\$ 988	\$ 3	\$ 990	\$ 9	\$ 1,978	\$ 12
U.S. government agencies	-	-	13,627	2,017	13,627	2,017
Mortgage-backed securities	1,022	4	4,434	271	5,456	275
Total	<u>\$ 2,010</u>	<u>\$ 7</u>	<u>\$ 19,051</u>	<u>\$ 2,297</u>	<u>\$ 21,061</u>	<u>\$ 2,304</u>

Beginning January 1, 2023, the Company evaluates all securities quarterly to determine if any debt securities in a loss position require an allowance for credit losses in accordance with ASC 326. The Company had a total of twenty-three (23) investment positions in the unrealized loss position as of December 31, 2023.

As of December 31, 2023, no allowance for credit losses has been recognized on available for sale and held to maturity securities in an unrealized loss position as management does not believe any of the securities are impaired due to reasons of credit quality. This is based upon our analysis of the underlying risk characteristics, including credit ratings, and other qualitative factors related to our securities and in consideration of our historical credit loss experience and internal forecasts, along with current payment history and no delinquent payments as of December 31, 2023. The issuers of these securities are U.S. government agencies who continue to make timely principal and interest payments under the contractual terms of the securities. Furthermore, management does not have the intent to sell any of the securities classified as available for sale in the table above and believes that it is more likely than not that we will not have to sell any such securities before a recovery of cost. The unrealized losses are due to increases in market interest rates over the yields available at the time the underlying securities were purchased. The fair value is expected to recover as the securities approach their maturity date or repricing date or if market yields for such investments decline.

The amortized cost and estimated fair value of securities as of December 31, 2023, are presented below by contractual maturity. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations. Residential mortgage-backed securities are shown separately since they are not due at a single maturity date.

(In thousands)	Available for Sale		Held to Maturity	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Due in one year or less	\$ 3,906	\$ 3,894	\$ -	\$ -
Due after one year through five years	11,997	10,758	1,431	1,476
Due after five years through ten years	86	82	367	343
Due after ten years	3,561	2,787	22,396	22,030
Mortgage-backed securities	5,731	5,456	-	-
Total	<u>\$ 25,281</u>	<u>\$ 22,977</u>	<u>\$ 24,194</u>	<u>\$ 23,849</u>

**Note 3. Loans and Allowance for Credit Losses on Loans**

Major classifications of loans held for investment are as follows:

(In thousands)	December 31, 2023	December 31, 2022
Commercial and industrial	\$ 82,483	\$ 92,946
Consumer installment	900	1,058
Real estate – residential	8,181	5,566
Real estate – commercial	68,792	63,924
Real estate – construction and land	44,663	3,873
SBA:		
SBA 7(a) guaranteed	162,144	149,374
SBA 7(a) unguaranteed	64,858	56,268
SBA 504	41,906	52,668
USDA	2,124	2,235
Factored receivables	25,044	22,420
Gross loans	501,095	450,332
Less:		
Allowance for credit losses	6,308	4,513
Net loans	<u>\$ 494,787</u>	<u>\$ 445,819</u>

As of December 31, 2023, our loan portfolio included \$78.2 million of loans, approximately 15.6% of our total funded loans to the dental industry, as compared to \$83.9 million of loans, approximately 18.6% of our total funded loans at December 31, 2022. The Bank believes that these loans are to credit worthy borrowers and are diversified geographically.

Accrued interest receivable on loans totaled \$3.1 million and \$2.2 million at December 31, 2023 and 2022, respectively, and is included in other assets in the Company's consolidated balance sheets.

The Company serves the small business community by offering loans promulgated under the SBA's 7(a) and 504 loan programs, and loans guaranteed by the USDA. SBA 7(a) and USDA loans are typically guaranteed by each agency in amounts ranging from 75% to 80% of the principal balance. For SBA construction loans, the Company records the guaranteed funded portion of the loans as held for sale. When the SBA loans are fully funded, the Company may sell the guaranteed portion into the secondary market, on a servicing-retained basis, or reclassify from loans held for sale to loans held for investment if the Company determines that holding these loans provide better long-term risk adjusted returns than selling the loans. In calculating gain on the sale of loans, the Company performs an allocation based on the relative fair values of the sold portion and retained portion of the loan. The Company's assumptions are validated by reference to external market information.

The Company had \$26.6 million and \$33.9 million of SBA/USDA loans held for sale as of December 31, 2023 and December 31, 2022, respectively. The Company sold the guaranteed portion of one USDA loan totaling \$5.8 million, resulting in a gain on sale loans of \$581,000 for the year ended December 31, 2023. There were no loans sold for the year ended December 31, 2022. The Company elected to reclassify \$52.6 million and \$55.4 million, respectively, of the SBA 7(a) loans held for sale to loans held for investment during the years ended December 31, 2023 and 2022.

**Loan Origination/Risk Management.**

The Company maintains written loan origination policies, procedures, and processes which address credit quality at several levels including individual loan level, loan type, and loan portfolio levels.

Commercial and industrial loans, which are predominantly loans to dentists, are underwritten based on historical and projected income of the business and individual borrowers and guarantors. The Company utilizes a comprehensive global debt service coverage analysis to determine debt service coverage ratios. This analysis compares global cash flow of the borrowers and guarantors on an individual credit to existing and proposed debt after consideration of personal and business related other expenses. Collateral is generally a lien on all available assets of the business borrower including intangible assets. Credit worthiness of individual borrowers and guarantors is established through the use of credit reports and credit scores.

Consumer loans are evaluated on the basis of credit worthiness as established through the use of credit reports and credit scores. Additional credit quality indicators include borrower debt to income ratios based on verifiable income sources.

Real estate mortgage loans are evaluated based on collateral value as well as global debt service coverage ratios based on historical and projected income from all related sources including the collateral property, the borrower, and all guarantors where applicable.

The Company originates SBA loans which are sometimes sold into the secondary market. The Company continues to service these loans after sale and is required under the SBA programs to retain specified amounts. The two primary SBA loan programs that the Company offers are the basic 7(a) loan guaranty program and the 504 loan program in conjunction with junior lien financing from a Certified Development Company ("CDC"). The SBA has designated the Bank as a "Preferred Lender." As an SBA Preferred Lender, the Bank has been delegated loan approval, closing and most servicing and liquidation authority from the SBA.

The 7(a) program serves as the SBA's primary business loan program to help qualified small businesses obtain financing when they might not be eligible for business loans through normal lending channels. Loan proceeds under this program can be used for most business purposes including working capital, machinery and equipment, furniture and fixtures, land and building (including purchase, renovation and new construction), leasehold improvements and debt refinancing. Loan maturity is generally up to 10 years for non-real estate collateral and up to 25 years for real estate collateral. The 7(a) loan is approved and funded by a qualified lender, partially guaranteed by the SBA and subject to applicable regulations. In general, the SBA guarantees up to 75% of the loan amount depending on loan size. The Company is required by the SBA to service the loan and retain a contractual minimum of 5% on all SBA 7(a) loans, but generally retains 25% (the unguaranteed portion). The servicing spread is 1% of the guaranteed portion of the loan that is sold in the secondary market.

The 504 program is an economic development-financing program providing long-term, low down payment loans to businesses. Typically, a 504 project includes a loan secured from a private-sector lender with a senior lien, a loan secured from a CDC (funded by a 100% SBA-guaranteed debenture) with a junior lien covering up to 40% of the total cost, and a contribution of at least 10% equity from the borrower. Debenture limits are \$5.0 million for regular 504 loans and \$5.5 million for those 504 loans that meet a public policy goal.

The Company also offers Business & Industry ("B&I") program loans through the USDA. These loans are similar to the SBA product, except they are guaranteed by the USDA. The guaranteed amount is generally 80%. B&I loans are made to businesses in designated rural areas and are generally larger loans to larger businesses than the SBA 7(a) loans. Similar to the SBA 7(a) product, they can be sold into the secondary market. These loans can be utilized for rural commercial real estate and equipment. The loans can have maturities up to 30 years and the rates can be fixed or variable.

Construction and land development loans are evaluated based on the borrower's and guarantor's credit worthiness, past experience in the industry, track record and experience with the type of project being considered, and other factors. Collateral value is determined generally by independent appraisal utilizing multiple approaches to determine value based on property type.

The Bank engages in third-party factoring of certain business' accounts receivable invoices. The Bank's factoring clients are primarily in the transportation industry. Each account debtor is credit qualified, confirming credit worthiness and stability, because the underlying debtor represents the substantive underlying credit risk. Some factored receivables are full recourse to and personally guaranteed by the factoring client. In such cases, the client is credit qualified under specific policy guidelines. Concentration limits are set and monitored for aggregate factored receivables, account debtors, and individual factoring clients. In addition, we consider the overall state of each specific industry, primarily over-the-road trucking, in our evaluation of the credit worthiness of the factoring client and the underlying debtor.

For all loan types, the Company establishes guidelines for its underwriting criteria including collateral coverage ratios, global debt service coverage ratios, and maximum amortization or loan maturity terms.

At the portfolio level, the Company monitors concentrations of loans based on several criteria including loan type, collateral type, industry, geography, and other factors. The Company also performs periodic market research and economic analysis at a local geographic and national level. Based on this research, the Company may from time to time change the minimum or benchmark underwriting criteria applied to the above loan types.

Loans are placed on non-accrual status when, in management's opinion, the borrower may be unable to meet payment obligations as they become due, as well as when required by regulatory provisions. Loans may be placed on non-accrual status regardless of whether or not such loans are considered past due. When interest accrual is discontinued, all unpaid accrued interest is reversed. A loan may be returned to accrual status when all the principal and interest amounts contractually due are brought current and future principal and interest amounts contractually due are reasonably assured, which is typically evidenced by a sustained period of repayment performance by the borrower.

Year-end non-accrual loans, segregated by class of loans, were as follows:

	December 31, 2023		December 31, 2022
	Total Non-Accrual	Non-Accrual with No Credit Loss Allowance	Total Non-Accrual
(In thousands)			
Real estate - commercial	\$ 221	\$ 221	\$ 138
SBA guaranteed	1,951	1,951	2,221
SBA unguaranteed	251	251	107
Total	\$ 2,423	\$ 2,423	\$ 2,466

The Company recognized \$19,000 of interest income on non-accrual loans during the year ended December 31, 2023, and did not recognize any interest income on non-accrual loans during the year ended December 31, 2022.

From time to time, we may modify certain loans to borrowers who are experiencing financial difficulty. In some cases, these modifications may result in new loans. Loan modifications to borrowers experiencing financial difficulty may be in the form of a principal forgiveness, an interest rate reduction, an other-than-insignificant payment delay, or a term extension or a combination thereof, among other things. As of December 31, 2023, the period-end balance of loan modifications to borrowers experiencing financial difficulty included a SBA loan with an outstanding balance of \$1.1 million to temporarily reduce the interest rate and a SBA loan with an outstanding balance of \$2.4 million to temporarily lower the monthly payment amounts. These loans were current as of December 31, 2023, and there were no commitments to lend additional funds to these borrowers at December 31, 2023.

Under ASC 326, the allowance for credit losses is a valuation account that is deducted from the amortized cost basis of loans to present the net amount expected to be collected on the loans. Loans, or portions thereof, are charged-off against the allowance when they are deemed uncollectible. The Company's allowance for credit losses for loans consists of two components: (1) a specific valuation allowance based on probable losses on specifically identified loans and (2) a general valuation allowance based on historical credit loss experience, general economic conditions and other qualitative risk factors both internal and external to the Company.

The Company uses the open pool life method to estimate expected losses for all of the Company's loan pools. The loan portfolio pools were selected in order to generally align with the loan categories specified in the quarterly call reports required to be filed with the Federal Financial Institutions Examination Council, except for the dental, SBA and USDA loans, are segregated in separate pools.

Loans that do not share risk characteristics are evaluated on an individual basis and are not included in the collective evaluation. In setting the specific valuation allowance, the Company follows a loan review program to evaluate the credit risk in the total loan portfolio and assigns risk grades to each loan. Through this loan review process, the Company maintains an internal list of impaired loans, which along with the delinquency list of loans, helps management assess the overall quality of the loan portfolio and the adequacy of the allowance for credit losses. All loans that have been identified as impaired are reviewed on a quarterly basis in order to determine whether a specific reserve is required. For certain impaired loans, the Company allocates a specific reserve primarily based on the value of the collateral securing the loan or when the discounted cash flows for the loan is lower than the carrying value of that loan. A loan is considered to be collateral dependent when, based upon management's assessment, the borrower is experiencing financial difficulty and repayment is expected to be provided substantially through the operation or sale of the collateral. In such cases, expected credit losses are based on the fair value of the collateral at the measurement date, adjusted for estimated selling costs if satisfaction of the loan depends on the sale of the collateral. We reevaluate the fair value of collateral supporting collateral dependent loans on a quarterly basis.

In determining the amount of the general valuation allowance, management considers factors such as historical lifetime credit loss experience, concentration risk of specific loan types, the volume, growth and composition of the Company's loan portfolio, current economic conditions and reasonable and supportable forecasted economic conditions that may affect the borrower's ability to pay and the value of collateral, the evaluation of the Company's loan portfolio through its internal loan review process, general economic conditions and other qualitative risk factors both internal and external to the Company and other relevant factors in accordance with ASC Topic 326, "*Financial Instruments – Credit Losses*." Historical lifetime credit loss experience is determined by utilizing an open-pool ("cumulative loss rate") methodology. Adjustments to the historical lifetime credit loss experience are made for differences in current loan pool risk characteristics such as portfolio concentrations, delinquency, non-accrual, and watch list levels, as well as changes in current and forecasted economic conditions such as unemployment rates, property and collateral values, and other indices relating to economic activity. The utilization of reasonable and supportable forecasts includes an immediate reversion to lifetime historical loss rates. For all loan pools, management has determined two years represents a reasonable and supportable forecast period and reverts to a historical loss rate over two years on a straight-line basis. Based on a review of these factors for each loan type, the Company applies an estimated percentage to the outstanding balance of each loan type, excluding any loan that has a specific reserve allocated to it. Allocation of a portion of the allowance to one category of loans does not preclude its availability to absorb losses in other categories.



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Management estimates the allowance balance using relevant available information, from internal and external sources, relating to past events, current conditions, and reasonable and supportable forecasts. Historical credit loss experience provides the basis for the estimation of expected credit losses. Adjustments to historical loss information are made for differences in current loan-specific risk characteristics.

The following table presents the amortized cost basis of collateral-dependent loans by class of loans as of December 31, 2023:

(In thousands)		Residential Real Estate
Real estate – residential	\$	221
SBA unguaranteed		251
Total	\$	472

Prior to the adoption of ASC 326, loans were considered impaired when, based on current information and events, it is probable the Company will be unable to collect all amounts due in accordance with the original contractual terms of the loan agreement, including scheduled principal and interest payments. If a loan is impaired, a specific valuation allowance was allocated, if necessary, so that the loan was reported net, at the present value of estimated future cash flows using the loan's existing rate or at the fair value of collateral if repayment is expected solely from the collateral. Interest payments on impaired loans are typically applied to principal unless collectability of the principal amount is reasonably assured, in which case interest is recognized on a cash basis. Impaired loans, or portions thereof, are charged off when deemed uncollectible.

The Company's impaired loans and related allowance is summarized in the following table as of December 31, 2022:

(In thousands)	Unpaid Contractual Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment	Interest Income Recognized
						Year Ended December	
						31, 2022	
Commercial and industrial	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 181	\$ -
SBA	2,759	2,126	-	2,126	-	2,287	-
Total	\$ 2,759	\$ 2,126	\$ -	\$ 2,126	\$ -	\$ 2,468	\$ -

Loans are considered past due if the required principal and interest payments have not been received as of the date such payments were due. The Company's past due loans (including both accruing and non-accruing loans) are as follows:

	30-89 Days Past Due	90 Days or More Past Due	Total Past Due	Total Current	Total Loans	Total 90 Days Past Due Still Accruing
(In thousands)						
December 31, 2023						
Commercial and industrial	\$ 30	\$ -	\$ 30	\$ 82,453	\$ 82,483	\$ -
Consumer installment	-	-	-	900	900	-
Real estate – residential	93	-	93	8,088	8,181	-
Real estate – commercial	-	-	-	68,792	68,792	-
Real estate – construction and land	-	-	-	44,663	44,663	-
SBA	-	1,167	1,167	267,741	268,908	-
USDA	-	-	-	2,124	2,124	-
Factored receivables	879	147	1,026	24,018	25,044	147
Total	<u>\$ 1,002</u>	<u>\$ 1,314</u>	<u>\$ 2,316</u>	<u>\$ 498,779</u>	<u>\$ 501,095</u>	<u>\$ 147</u>
December 31, 2022						
Commercial and industrial	\$ 395	\$ -	\$ 395	\$ 92,551	\$ 92,946	\$ -
Consumer installment	-	-	-	1,058	1,058	-
Real estate – residential	138	-	138	5,428	5,566	-
Real estate – commercial	-	206	206	63,718	63,924	206
Real estate – construction and land	-	-	-	3,873	3,873	-
SBA	-	2,327	2,327	255,983	258,310	-
USDA	-	-	-	2,235	2,235	-
Factored receivables	966	132	1,098	21,322	22,420	132
Total	<u>\$ 1,499</u>	<u>\$ 2,665</u>	<u>\$ 4,164</u>	<u>\$ 446,168</u>	<u>\$ 450,332</u>	<u>\$ 338</u>

As part of the on-going monitoring of the credit quality of the Company's loan portfolio, management tracks certain credit quality indicators including internal credit risk based on past experiences as well as external statistics and factors. Loans are graded in one of six categories: (i) pass, (ii) pass-watch, (iii) special mention, (iv) substandard, (v) doubtful, or (vi) loss. Loans graded as loss are charged-off.

The classifications of loans reflect a judgment about the risks of default and loss associated with the loan. The Company reviews the ratings on credits quarterly. No significant changes were made to the loan risk grading system definitions and allowance for credit loss methodology during the past year. Ratings are adjusted to reflect the degree of risk and loss that is felt to be inherent in each credit. The Company's methodology is structured so that specific allocations are increased in accordance with deterioration in credit quality (and a corresponding increase in risk and loss) or decreased in accordance with improvement in credit quality (and a corresponding decrease in risk and loss).

Credits rated pass are acceptable loans, appropriately underwritten, bearing an ordinary risk of loss to the Company. Loans in this category are loans to highly credit worthy borrowers with financial statements presenting a good primary source as well as an adequate secondary source of repayment.

Credits rated pass-watch loans have been determined to require enhanced monitoring for potential weaknesses which require further investigation. They have no significant delinquency in the past twelve months. This rating causes the loan to be actively monitored with greater frequency than pass loans and allows appropriate downgrade transition if verifiable adverse events are confirmed. This category may also include loans that have improved in credit quality from special mention but are not yet considered pass loans.

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

Credits rated substandard are those in which the normal repayment of principal and interest may be, or has been, jeopardized by reason of adverse trends or developments of a financial, managerial, economic or political nature, or important weaknesses exist in collateral. A protracted workout on these credits is a distinct possibility. Prompt corrective action is therefore required to strengthen the Company's position, and/or to reduce exposure and to assure that adequate remedial measures are taken by the borrower. Credit exposure becomes more likely in such credits and a serious evaluation of the secondary support to the credit is performed. Guaranteed portions of SBA loans graded substandard are generally on non-accrual due to the limited amount of interest covered by the guarantee, usually 60 days maximum. However, there typically will be no exposure to loss on the principal amount of these guaranteed portions of the loan.

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

Loans classified loss are considered uncollectible and of such little value that their continuance as bankable assets is not warranted. This classification does not mean that the loan has absolutely no recovery or salvage value, but rather that it is not practical or desirable to defer writing off this asset even though partial recovery may be affected in the future.

The following table summarizes the amortized cost basis of loans by year of origination, internal ratings, and gross write-offs by year of origination as of December 31, 2023:

	Term Loans by Origination Year							
(In thousands)	2023	2022	2021	2020	2019	Prior	Revolving Loans	Total
<b>Commercial and industrial</b>								
Pass	\$ 14,632	\$ 23,938	\$ 16,625	\$ 7,769	\$ 5,229	\$ 9,289	\$ 1,847	\$ 79,329
Pass-watch	-	604	343	231	-	-	-	1,178
Special mention	-	-	-	-	-	-	-	-
Substandard	-	-	-	115	-	1,768	-	1,883
Doubtful	-	-	-	93	-	-	-	93
Total	\$ 14,632	\$ 24,542	\$ 16,968	\$ 8,208	\$ 5,229	\$ 11,057	\$ 1,847	\$ 82,483
Current period gross write-offs	\$ -	\$ 214	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 214
<b>Consumer installment</b>								
Pass	\$ 275	\$ 128	\$ 188	\$ 52	\$ 94	\$ 93	\$ 70	\$ 900
Pass-watch	-	-	-	-	-	-	-	-
Special mention	-	-	-	-	-	-	-	-
Substandard	-	-	-	-	-	-	-	-
Doubtful	-	-	-	-	-	-	-	-
Total	\$ 275	\$ 128	\$ 188	\$ 52	\$ 94	\$ 93	\$ 70	\$ 900
Current period gross write-offs	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
<b>Real estate-- residential</b>								
Pass	\$ 470	\$ 4,679	\$ 1,944	\$ 754	\$ -	\$ 207	\$ -	\$ 8,054
Pass-watch	-	-	-	-	-	-	-	-
Special mention	-	-	-	-	-	-	-	-
Substandard	-	-	-	-	-	127	-	127
Doubtful	-	-	-	-	-	-	-	-
Total	\$ 470	\$ 4,679	\$ 1,944	\$ 754	\$ -	\$ 334	\$ -	\$ 8,181
Current period gross write-offs	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
<b>Real estate-- commercial</b>								
Pass	\$ 13,330	\$ 10,920	\$ 18,970	\$ 4,917	\$ 8,937	\$ 11,718	\$ -	\$ 68,792
Pass-watch	-	-	-	-	-	-	-	-
Special mention	-	-	-	-	-	-	-	-
Substandard	-	-	-	-	-	-	-	-
Doubtful	-	-	-	-	-	-	-	-
Total	\$ 13,330	\$ 10,920	\$ 18,970	\$ 4,917	\$ 8,937	\$ 11,718	\$ -	\$ 68,792
Current period gross write-offs	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
<b>Real estate -- construction/land</b>								
Pass	\$ 21,358	\$ 23,305	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 44,663
Pass-watch	-	-	-	-	-	-	-	-
Special mention	-	-	-	-	-	-	-	-
Substandard	-	-	-	-	-	-	-	-
Doubtful	-	-	-	-	-	-	-	-
Total	\$ 21,358	\$ 23,305	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 44,663
Current period gross write-offs	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
<b>SBA 7a</b>								
Pass	\$ 40,937	\$ 47,509	\$ 49,245	\$ 14,946	\$ 12,782	\$ 22,533	\$ -	\$ 187,952
Pass-watch	749	3,209	9,343	7,137	5,267	5,704	-	31,409
Special mention	-	127	576	1,364	1,217	2,550	-	5,834
Substandard	-	466	-	129	356	800	-	1,751
Doubtful	-	-	-	-	-	-	-	-
Loss	-	-	-	-	-	56	-	56
Total	\$ 41,686	\$ 51,311	\$ 59,164	\$ 23,576	\$ 19,622	\$ 31,643	\$ -	\$ 227,002
Current period gross write-offs	\$ -	\$ -	\$ -	\$ -	\$ 58	\$ 270	\$ -	\$ 328
<b>SBA 504</b>								
Pass	\$ 4,186	\$ 7,235	\$ 6,755	\$ 7,512	\$ 6,610	\$ 9,608	\$ -	\$ 41,906
Pass-watch	-	-	-	-	-	-	-	-
Special mention	-	-	-	-	-	-	-	-
Substandard	-	-	-	-	-	-	-	-
Doubtful	-	-	-	-	-	-	-	-
Total	\$ 4,186	\$ 7,235	\$ 6,755	\$ 7,512	\$ 6,610	\$ 9,608	\$ -	\$ 41,906
Current period gross write-offs	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -

(In thousands)	Term Loans by Origination Year						Revolving Loans	Total
	2023	2022	2021	2020	2019	Prior		
<b>USDA</b>								
Pass	\$ -	\$ 1,320	\$ -	\$ -	\$ -	\$ 804	\$ -	\$ 2,124
Pass-watch	-	-	-	-	-	-	-	-
Special mention	-	-	-	-	-	-	-	-
Substandard	-	-	-	-	-	-	-	-
Doubtful	-	-	-	-	-	-	-	-
Total	\$ -	\$ 1,320	\$ -	\$ -	\$ -	\$ 804	\$ -	\$ 2,124
Current period gross write-offs	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
<b>Factored Receivables</b>								
Pass	\$ 25,044	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 25,044
Pass-watch	-	-	-	-	-	-	-	-
Special mention	-	-	-	-	-	-	-	-
Substandard	-	-	-	-	-	-	-	-
Doubtful	-	-	-	-	-	-	-	-
Total	\$ 25,044	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 25,044
Current period gross write-offs	\$ 510	\$ 128	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 638
<b>Total</b>								
Pass	\$ 120,232	\$ 119,034	\$ 93,727	\$ 35,950	\$ 33,652	\$ 54,252	\$ 1,917	\$ 458,764
Pass-watch	749	3,813	9,686	7,368	5,267	5,704	-	32,587
Special mention	-	127	576	1,364	1,217	2,550	-	5,834
Substandard	-	466	-	244	356	2,695	-	3,761
Doubtful	-	-	-	93	-	-	-	93
Loss	-	-	-	-	-	56	-	56
Total	\$ 120,981	\$ 123,440	\$ 103,989	\$ 45,019	\$ 40,492	\$ 65,257	\$ 1,917	\$ 501,095
Current period gross write-offs	\$ 510	\$ 342	\$ -	\$ -	\$ 58	\$ 270	\$ -	\$ 1,180

The following table summarizes the Company's internal ratings of its loans in accordance with previously applicable incurred loss model under GAAP as of December 31, 2022:

(In thousands)	Pass	Pass- Watch	Special Mention	Substandard	Doubtful	Total
Commercial and industrial	\$ 92,551	\$ 395	\$ -	\$ -	\$ -	\$ 92,946
Consumer installment	1,058	-	-	-	-	1,058
Real estate – residential	5,428	-	-	138	-	5,566
Real estate – commercial	63,718	-	-	206	-	63,924
Real estate – construction and land	3,873	-	-	-	-	3,873
SBA	231,914	20,665	4,778	953	-	258,310
USDA	2,235	-	-	-	-	2,235
Factored receivables	22,420	-	-	-	-	22,420
Total	\$ 423,197	\$ 21,060	\$ 4,778	\$ 1,297	\$ -	\$ 450,332

The following table details activity in the allowance for credit losses on loans by portfolio segment for year ended December 31, 2023 and 2022.

(In thousands)	Commercial and Industrial	Consumer Installment	Real Estate Residential	Real Estate Commercial	Real Estate Construction and Land	SBA	USDA	Factored Receivables	Total
<b>December 31, 2023</b>									
Beginning Balance	\$ 1,302	\$ 14	\$ 79	\$ 899	\$ 55	\$ 1,505	\$ 51	\$ 608	\$ 4,513
Impact of adopting ASC 326	1,042	13	(32)	(308)	57	651	(33)	-	1,390
Provision for credit losses	351	(9)	24	25	31	588	1	322	1,333
Charge-offs	(214)	-	-	-	-	(328)	-	(638)	(1,180)
Recoveries	14	-	-	-	-	69	-	169	252
Net charge-offs	(200)	-	-	-	-	(259)	-	(469)	(928)
Ending balance	<u>\$ 2,495</u>	<u>\$ 18</u>	<u>\$ 71</u>	<u>\$ 616</u>	<u>\$ 143</u>	<u>\$ 2,485</u>	<u>\$ 19</u>	<u>\$ 461</u>	<u>\$ 6,308</u>
<b>December 31, 2022</b>									
Beginning Balance	\$ 1,154	\$ 15	\$ 76	\$ 869	\$ 40	\$ 1,324	\$ 20	\$ 654	\$ 4,152
Provision for credit losses	454	(1)	3	30	15	202	31	530	1,264
Charge-offs	(337)	-	-	-	-	(43)	-	(617)	(997)
Recoveries	31	-	-	-	-	22	-	41	94
Net charge-offs	(306)	-	-	-	-	(21)	-	(576)	(903)
Ending balance	<u>\$ 1,302</u>	<u>\$ 14</u>	<u>\$ 79</u>	<u>\$ 899</u>	<u>\$ 55</u>	<u>\$ 1,505</u>	<u>\$ 51</u>	<u>\$ 608</u>	<u>\$ 4,513</u>

The following table presents the allowance for credit losses for loans by type of allowance methodology as of December 31, 2022.

(In thousands)	Commercial and Industrial	Consumer Installment	Real Estate Residential	Real Estate Commercial	Real Estate Construction and Land	SBA	USDA	Factored Receivables	Total
<b>December 31, 2022</b>									
Loans individually evaluated for impairment	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Loans collectively evaluated for impairment	1,302	14	79	899	55	1,505	51	608	4,513
Ending balance	<u>\$ 1,302</u>	<u>\$ 14</u>	<u>\$ 79</u>	<u>\$ 899</u>	<u>\$ 55</u>	<u>\$ 1,505</u>	<u>\$ 51</u>	<u>\$ 608</u>	<u>\$ 4,513</u>

The following table presents the recorded investment in loans as of December 31, 2022, related to each balance in the allowance for credit losses for loans by portfolio segment by type of allowance methodology.

(In thousands)	Commercial and Industrial	Consumer Installment	Real Estate Residential	Real Estate Commercial	Real Estate Construction and Land	SBA	USDA	Factored Receivables	Total
<b>December 31, 2022</b>									
Loans individually evaluated for impairment	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 2,126	\$ -	\$ -	\$ 2,126
Loans collectively evaluated for impairment	92,946	1,058	5,566	63,924	3,873	256,184	2,235	22,420	448,206
Ending balance	<u>\$ 92,946</u>	<u>\$ 1,058</u>	<u>\$ 5,566</u>	<u>\$ 63,924</u>	<u>\$ 3,873</u>	<u>\$ 258,310</u>	<u>\$ 2,235</u>	<u>\$ 22,420</u>	<u>\$ 450,332</u>

Management continues to closely monitor for credit changes resulting from the uncertain forecasted economic conditions, the continued elevated interest rate environment, and the persistent high inflation levels in the United States and our market areas, and potential recession in the United States and our market areas. Additional provisions for credit losses may be necessary in future periods.

**Note 4. Premises and Equipment and Leases**

Year-end premises and equipment were as follows:

(In thousands)	December 31, 2023	December 31, 2022
Land	\$ 698	\$ 698
Leasehold improvements	178	223
Building	4,568	4,455
Furniture and equipment	752	474
	6,196	5,850
Less: accumulated depreciation	(1,438)	(1,221)
Balance at end of period	<u>\$ 4,758</u>	<u>\$ 4,629</u>

Depreciation of premises and equipment totaled \$247,000 and \$228,000 for the years ended December 31, 2023 and 2022, respectively. During 2022, there were disposals of equipment with fully depreciated cost of \$1.4 million.

The Company leases certain office facilities and office equipment under operating leases. Certain of the leases contain provisions for renewal options, escalation clauses based on increases in certain costs incurred by the lessor, as well as free rent periods and tenant improvement allowances. The Company amortizes office lease incentives and rent escalations on a straight-line basis over the life of the respective leases. The Company has obligations under operating leases that expire between 2023 and 2029 with initial non-cancellable terms in excess of one year.

Under the lease accounting standards, right-of-use assets represent our right to utilize the underlying asset during the lease term, while the lease liability represents the obligation to make periodic lease payments over the life of the lease. As of December 31, 2023 and 2022, right-of-use assets and related lease liabilities totaled \$2.5 million and \$2.5 million, and \$1.6 million and \$1.7 million, respectively, and are included in other assets and other liabilities, respectively, on our accompanying consolidated balance sheets. As of December 31, 2023 and 2022, the weighted average remaining lease term was 64 months and 46 months, respectively, and the weighted average discount rate was 4.12% and 3.74%, respectively.

As of December 31, 2023, the minimum rental commitments under these noncancelable operating leases are as follows:

(In thousands)	
2024	\$ 682
2025	769
2026	509
2027	228
2028	179
Thereafter	524
Total minimum rental payments	2,891
Less: Interest	(343)
Present value of lease liabilities	<u>\$ 2,548</u>

The Company currently receives rental income from seven tenants in its headquarters building for office space the Company does not occupy. Aggregate future minimum rentals to be received under non-cancelable leases as of December 31, 2023 through 2031 were as follows.

(In thousands)	
2024	\$ 348
2025	361
2026	282
2027	216
2028	101
Thereafter	91
Total minimum rental payments	<u>\$ 1,399</u>

**Note 5. Other Real Estate Owned**

There was no OREO as of December 31, 2023 and 2022.

**Note 6. Goodwill and Core Deposit Intangible**

Goodwill and core deposit intangible assets were as follows:

(In thousands)	December 31, 2023	December 31, 2022
Goodwill	\$ 21,440	\$ 21,440
Core deposit intangible	359	569

Core deposit intangible is amortized on a straight-line basis over the estimated lives of the deposits, which range from five to twelve years. The core deposit intangible amortization totaled \$210,000 and \$208,000 for the years ended December 31, 2023 and 2022, respectively.

The carrying basis and accumulated amortization of the core deposit intangible as of December 31, 2023 and 2022 were as follows:

(In thousands)	December 31, 2023	December 31, 2022
Gross carrying basis	\$ 1,708	\$ 1,708
Accumulated amortization	(1,349)	(1,139)
Net carrying amount	<u>\$ 359</u>	<u>\$ 569</u>

The estimated amortization expense of the core deposit intangible for each of the following five years is as follows:

(In thousands)	
2024	\$ 210
2025	149
Total	<u>\$ 359</u>

**Note 7. Deposits**

Deposits were as follows:

(In thousands, except percentages)	December 31, 2023		December 31, 2022	
Non-interest bearing demand	\$ 68,433	13%	\$ 94,187	19%
Interest-bearing demand (NOW)	4,295	1	6,216	1
Money market accounts	139,596	25	122,880	25
Savings accounts	6,132	2	8,052	2
Time deposits	308,435	59	261,690	53
Total	<u>\$ 526,891</u>	<u>100%</u>	<u>\$ 493,025</u>	<u>100%</u>

The aggregate amount of demand deposit overdrafts that have been reclassified as loans as of December 31, 2023 and 2022 was insignificant.

As of December 31, 2023 the scheduled maturities of time deposits were as follows:

(In thousands)	
2024	\$ 250,876
2025	44,243
2026	10,044
2027	3,008
2028	264
Total	<u>\$ 308,435</u>

The aggregate amount of time deposits that exceeded the \$250,000 FDIC insurance limit totaled \$71.9 million and \$85.1 million at December 31, 2023 and 2022, respectively.



## Note 8. Borrowed Funds and Subordinated Notes

The Company has a blanket lien credit line with the FHLB with borrowing capacity of \$56.8 million secured by commercial loans. The Company determines its borrowing needs and utilizes overnight advance accordingly at varying terms. The Company had no borrowings with FHLB as of December 31, 2023 and 2022.

The Company also has a credit line with the FRB with borrowing capacity of \$43.5 million, which is secured by commercial loans. The Company had no borrowings under this line from the FRB at December 31, 2023 and 2022.

As part of the BTFP, the Federal Reserve offered loans of up to one year in length to banks and other eligible depository institutions pledging U.S. treasuries, agency debt and mortgage-backed securities, and other qualifying assets as collateral, which are assessed at par value. The Bank pledged available for sale securities with par value of \$23.3 million to provide additional liquidity to meet the needs of depositors as of December 31, 2023. The Company borrowed \$21.0 million related to the BTFP as of December 31, 2023, with interest rate of 4.85% and maturing on December 26, 2024.

As of December 31, 2023, T Bancshares had an outstanding subordinated note for \$8.0 million issued in 2017 bearing an interest rate of three-month CME Term SOFR plus a spread adjustment of 0.26161% plus 5.125%, with interest payable quarterly and maturing on July 20, 2027, at which all principal is due. As of December 31, 2023, the rate was 10.78165%. T Bancshares also had an outstanding subordinated note for \$4.0 million issued in 2018 bearing a fixed interest rate of 7.125% payable semi-annually up to July 18, 2023, and converting to variable rate of three-month CME Term SOFR plus a spread adjustment of 0.26161% plus 4.348%, payable quarterly, and maturing on March 31, 2028. As of December 31, 2023, the rate was 10.00465%. The subordinated notes are unsecured and subordinated in right of payment to the payment of our existing and future senior indebtedness and structurally subordinated to all existing and future indebtedness of our subsidiaries.

## Note 9. Benefit Plans

The Company funds certain costs for medical benefits in amounts determined at the discretion of management. The Company has a retirement savings 401(k) plan covering substantially all employees of the Bank, and a second 401(k) plan covering substantially all employees of Sanders Morris and Tectonic Advisors.

Under both 401(k) plans covering the Company's employees, an employee may contribute up to the annual maximum contribution allowed for a given year under IRS regulations. The Company matches 100% of the employee's contribution on the first 1% of the employee's compensation and 50% of the employee's contribution on the next 5% of the employee's compensation, up to the maximum amount under IRS regulations.

At its discretion, the Company may also make additional annual contributions to the 401(k) plans. Each of the 401(k) plans is a participant directed plan, and as such, contributions to such 401(k) plan are invested as directed by the respective 401(k) plan participant.

The amount of employer contributions charged to expense under the two plans was \$707,000 and \$575,000 for the years ended December 31, 2023 and 2022, respectively, and is included in salaries and employee benefits on the consolidated statements of income. There was no accrual payable to either plan as of December 31, 2023 and 2022.

## Note 10. Income Taxes

The provision (benefit) for income taxes consists of the following:

(In thousands)	2023	2022
Current:		
Federal income tax	\$ 3,801	\$ 3,986
State income tax	91	125
Total current	3,892	4,111
Deferred federal	(56)	311
Income tax expense	\$ 3,836	\$ 4,422

The effective tax rate differs from the U. S. statutory tax rate due to the following for 2023 and 2022:

	2023	2022
U.S. statutory rate	21.0%	21.0%
Stock compensation deductible for tax purposes and various other	(0.9)	(0.4)
Effective tax rate	20.1%	20.6%

A reconciliation between reported income tax expense and the amounts computed by applying the U.S. federal statutory income tax rate of 21% to income before income taxes is presented in the following table.

(In thousands)	2023	2022
Income tax expense computed at the statutory rate	\$ 3,982	\$ 4,479
State income tax	91	125
Other	(237)	(182)
Income tax expense, as reported	\$ 3,836	\$ 4,422

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities as of December 31, 2023 and 2022 are as follows:

(In thousands)	2023	2022
Deferred tax assets:		
Allowance for credit losses	\$ 1,411	\$ 793
Non-accrual loan interest	49	84
Servicing asset valuation allowance	8	16
Accrued liabilities	223	231
Stock compensation	74	74
Lease liabilities under operating leases	48	30
Available for sale securities discount accretion	-	1
Net unrealized loss on securities available for sale	484	629
Total deferred tax assets	2,297	1,858
Deferred tax liabilities:		
Net deferred loan costs	(742)	(592)
Depreciation and amortization	(327)	(248)
Held-to-maturity securities premium	(19)	(42)
Loan discount	(75)	(87)
Adjustment for FHLB stock	(5)	(2)
Intangible assets	(240)	(251)
Total deferred tax liabilities	(1,408)	(1,222)
Net deferred tax asset	\$ 889	\$ 636

Projections for continued levels of profitability will be reviewed quarterly and any necessary adjustments to the deferred tax assets will be recognized in the provision or benefit for income taxes. In assessing the realization rate of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. No valuation allowance for deferred tax assets was recorded at December 31, 2023 and 2022, as management believes it is more likely than not that all of the deferred tax assets will be realized against deferred tax liabilities and projected future taxable income.

#### Note 11. Stock Compensation Plans

The board of directors and shareholders adopted the Amended and Restated Tectonic Financial, Inc. 2017 Equity Incentive Plan ("Plan"). The Plan is administered by the Compensation Committee of the board of directors and authorizes the granting of options, stock appreciation rights, restricted stock and restricted stock units to employees, directors and consultants in order to promote the success of the Company's business. Incentive stock options may be granted only to employees of the Company, or a parent or subsidiary of the Company. The Company reserved 750,000 authorized shares of common stock for the Plan. The term of each option is no longer than 10 years from the date of the grant. At December 31, 2023, the Company had 340,000 shares of common stock remaining available for future grants.

The Company accounts for stock-based employee compensation plans using the fair value-based method of accounting. The fair value of each option award is estimated on the date of grant by a third party using a closed form option valuation (Black-Scholes) model. The fair value of each grant award is estimated on the date of grant by a third party using the market approach based on the application of latest 12-month Company metrics to guideline public company multiples.

On September 27, 2021, 40,000 shares of restricted stock of the Company with an exercise price of \$10.00 and an intrinsic value of \$6.92 were granted with a contract life through December 31, 2021. Sanders Morris issued a full recourse secured promissory note at the time of the grant. These shares of restricted stock vested immediately, and were exercised on October 29, 2021, with the grantees utilizing the proceeds of the promissory note from Sanders Morris to fund the exercise price. This note receivable is recognized within a contra-equity account, with payments by the grantees reducing this balance as they occur. Once exercised, the shares were subject to a right of repurchase by the Company under certain circumstances which right expired on December 31, 2023.

No stock options were exercised during the year ended December 31, 2023. During the year ended December 31, 2022, options on 22,500 shares of the Company's common stock were exercised at \$4.30 per share for a total exercise price of \$96,750. There were no stock options granted or forfeited during the year ended December 31, 2023 or 2022.

The number of option shares outstanding was 167,500 as of December 31, 2023 and 2022, and the weighted average exercise price was \$5.51. The weighted average contractual life of the stock awards as of December 31, 2023 and 2022 was 3.37 years and 4.37 years, respectively. Stock options outstanding at the end of the period had immaterial aggregate intrinsic values. The weighted-average grant date fair value of the options as of December 31, 2023 and 2022 was \$1.98. Under Topic 805, the grant date fair value has been restated as though the Tectonic Merger, under which Tectonic Holdings, LLC merged with and into Tectonic Financial, Inc., had occurred upon the date at which the entities came under common control.

As of December 31, 2023, all 167,500 stock options outstanding were vested, and there was no remaining unrecognized compensation cost. The Company recorded compensation expense on a straight-line basis over the vesting periods, and for the 40,000 shares of restricted stock granted September 27, 2021, over the right of repurchase period. The Company recorded salaries and employee benefits expense on our consolidated statements of income in connection with the options issued and restricted stock issued under the plan of \$81,000 and \$78,000 for the years ended December 31, 2023 and 2022, respectively.

On September 30, 2020, the Company granted restricted stock units totaling 210,000 shares of common stock. The fair value of each unit award was estimated on the date of grant by a third party using the market approach based on the application of latest 12-month Company metrics to guideline public company multiples. The vesting schedules vary by award, with all of the units awarded vesting over a three year period from 2023 through 2025. The restricted stock units are subject to accelerated vesting due to death, total disability, or change in control of the Company.

As of December 31, 2023, 78,000 awarded units of restricted stock were outstanding, and the grant date fair value was \$4.81. During the year ended December 31, 2023, 92,000 units awarded became vested and shares were issued. During the year ended December 31, 2022, 10,000 units awarded became vested and shares were issued, and 30,000 restricted stock units were forfeited with a grant date fair value of \$4.81 per share. The weighted average contractual life as of December 31, 2023 and 2022 was 1.18 years and 1.54 years, respectively. The Company is recording compensation expense on a straight-line basis over the respective vesting periods. There was a \$78,000 reversal in compensation expense for the year ended December 31, 2022, which was related to the forfeiture of 30,000 unvested restricted stock awards. For the years ended December 31, 2023 and 2022, the Company recorded salaries and employee benefits expense on our consolidated statements of income of \$221,000 and \$193,000, respectively, related to the restricted stock awards. As of December 31, 2023, there was \$98,000 of unrecognized compensation cost related to the restricted stock awards.

As of December 31, 2023 and 2022, 78,000 and 170,000 restricted units awarded were outstanding, respectively. The weighted average grant date fair value of the awards as of December 31, 2023, was \$4.81.

## **Note 12. Commitments and Contingencies**

The Company is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. These instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the accompanying balance sheets. The Company's exposure to credit loss in the event of non-performance by the other party to the financial instruments for commitments to extend credit and standby letters of credit is represented by the contractual amount of those instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

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

The following table summarizes loan commitments:

(In thousands)	December 31, 2023	December 31, 2022
Undisbursed loan commitments	\$ 45,743	\$ 43,427
Standby letters of credit	162	161
	<u>\$ 45,905</u>	<u>\$ 43,588</u>

*Allowance For Credit Losses - Off-Balance-Sheet Credit Exposures.* The allowance for credit losses for off-balance-sheet credit exposures is a liability account, calculated in accordance with ASC 326, representing expected credit losses over the contractual period for which we are exposed to credit risk resulting from a contractual obligation to extend credit. No allowance is recognized if we have the unconditional right to cancel the obligation. Off-balance-sheet credit exposures primarily consist of amounts available under outstanding lines of credit and letters of credit detailed in the table above. For the period of exposure, the estimate of expected credit losses considers both the likelihood that funding will occur, and the amount expected to be funded over the estimated remaining life of the commitment or other off-balance-sheet exposure. The likelihood and expected amount of funding are based on historical utilization rates. The amount of the allowance represents management's best estimate of expected credit losses on commitments expected to be funded over the contractual life of the commitment. Estimating credit losses on amounts expected to be funded uses the same methodology as described for loans in Note 3 - Loans and Allowance for Credit Losses, as if such commitments were funded.

The following table details activity in the allowance for credit losses for off-balance-sheet commitments.

(In thousands)	2023	2022
Beginning balance	\$ -	\$ -
Impact of adopting ASC 326	238	-
Provision for off-balance sheet credit exposure	(45)	-
Ending balance	<u>\$ 193</u>	<u>\$ -</u>

The Company is involved in various regulatory inspections, inquiries, investigations and proceedings, and litigation matters that arise from time to time in the ordinary course of business. The process of resolving matters through litigation or other means is inherently uncertain, and it is possible that an unfavorable resolution of these matters, will adversely affect the Company, its results of operations, financial condition and cash flows. The Company's regular practice is to expense legal fees as services are rendered in connection with legal matters, and to accrue for liabilities when payment is probable.

The Company, through its wholly owned subsidiary Sanders Morris, has uncommitted financing arrangements with clearing brokers that finance its customer accounts, certain broker-dealer balances, and firm trading positions. Although these customer accounts and broker-dealer balances are not reflected on the consolidated balance sheets for financial reporting purposes, Sanders Morris has generally agreed to indemnify these clearing brokers for losses they may sustain in connection with the accounts, and therefore, retains risk on these accounts. Sanders Morris is required to maintain certain cash or securities on deposit with its clearing brokers. Deposits with clearing organizations were \$250,000 as of December 31, 2023 and 2022.

## Employment Agreements

The Company is party to amended and restated employment agreements with Patrick Howard, President and Chief Operating Officer of the Company, and Ken Bramlage, Executive Vice President and Chief Financial Officer of the Company. In addition, the Company entered into an employment agreement with A. Haag Sherman, Chief Executive Officer of the Company, in connection with the Company's merger with Tectonic Holdings and its initial public offering. Messrs. Sherman and Howard's employment agreements had a four year term and now is year to year, and Mr. Bramlage's employment agreement had a three year term and now is year to year.

### Note 13. Related Parties

**Advisors' service agreements:** In January 2006, the Company entered into a services agreement (the "Tectonic Advisors-CWA Services Agreement") with Cain Watters. The owners of Cain Watters together hold approximately 29.5% ownership in the Company. Under the Tectonic Advisors-CWA Services Agreement, Cain Watters pays the Company for due diligence and research services on investment alternatives available to Cain Watters' clients. The Company earned \$257,000 and \$291,000 during the years ended December 31, 2023 and 2022, respectively, under the Tectonic Advisors-CWA Services Agreement. These fees are included in investment advisory and other related services in the accompanying consolidated statements of income. The Company had \$95,000 in fees payable and \$21,000 in fees receivable, respectively, related to these services at December 31, 2023 and 2022, respectively, which are included in other liabilities and other assets, respectively, on the consolidated balance sheets.

**CWA Fee Allocation Agreement:** In January 2006, Tectonic Advisors entered into an agreement (the "Fee Allocation Agreement") with Cain Watters with reference to its advisory agreement with the Bank. Tectonic Advisors had \$215,000 and \$193,000 payable to Cain Watters related to this agreement at December 31, 2023 and 2022, respectively, which are included in other liabilities on the accompanying consolidated balance sheets.

Certain officers, directors and their affiliated companies had depository accounts with the Bank as of December 31, 2023 and 2022, totaling approximately \$7.7 million and \$8.3 million, respectively. None of those deposit accounts have terms more favorable than those available to any other depositor. As of December 31, 2023 and 2022, there were no loans outstanding to directors of the Bank or their affiliated companies.

### Note 14. Regulatory Matters

The Company and the Bank are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Bank's and, accordingly, the Company's business, results of operations and financial condition. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities and certain off-balance-sheet items as calculated under GAAP, regulatory reporting requirements, and regulatory capital standards. The Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors. Furthermore, the Bank's regulators could require adjustments to regulatory capital not reflected in these financial statements.

Quantitative measures established by regulatory capital standards to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of total and tier 1 capital to risk-weighted assets, common equity Tier 1 ("CET1") capital to total risk-weighted assets, and of tier 1 capital to average assets. To be categorized as "well-capitalized" under the prompt corrective action framework, the Bank must maintain (i) a Total risk-based capital ratio of 10%; (ii) a Tier 1 risk-based capital ratio of 8%; (iii) a Tier 1 leverage ratio of 5%; and (iv) a CET1 risk-based capital ratio of 6.5%.

In addition, the Basel III regulatory capital reforms ("Basel III") implemented a capital conservation buffer of 2.5%. The Basel III minimum capital ratio requirements as applicable to the Bank are summarized in the table below.

	BASEL III Minimum for Capital Adequacy Requirements	BASEL III Additional Capital Conservation Buffer	BASEL III Ratio with Capital Conservation Buffer
Total Risk Based Capital (total capital to risk weighted assets)	8.0%	2.5%	10.5%
Tier 1 Risk Based Capital (tier 1 to risk weighted assets)	6.0%	2.5%	8.5%
Common Equity Tier 1 Risk Based ( CET1 to risk weighted assets)	4.5%	2.5%	7.0%
Tier 1 Leverage Ratio (tier 1 to average assets)	4.0%	-%	4.0%

Accordingly, a financial institution may be considered "well capitalized" under the prompt corrective action framework, but not satisfy the Basel III capital ratios. As of December 31, 2023, the Bank's regulatory capital ratios are in excess of the capital conservation buffer and the levels established for "well capitalized" institutions under the Basel III rules.

The regulatory capital ratios of the Company and the Bank are as follows:

(In thousands, except percentages) As of December 31, 2023	Actual		Minimum Capital Required - Basel III		Required to be Considered Well Capitalized	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Total Capital (to Risk Weighted Assets)						
Tectonic Financial, Inc. (consolidated)	\$ 92,385	20.90%	\$ 46,415	10.50%	\$ 44,205	10.00%
T Bank, N.A.	92,957	21.29	45,835	10.50	43,652	10.00
Tier 1 Capital (to Risk Weighted Assets)						
Tectonic Financial, Inc. (consolidated)	86,847	19.65	37,574	8.50	35,364	8.00
T Bank, N.A.	87,488	20.04	37,105	8.50	34,922	8.00
Common Equity Tier 1 (to Risk Weighted Assets)						
Tectonic Financial, Inc. (consolidated)	69,597	15.74	30,944	7.00	28,733	6.50
T Bank, N.A.	87,488	20.04	30,557	7.00	28,374	6.50
Tier 1 Capital (to Average Assets)						
Tectonic Financial, Inc. (consolidated)	86,847	13.97	24,861	4.00	31,076	5.00
T Bank, N.A.	87,488	14.26	24,534	4.00	30,667	5.00
As of December 31, 2022						
Total Capital (to Risk Weighted Assets)						
Tectonic Financial, Inc. (consolidated)	\$ 81,317	20.21%	\$ 42,243	10.50%	\$ 40,232	10.00%
T Bank, N.A.	81,279	20.42	41,786	10.50	39,796	10.00
Tier 1 Capital (to Risk Weighted Assets)						
Tectonic Financial, Inc. (consolidated)	76,805	19.09	34,197	8.50	32,185	8.00
T Bank, N.A.	76,767	19.29	33,826	8.50	31,837	8.00
Common Equity Tier 1 (to Risk Weighted Assets)						
Tectonic Financial, Inc. (consolidated)	59,555	14.80	28,162	7.00	26,150	6.50
T Bank, N.A.	76,767	19.29	27,857	7.00	25,867	6.50
Tier 1 Capital (to Average Assets)						
Tectonic Financial, Inc. (consolidated)	76,805	13.27	23,153	4.00	28,941	5.00
T Bank, N.A.	76,767	13.47	22,795	4.00	28,494	5.00

*Dividend Restrictions.* Banking regulations may limit the amount of dividends that may be paid. Approval by regulatory authorities is required if the effect of dividends declared (including those on the Series A preferred stock) would cause the regulatory capital of the Bank and/or the Company to fall below specified minimum levels. Approval is also required if dividends declared exceed the net profits for that year combined with the retained net profits for the preceding two years. As of December 31, 2023, approximately \$16.6 million was available for the declaration of dividends by the Bank to the Company without prior approval of regulatory agencies and still maintain its “well capitalized” status. In addition, as a Texas corporation, we are restricted under the Texas Business Organizations Code from paying dividends under certain conditions. Under Texas law, we cannot pay dividends to shareholders if the dividends exceed our surplus or if after giving effect to the dividends, we would be insolvent.

In addition to the regulatory requirements of the federal banking agencies, Sanders Morris and Tectonic Advisors are subject to the regulatory framework applicable to registered investment advisors under the SEC’s Division of Investment Management, and additionally, Sanders Morris is regulated by FINRA, which, among other requirements, imposes minimums on its net regulatory capital.

#### Note 15. Operating Segments

The Company’s reportable segments consist of Banking, Other Financial Services, and HoldCo operations.

The Banking segment consists of operations relative to the Company’s full service banking operations, including providing depository and lending services to individual and business customers, and other related banking services, as well as operations of the Bank’s Integra factoring division.

The Other Financial Services segment includes managed and directed brokerage, investment advisory services, including related trust company operations, third party administration, and insurance brokerage services to both individuals and businesses.

The HoldCo operations include the operations and subordinated debt held at the Bank's immediate parent, as well as the activities of the financial holding company which serves as T Bancshares's parent.

The tables below present the financial information for each segment that is specifically identifiable, or based on allocations using internal methods, for the years ended December 31, 2023 and 2022:

(In thousands)	Banking	Other Financial Services	HoldCo	Consolidated
<b>Year Ended December 31, 2023</b>				
<b>Income Statement</b>				
Total interest income	\$ 46,467	\$ -	\$ -	\$ 46,467
Total interest expense	17,909	-	1,197	19,106
Provision for credit losses	1,288	-	-	1,288
Net interest income (loss) after provision for credit losses	27,270	-	(1,197)	26,073
Non-interest income	2,050	37,854	(100)	39,804
Depreciation and amortization expense	403	52	2	457
All other non-interest expense	16,997	25,529	3,838	46,364
Income (loss) before income tax	\$ 11,920	\$ 12,273	\$ (5,137)	\$ 19,056
Goodwill and other intangibles	\$ 19,449	\$ 2,350	\$ -	\$ 21,799
<b>Total assets</b>	<b>\$ 663,001</b>	<b>\$ 12,661</b>	<b>\$ 1,684</b>	<b>\$ 677,346</b>

(In thousands)	Banking	Other Financial Services	HoldCo	Consolidated
<b>Year Ended December 31, 2022</b>				
<b>Income Statement</b>				
Total interest income	\$ 33,385	\$ -	\$ -	\$ 33,385
Total interest expense	4,993	-	911	5,904
Provision for credit losses	1,264	-	-	1,264
Net interest income (loss) after provision for credit losses	27,128	-	(911)	26,217
Non-interest income	1,238	38,788	14	40,040
Depreciation and amortization expense	381	55	-	436
All other non-interest expense	14,879	27,569	1,921	44,369
Income (loss) before income tax	\$ 13,106	\$ 11,164	\$ (2,818)	\$ 21,452
Goodwill and other intangibles	\$ 19,659	\$ 2,350	\$ -	\$ 22,009
<b>Total assets</b>	<b>\$ 599,305</b>	<b>\$ 12,316</b>	<b>\$ 915</b>	<b>\$ 612,536</b>

#### Note 16. Fair Value of Financials Instruments

The fair value of an asset or liability is the price that would be received to sell that asset or paid to transfer that liability in an orderly transaction occurring in the principal market (or most advantageous market in the absence of a principal market) for such asset or liability. In estimating fair value, the Company utilizes valuation techniques that are consistent with the market approach, the income approach and/or the cost approach. Such valuation techniques are consistently applied. Inputs to valuation techniques include the assumptions that market participants would use in pricing an asset or liability. FASB ASC Topic 820, *Fair Value Measurement*, establishes a fair value hierarchy for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy is as follows:

- *Level 1 Inputs* - Unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.
- *Level 2 Inputs* - Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These might include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (such as interest rates, volatilities, prepayment speeds, credit risks, etc.) or inputs that are derived principally from or corroborated by market data by correlation or other means.
- *Level 3 Inputs* - Unobservable inputs for determining the fair values of assets or liabilities that reflect an entity's own assumptions about the assumptions that market participants would use in pricing the assets or liabilities.



Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated by using quoted prices of securities with similar characteristics or independent asset pricing services and pricing models, the inputs of which are market-based or independently sourced market parameters, including, but not limited to, yield curves, interest rates, volatilities, prepayments, defaults, cumulative loss projections and cash flows. Such securities are classified in Level 2 of the valuation hierarchy. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy. The Company has no securities in the Level 1 or Level 3 inputs.

The following table summarizes securities available for sale measured at fair value on a recurring basis, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value:

(In thousands)	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
<b>As of December 31, 2023</b>				
Securities available for sale:				
U.S. Treasuries	\$ -	\$ 3,894	\$ -	\$ 3,894
U.S. government agencies	-	13,627	-	13,627
Mortgage-backed securities	-	5,456	-	5,456
<b>As of December 31, 2022</b>				
Securities available for sale:				
U.S. government agencies	\$ -	\$ 1,953	\$ -	\$ 1,953
U.S. government agencies	-	13,088	-	13,088
Mortgage-backed securities	-	5,592	-	5,592

Market valuations of our investment securities which are classified as Level 2 are provided by an independent third party. The fair values are determined by using several sources for valuing fixed income securities. Their techniques include pricing models that vary based on the type of asset being valued and incorporate available trade, bid and other market information. In accordance with the fair value hierarchy, the market valuation sources include observable market inputs and are therefore considered Level 2 inputs for purposes of determining the fair values.

The Company considers transfers between the levels of the hierarchy to be recognized at the end of related reporting periods. During the year ended December 31, 2023, no assets for which fair value is measured on a recurring basis transferred between any levels of the hierarchy.

Certain financial assets and financial liabilities are measured at fair value on a nonrecurring basis; that is, the instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment).

Financial assets measured at fair value on a non-recurring basis during the reported periods include impaired loans and loans held for sale.

*Impaired loans.* As of December 31, 2022, there were no impaired loans that were reduced by specific valuation allowances.

The significant unobservable inputs (Level 3) used in the fair value measurement of collateral for collateral-dependent impaired loans primarily relate to the specialized discounting criteria applied to the borrower's reported amount of collateral. The amount of the collateral discount depends upon the condition and marketability of the collateral, as well as other factors which may affect the collectability of the loan. As the Company's primary objective in the event of default would be to liquidate the collateral to settle the outstanding balance of the loan, collateral that is less marketable would receive a larger discount. During the years ended December 31, 2023 and 2022, there were no discounts for collateral-dependent impaired loans.

The valuation of our not readily marketable investment securities which are classified as Level 3 are based on the Company's own assumptions and inputs that are both significant to the fair value measurement, and are unobservable.

Our assessment of the significance of a particular input to the Level 3 fair value measurements in their entirety requires judgment and considers factors specific to the assets. It is reasonably possible that a change in the estimated fair value for instruments measured using Level 3 inputs could occur in the future.

*Loans held for sale.* Loans held for sale include the guaranteed portion of SBA and USDA loans and are reported at the lower of cost or estimated fair value. Fair value for SBA and USDA loans is based on market indications available in the market. There were no impairments reported for the periods presented.

Non-financial assets measured at fair value on a non-recurring basis during the reported periods include other real estate owned which, upon initial recognition, was re-measured and reported at fair value through a charge-off to the allowance for credit losses. Additionally, foreclosed assets which, subsequent to their initial recognition, are re-measured at fair value through a write-down included in other non-interest expense. Regulatory guidelines require the Company to reevaluate the fair value of foreclosed assets on at least an annual basis. The fair value of foreclosed assets, upon initial recognition and impairment, are re-measured using Level 2 inputs based on observable market data. Estimated fair value of other real estate is based on appraisals. Appraisers are selected from the list of approved appraisers maintained by management. As of December 31, 2023 and 2022, there were no foreclosed assets. There were no foreclosed assets re-measured during the years ended December 31, 2023 and 2022.

The methods and assumptions used to estimate fair value of financial assets and financial liabilities that are not measured and reported at fair value on a recurring basis or non-recurring basis are described as follows:

Carrying amount is the estimated fair value for cash and cash equivalents, restricted securities, accrued interest receivable and accrued interest payable. The estimated fair value of demand and savings deposits is the carrying amount since rates are regularly adjusted to market rates and amounts are payable on demand. For borrowed funds and variable rate loans or deposits that re-price frequently and fully, the estimated fair value is the carrying amount. For fixed rate loans or deposits and for variable rate loans or deposits with infrequent re-pricing, fair value is based on discounted cash flows using current market rates applied to the estimated life and credit risk. For loans held for sale, the estimated fair value is based on market indications for similar assets in the active market. The estimated fair value of other financial instruments and off-balance-sheet loan commitments approximate cost and are not considered significant to this presentation.

The Company adds a servicing asset when loans are sold and the servicing is retained, and uses the amortization method for the treatment of the servicing asset. The servicing asset is carried at lower of cost or fair value. Loan servicing assets do not trade in an active, open market with readily observable prices. Accordingly, fair value is estimated using a discounted cash flow model having significant inputs of discount rate, prepayment speed and default rate. Due to the nature of the valuation inputs, servicing rights are classified within Level 3 of the hierarchy. During the year ended December 31, 2023, the Company added servicing assets totaling \$38,000 in connection with the sale of a \$5.8 million USDA loan. There was no sale of loans during the year ended December 31, 2022. For the years ended December 31, 2023 and 2022, the Company amortized \$56,000 and \$168,000, respectively, using the amortization method for the treatment of servicing loans. The Company reversed \$35,000 of the servicing assets allowance for the year ended December 31, 2023, and recorded an allowance provision of \$10,000 for the year ended December 31, 2022.

FASB ASC Topic 825, *Financial Instruments*, requires disclosure of the fair value of financial assets and financial liabilities, including those financial assets and financial liabilities that are not measured and reported at fair value on a recurring basis or non-recurring basis. The estimated fair value approximates carrying value for cash and cash equivalents and accrued interest. The methodologies for other financial assets and financial liabilities that are not measured and reported at fair value on a recurring basis or non-recurring basis are discussed below:

*Securities held to maturity.* The securities in this category are PACE and PID/TIRZ investments. These investment contracts or bonds originate under a contractual obligation between the property owners, the local county administration, and a third-party administrator and sponsor. The fair value of these investments are estimated using observable market inputs in a discounted cash flow analysis.

*Loans.* The estimated fair value approximates carrying value for variable-rate loans that reprice frequently and with no significant change in credit risk. The fair value of fixed-rate loans and variable-rate loans which reprice on an infrequent basis is estimated by discounting future cash flows using the current interest rates at which similar loans with similar terms would be made to borrowers of similar credit quality.

*Deposits.* The fair values of demand deposits, savings deposits are, by definition, equal to the amount payable on demand and, therefore, approximate their carrying amounts. The fair values for time deposits are estimated using a discounted cash flow calculation that utilizes interest rates currently being offered on time deposits with similar contractual maturities.

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**Borrowed Funds.** The estimated fair value approximates carrying value for short-term borrowings. The fair value of long-term fixed-rate borrowings is estimated using quoted market prices, if available, or by discounting future cash flows using current interest rates for similar financial instruments. The estimated fair value approximates carrying value for variable-rate junior subordinated deferrable interest debentures that reprice quarterly.

**Loan Commitments, Standby and Commercial Letters of Credit.** Our lending commitments have variable interest rates and “escape” clauses if the customer’s credit quality deteriorates. Therefore, the fair values of these items are not significant and are not included in the following table.

Carrying amounts and estimated fair values of other financial instruments by level of valuation input were as follows:

	December 31, 2023	
	Carrying Amount	Estimated Fair Value
<b>(In thousands)</b>		
Financial assets:		
Level 1 inputs:		
Cash and cash equivalents	\$ 58,767	\$ 58,767
Level 2 inputs:		
Securities available for sale	22,977	22,977
Securities, restricted	4,176	4,176
Loans held for sale	26,573	28,671
Accrued interest receivable	4,829	4,829
Level 3 inputs:		
Securities held to maturity	24,194	23,849
Loans, net	494,787	484,848
Servicing asset	321	321
Financial liabilities:		
Level 1 inputs:		
Non-interest bearing deposits	68,433	68,433
Level 2 inputs:		
Interest bearing deposits	458,458	459,549
Borrowed funds	33,000	33,000
Accrued interest payable	913	913

	December 31, 2022	
	Carrying Amount	Estimated Fair Value
<b>(In thousands)</b>		
Financial assets:		
Level 1 inputs:		
Cash and cash equivalents	\$ 42,155	\$ 42,155
Level 2 inputs:		
Securities available for sale	20,633	20,633
Securities, restricted	3,496	3,496
Loans held for sale	33,902	36,470
Accrued interest receivable	3,102	3,102
Level 3 inputs:		
Securities held to maturity	25,262	26,482
Securities not readily marketable	100	100
Loans, net	445,819	438,956
Servicing asset	324	324
Financial liabilities:		
Level 1 inputs:		
Non-interest bearing deposits	94,187	94,187
Level 2 inputs:		
Interest bearing deposits	398,838	389,806
Borrowed funds	12,000	12,000
Accrued interest payable	592	592

**Note 17. Recent Accounting Pronouncements**

The Company has evaluated new accounting standards that have recently been issued and have determined that there are no new accounting standards that should be described in this section that will materially impact the Company's operations, financial condition or liquidity in future periods.

**Note 18. Parent Company Condensed Financial Statements**

**TECTONIC FINANCIAL, INC.  
CONDENSED BALANCE SHEETS**

(In thousands)	December 31, 2023	December 31, 2022
<b>ASSETS</b>		
Cash and due from banks	\$ 356	\$ 2,664
Securities, not readily marketable	-	100
Investment in subsidiaries	104,954	93,788
Other assets	1,619	669
<b>Total assets</b>	<b>\$ 106,929</b>	<b>\$ 97,221</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Other liabilities	\$ 72	\$ 473
Shareholders' equity	106,857	96,748
<b>Total liabilities and shareholders' equity</b>	<b>\$ 106,929</b>	<b>\$ 97,221</b>

**TECTONIC FINANCIAL, INC.  
CONDENSED STATEMENTS OF INCOME  
YEARS ENDED DECEMBER 31,**

(In thousands)	2023	2022
Income from subsidiaries	\$ 17,523	\$ 18,211
Other income	807	592
<b>Total income</b>	<b>18,330</b>	<b>18,803</b>
<b>Non-interest expense:</b>		
Salaries and employee benefits	2,674	1,194
Occupancy and equipment	84	5
Professional and administrative	491	283
Data processing	5	1
Other	831	759
<b>Total non-interest expense</b>	<b>4,085</b>	<b>2,242</b>
<b>Income before income taxes</b>	<b>14,245</b>	<b>16,561</b>
Income tax benefit	(975)	(469)
<b>Net Income</b>	<b>\$ 15,220</b>	<b>\$ 17,030</b>

**TECTONIC FINANCIAL, INC.  
CONDENSED STATEMENTS OF COMPREHENSIVE INCOME  
YEARS ENDED DECEMBER 31,**

(In thousands)	2023	2022
<b>Net Income</b>	<b>\$ 15,220</b>	<b>\$ 17,030</b>
<b>Other comprehensive income (loss):</b>		
Change in unrealized loss on investment securities available for sale	693	(2,582)
Tax effect	145	(542)
<b>Other comprehensive income (loss)</b>	<b>548</b>	<b>(2,040)</b>
<b>Comprehensive income</b>	<b>\$ 15,768</b>	<b>\$ 14,990</b>

**TECTONIC FINANCIAL, INC.**  
**CONDENSED STATEMENTS OF CASH FLOWS**  
**YEARS ENDED DECEMBER 31,**

(In thousands)	2023	2022
<b>Cash Flows from Operating Activities</b>		
Net income	\$ 15,220	\$ 17,030
Adjustments to reconcile net income to net cash used in operating activities:		
Equity in income of subsidiaries	(17,523)	(18,211)
Loss on disposal of securities not readily available	100	-
Depreciation and amortization	2	-
Stock based compensation	221	192
Net change in other assets	(1,010)	(401)
Net change in other liabilities	(401)	(79)
Net cash used in operating activities	(3,391)	(1,469)
<b>Cash Flows from Investing Activities</b>		
Contributions to subsidiaries	-	(200)
Purchase of property and equipment	58	-
Distributions from subsidiaries	5,700	4,570
Net cash provided by investing activities	5,758	4,370
<b>Cash Flows from Financing Activities</b>		
Proceeds from issuance of common shares	-	97
Dividends paid on Series B Preferred Shares	(1,553)	(1,552)
Dividends on common shares	(2,028)	(1,765)
Repurchase of common stock	(1,094)	(481)
Net cash used in financing activities	(4,675)	(3,701)
<b>Net change in cash and cash equivalents</b>	(2,308)	(800)
Cash and cash equivalents at beginning of period	2,664	3,464
<b>Cash and cash equivalents at end of period</b>	<u>\$ 356</u>	<u>\$ 2,664</u>
<b>Supplemental disclosures of cash flow information</b>		
Cash paid during the year for:		
Income taxes	\$ 3,350	\$ 4,715

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

None.

**Item 9A. Controls and Procedures.**

Our principal executive officer and principal financial officer have evaluated the effectiveness of our “disclosure controls and procedures” (as defined in Rule 13a-15(e) and 15d-15(e) of the Exchange Act, “Disclosure Controls”) as of the end of the period covered by this Form 10-K. Our management, including the principal executive officer and principal financial officer, does not expect that our Disclosure Controls will prevent all error and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

Based on such evaluation, our principal executive officer and principal financial officer have concluded that, as of the end of the period covered by this Form 10-K, the Company’s disclosure controls and procedures were effective to provide reasonable assurance that the information required to be disclosed by the Company in the reports it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC and is accumulated and communicated to the Company’s management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure.

**Management’s Report on Internal Control over Financial Reporting**

This Form 10-K does not include an attestation report of the Company’s registered public accounting firm regarding internal controls over financial reporting. Management’s report was not subject to attestation by the Company’s registered public accounting firm pursuant to rules of the SEC that permit the Company to provide only management’s report in this Form 10-K.

Management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rule 13a-15(f) and 15d-15(f) of the Exchange Act. The Company’s internal control over financial reporting system is designed to provide reasonable assurance to management and the Board of Directors regarding the reliability of the Company’s financial reporting and the preparation of published financial statements in accordance with generally accepted accounting principles.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to the financial statement preparation and presentation. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

As of December 31, 2023, management assessed the effectiveness of the Company’s internal control over financial reporting based on the criteria for effective internal control over financial reporting established in “Internal Control-Integrated Framework,” issued by the Committee of Sponsoring Organizations (“COSO”) of the Treadway Commission in 2013. Based on this assessment, management determined that the Company maintained effective internal control over financial reporting as of December 31, 2023.

Whitley Penn LLP, Dallas, Texas, (U.S. PCAOB Auditor Firm I.D.: 726) an independent registered public accounting firm, audited the consolidated financial statements of the Company for the years ended December 31, 2023 and 2022 included in this Annual Report on Form 10-K. Their report is included in “Item 8. Financial Statements and Supplementary Data.” This Annual Report on Form 10-K does not include an attestation report of the Company’s registered public accounting firm on the Company’s internal control over financial reporting due to the Company’s status as a Smaller Reporting Company.

**Changes in Internal Control over Financial Reporting**

There was no change in our internal control over financial reporting (as such term is defined in Rule 13a-15(f) under the Exchange Act) during the quarter ended December 31, 2023, that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting. The design of any system of controls and procedures is based in part upon certain assumptions about the likelihood of future events. There can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions, regardless of how remote.

**Item 9B. Other Information.**

During the three months ended December 31, 2023, none of the directors or officers of the Company adopted or terminated a "Rule 10b5-1 trading arrangement" or a "non-Rule 10b5-1 trading arrangement," as each term is defined in Item 408 of Regulation S-K.

**Item 9C. Disclosure regarding Foreign Jurisdictions that Prevent Inspections.**

Not applicable.



### PART III

#### Item 10. Directors, Executive Officers, and Corporate Governance

##### General

We have an experienced executive management team and board of directors. Our board of directors is comprised of ten directors who are elected by our shareholders at each annual meeting of shareholders for a term of one year. Our directors hold office until the next annual meeting of shareholders following their election and thereafter until their successors shall have been duly elected and qualified. Our executive officers are appointed by our board of directors and hold office until their successors are duly appointed and qualified, or until their earlier death, resignation or removal.

Pursuant to our certificate of formation and bylaws, our board of directors must be comprised of no less than one nor more than 15 directors, and is currently comprised of ten directors. The exact number of directors may be fixed from time to time within the range set forth in our bylaws by resolution of our board of directors.

As discussed in greater detail below, our board of directors has affirmatively determined that Eric Langford, Thomas McDougal and Barb Bomersbach qualify as independent directors based upon the rules of NASDAQ and the SEC. There are no arrangements or understandings between any of the directors, executive officers and any other person pursuant to which he or she was selected as a director.

##### Directors and Executive Officers

**Directors.** The following table sets forth certain information regarding our directors, including their ages and the years that they began serving as directors of the Company:

Name	Position with the Company	Age at March 1, 2024	Director Since
George L. Ball	Executive Co-Chairman	85	Nov 2018
Barb Bomersbach	Director	49	Mar 2019
Darrell W. Cain	Co-Chairman	67	Nov 2018
Steven B. “Brad” Clapp	Director	51	May 2017
Patrick Howard	Director; President	62	May 2017
Eric Langford	Director	64	May 2017
Thomas McDougal	Director	84	May 2017
Thomas R. Sanders	Director	49	May 2017
A. Haag Sherman	Director; Chief Executive Officer	58	Oct 2016
Daniel C. Wicker	Director	53	May 2017

**Executive Officers.** The following table sets forth certain information regarding our executive officers, including their positions and length of service with the Company.

Name	Position with the Company	Age at March 1, 2024	Director Since
George L. Ball	Executive Co-Chairman	85	Nov 2018
Ken Bramlage	Executive Vice President & Chief Financial Officer	63	—
David J. Clifford	Chief Operating Officer	46	—
Patrick Howard	President	62	May 2017
A. Haag Sherman	Chief Executive Officer	58	Oct 2016

The following is a brief discussion of the business and banking background and experience of our directors and executive officers for at least the past five years. With respect to directors, the biographies also contain information regarding the person’s experience, qualifications, attributes or skills that led to the conclusion that the person should serve as a director. Unless otherwise indicated, directors and senior officers have held their positions for the past five years. No director or executive officer has any family relationship, as defined in Item 401 of Regulation S-K, with any other director or with any of our executive officers.

## **Board of Directors**

**George L. Ball.** Mr. Ball is Executive Co-Chairman of the Company. Mr. Ball has served as a director of the Company since May 2017 and former Co-Chairman of Tectonic Holdings from 2015 to May 2019. He has served as Chairman of Sanders Morris, and its predecessor, Sanders Morris Mundy Inc., from May 1992 to present, and served as Chief Executive Officer of Sanders Morris from 2008 to 2011. He previously served as Chairman of The Edelman Financial Group, or Edelman, a financial services holding company, from 2008 until its sale to Hellman and Friedman in 2015. During his tenure, Edelman experienced significant growth (from \$3 billion to \$18 billion in assets under management). From September 1992 to January 1994, Mr. Ball was a Senior Executive Vice President of Smith Barney Shearson Inc. From September 1991 to September 1992, he was a consultant to J. & W. Seligman & Co. Incorporated. Mr. Ball served as Chairman and Chief Executive Officer of Prudential-Bache Securities, Inc. from 1982 to 1991 and Chairman of the Board from 1986 to 1991. He also served a member of the Executive Office of Prudential Insurance Company of America from 1982 to 1991. Before joining Prudential, Mr. Ball served as President of E.F. Hutton & Co. Mr. Ball is a former governor of the American Stock Exchange and the Chicago Board Options Exchange, and served on the Executive Committee of the Securities Industries Association. He is a graduate of Brown University with honors in economics and served as an officer in the U.S. Navy. We believe Mr. Ball's broker-dealer expertise and leadership of public companies, both as an executive and as a director, and stock exchanges qualifies him to serve on our board of directors.

**Barb Bomersbach.** Ms. Bomersbach has served as a director of the Company since March 2019. Ms. Bomersbach currently serves as Chief Financial Officer of Matador Gas & Power, a residential propane distribution company. From 2010 to 2021 she served as Chief Financial Officer of Tristate Midstream, a natural gas gathering company. Prior to that, Ms. Bomersbach was the Chief Financial Officer of Wynn Crosby, an upstream oil and gas company, in 2009. Ms. Bomersbach is a Certified Public Accountant and Chartered Financial Analyst, and graduated summa cum laude from Texas A&M University with a BBA and MS in Accounting. We believe Ms. Bomersbach brings to the Board of Directors experience in financial and accounting matters, internal controls and compliance (from an accounting standpoint) and is our audit committee financial expert.

**Darrell W. Cain.** Mr. Cain is the non-executive Co-Chairman of the Company. Mr. Cain has served as a director of the Company since November 2018, former Chairman of Tectonic Holdings from 2015 to May 2019 and a partner at Cain Watters since 1983. Mr. Cain founded Cain Watters in 1983 as an accounting and investment advisory firm specializing in financial planning, working exclusively with members of the dental profession, and served as its President from 1983 until 2008; he is currently a partner of Cain Watters. Mr. Cain previously served on the board of directors of T Bancshares and the Bank from their formation until October 2005. Mr. Cain is a graduate of Baylor University where he received both a Bachelor of Business Administration and Master of Public Accounting degree. He holds certified public accountant and investment advisor representative designations. We believe Mr. Cain brings to our board of directors significant investment, financial planning and financial skills important to the oversight of enterprise and operational risk management of the Company.

**Steven B. "Brad" Clapp.** Mr. Clapp has served as a director of the Company, T Bancshares and the Bank since May 2017 and served as a board member of Tectonic Holdings from 2015 until its merger with the Company in May 2019. Mr. Clapp is a partner of Cain Watters and currently serves as the Partner in Charge of Information Technology, in addition to his duties of managing the financial plans of approximately 60-70 families. He has served the clients of the firm in various planning roles including the development of financial plans, tax planning and practice valuations. He joined Cain Watters in 1998 and became a partner in 2008. Mr. Clapp started his career at the international accounting firm KPMG in 1996. Mr. Clapp is a graduate of The University of Arkansas and The University of Denver. We believe Mr. Clapp brings to the board of directors strong investment, accounting and financial skills important to the oversight of our financial reporting and operational risk management.

**Patrick Howard.** Mr. Howard serves as President and a director of the Company. Prior to such appointment in connection with the Tectonic Merger, Mr. Howard served as President and Chief Executive Officer of the Company since May 2017, President and Chief Executive Officer of the Bank since 2010 and as the Managing Officer and director of the Bank and T Bancshares since 2007. During his tenure at the Bank, he has overseen the growth of the retirement and trust division to over \$1.9 billion in assets, the acquisition of The Nolan Company third party administrator, the organic growth of the Bank to over \$700 million in assets, and the acquisition of Integra Funding, the Bank's factoring division. He developed an operating culture based on strong internal controls and regulatory compliance. In addition, prior to its acquisition by the Company in May 2017, T Bancshares was an SEC reporting company, and Mr. Howard was jointly responsible for T Bancshares' SEC filings and compliance. Mr. Howard previously served as the Executive Vice President and Chief Operating Officer of a savings bank that he helped grow from \$50 million to \$2.2 billion over an 11-year period. Mr. Howard graduated magna cum laude from the University of Texas at San Antonio.

**Eric Langford.** Mr. Langford is a founding director of T Bancshares and the Bank since February 2003 and a director of the Company since May 2017. He has been active in the real estate industry for almost 40 years as an investor and developer. Since 1995, he has managed Langford Property Company. He previously served as Senior Vice President for two leading national real estate firms, Opus West Corporation from 2003 to 2006 and Koll Development Company from 1993 to 2000. A 65-year resident of Dallas, Mr. Langford was the founding President of North Texas Commercial Association of Realtors, which awarded him with the Stemmons Service Award, the highest honor in the Dallas real estate industry. Mr. Langford is a *magna cum laude* graduate from Texas A&M University. We believe that Mr. Langford's expansive business experience in the real estate industry provides leadership and management experience that is beneficial to the board of directors.

**Thomas McDougal, DDS.** Dr. McDougal has been a director of T Bancshares and the Bank since February 2003 and a director of the Company since May 2017. He served as Captain in the United States Air Force for two years. Dr. McDougal is a practicing dentist, having been in private practice since 1970. In 1970, Dr. McDougal founded his dental practice in Richardson, Texas which today is McDougal and Richards Dentistry. He received a Bachelor of Science degree from Oklahoma State University and his Doctor of Dental Surgery degree from Baylor University. He serves on the board of directors of several national dental associations, and served as President of the Dallas County Dental Society and the American Academy of Dental Practice. He has been an adjunct professor at Baylor College of Dentistry since 2008 and has been on the teaching faculty at the Center for Aesthetic and Restorative Dentistry since 2005. We believe Dr. McDougal's experience as a practicing dentist and leadership roles in the dental community provide particular benefit in overseeing our dental lending program and trust line of business as well as his corporate governance experience.

**Thomas R. Sanders.** Mr. Sanders has served as a director of the Company, T Bancshares and the Bank since May 2017 and was a director of Tectonic Holdings from 2015 until the Tectonic Merger. Mr. Sanders has been a partner of Cain Watters since 2008 after joining the firm in 2002. He currently serves as a member of the mentoring committee as well as the internal quality control committee helping financial planners at CWA grow personally and professionally. Mr. Sanders also manages the financial planning relationship for more than 65 of the firm's clients representing assets under management approximating \$300 million. Mr. Sanders started his career at Deloitte where he spent four years in their tax department including several international assignments. Mr. Sanders graduated from Baylor University in 1998 with a Bachelor of Business Administration and a Masters of Science in Taxation. We believe that Mr. Sanders' tax expertise enhances the skill set of our board of directors.

**A. Haag Sherman.** In connection with the Tectonic Merger, Mr. Sherman was appointed as a director and the Chief Executive Officer of the Company. Prior to such appointment, Mr. Sherman served as Chairman of the Company from November 2017 until the Tectonic Merger, and as Chairman of T Bancshares and the Bank since May 2017. Mr. Sherman was also the Chief Executive Officer and a director of Tectonic Holdings from 2015 until May 2019. Prior to joining the Company, Mr. Sherman co-founded Salient Partners, LP (a Houston-based investment firm) in 2002 and served in various executive positions, including Chief Executive Officer and Chief Investment Officer, through October 2011. In addition, he previously served as an executive officer and partner of The Redstone Companies from 1998 to 2002 where he, among other things, managed a private equity portfolio (where he was responsible for two finance companies). Mr. Sherman has served as a director of Hilltop Holdings, Inc. since its acquisition of PlainsCapital Corporation in November 2012. He previously served as a director of PlainsCapital from September 2009 to November 2012. Mr. Sherman has served as a member of the board of directors of CBIZ, Inc. since August 2020. He currently serves on the Executive Committee of Episcopal High School in Bellaire, Texas and on the Board of Trustees of the Episcopal Health Foundation. Mr. Sherman graduated cum laude from Baylor University in 1988 with a Bachelor of Business Administration with majors in Accounting and Economics and received a Juris Doctorate, with honors, from the University of Texas School of Law in 1992. Mr. Sherman previously served as an adjunct professor of law at The University of Texas School of Law. Mr. Sherman previously practiced corporate law at Akin, Gump, Strauss, Hauer & Feld, LLP from 1992 to 1996 and was an auditor at Price Waterhouse, a public accounting firm, from 1988 to 1989. Mr. Sherman is an attorney and certified public accountant. We believe that Mr. Sherman's leadership, board expertise, legal background and experience in financial services, including banking, trust and finance companies, qualify him to serve on our board of directors.

**Daniel C. Wicker.** Mr. Wicker has served as a director of the Company, T Bancshares and the Bank since May 2017. In addition, Mr. Wicker was a director of Tectonic Holdings from 2015 until May 2019. Mr. Wicker has been a partner of Cain Watters since 2008 after joining the firm in 1997. Mr. Wicker currently serves as the Partner in Charge of Operations, overseeing the financial planning process as well as the Cain Watters planners, among other operational responsibilities. He has served the clients of the firm in various planning roles including the development of financial plans, tax planning and practice valuations. Mr. Wicker started his career at the international accounting firm KPMG where he worked from 1993 to 1997. Mr. Wicker graduated from Kansas State University in 1993. We believe that Mr. Wicker's leadership and strategic planning abilities qualify him to serve on our board of directors.

### ***Executive Officers and Other Significant Employees***

**Ken Bramlage.** Mr. Bramlage has served as Executive Vice President and Chief Financial Officer of the Company since May 2017 and holds the same positions at T Bancshares and the Bank. He joined the Bank in July 2008 as Vice President and Controller and was promoted to Senior Vice President and Chief Financial Officer in April 2010 and Executive Vice President and Chief Financial Officer in 2013. Prior to joining the Company, Mr. Bramlage was Vice President and Controller for a \$1.0 billion savings bank headquartered in Olathe, Kansas since April 1999. Mr. Bramlage earned a Bachelor of Administration degree in Accounting at Kansas State University in 1984 and became licensed as a certified public accountant in the state of Texas in 1985.

**David Clifford.** Mr. Clifford was appointed as Chief Operating Officer of the Company effective November 14, 2023. Prior to such date, he had served as Chief Strategy Officer of the Company since January 1, 2018. Before joining the Company, from 2004 through 2011, Mr. Clifford served as the Director of Marketing and Intermediary Services at Salient Partners, LP (“Salient”) and was responsible for retail sales and distribution efforts. Mr. Clifford also served as the Head of Salient’s Sales and Distribution Platform, where he assisted in the development and marketing of alternative investment programs. Mr. Clifford began his career as an Associate and Consultant in the Helsinki, Finland office at McKinsey & Company (“McKinsey”). While at McKinsey, Mr. Clifford focused on serving high technology and telecommunications companies in the Nordic region. Mr. Clifford has a Bachelor of Business Administration in Finance from the University of Texas at Austin and a Masters of Business Administration from the Helsinki School of Economics.

### **Code of Business Conduct and Ethics**

We have adopted a Code of Business Conduct and Ethics, which is applicable to all directors, officers and employees of the Company and the Bank. The full text of our Code of Business Conduct and Ethics is posted to the Company’s website which is located at <https://www.t.financial/investors#corporategovernance>. We will post any amendments to our Code of Business Conduct and Ethics, or waivers of its requirements, on our website.

### **Audit Committee**

The members of our Audit Committee are Eric Langford, Thomas McDougal, and Barb Bomersbach, with Barb Bomersbach serving as chair of our Audit Committee. Our board of directors has evaluated the independence of each of the members of our Audit Committee and has affirmatively determined that each of the members of our Audit Committee (1) is an “independent director” under the rules of NASDAQ, (2) satisfies the additional independence standards under applicable SEC rules for audit committee service, and (3) has the ability to read and understand fundamental financial statements. The board of directors has determined that Barb Bomersbach qualifies as an “audit committee financial expert,” as defined by the SEC. The board of directors believes that the members of the Audit Committee are able to read and understand the consolidated financial statements of the Company and are familiar with the Company and its business.

### **Delinquent Section 16(a) Reports**

Section 16(a) of the Exchange Act requires our directors and executive officers and persons who own more than 10% of our outstanding common stock to file reports of ownership and changes in ownership of our equity securities, including our common stock with the SEC. Such persons are required by the SEC’s regulations to furnish us with copies of all reports they file pursuant to Section 16.

Based solely on a review of the reports furnished to us, or written representations from reporting persons that all reportable transactions were reported, we believe that during the fiscal year ended December 31, 2023, our officers, directors and greater than 10% owners timely filed all reports they were required to file under Section 16(a).

## Item 11. Executive Compensation

We are an “emerging growth company,” as defined in the JOBS Act and a “smaller reporting company,” as defined in Item 10(f)(1) of Regulation S-K. As such, we are eligible to take advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not emerging growth companies or smaller reporting companies. These include, but are not limited to, reduced disclosure obligations regarding executive compensation.

Our “named executive officers,” which consist of our principal executive officer and the two other most highly compensated executive officers, are A. Haag Sherman, Chief Executive Officer, Patrick Howard, President and David Clifford, Chief Operating Officer.

### Summary Compensation Table

The following table sets forth information regarding the compensation paid to, awarded to, or earned by our named executive officers for the fiscal years indicated.

Name and Principal Position	Year	Salary (\$)	Bonus (\$)	Stock Awards (\$)	Option Awards (\$)	Non-Equity Incentive Plan Compensation (\$)	All Other Compensation <sup>(1)</sup> (\$)	Total (\$)
A. Haag Sherman	2023	375,000	325,000	—	—	—	12,293	712,293
Chief Executive Officer	2022	360,000	375,000	—	—	—	11,222	746,222
Patrick Howard	2023	350,000	425,000	—	—	—	15,181	790,181
President	2022	328,333	175,000	—	—	—	14,273	517,606
David Clifford	2023	375,000	150,000	—	—	—	11,730	536,730
Chief Operating Officer	2022	350,000	150,000	—	—	—	10,848	510,848

(1) The amounts shown in this column are composed of the following items:

Name	Year	Company 401(k) Match	Life Insurance Premiums	Total “All Other Compensation”
Haag Sherman	2023	\$ 11,550	\$ 743	\$ 12,293
	2022	10,500	722	11,222
Patrick Howard	2023	\$ 11,550	\$ 3,631	\$ 15,181
	2022	10,675	3,598	14,273
David Clifford	2023	\$ 11,550	\$ 180	\$ 11,730
	2022	10,675	173	10,848

### General

We compensate our named executive officers through a combination of base salary, annual discretionary bonuses, equity awards and other benefits, including perquisites. Our board of directors believes the executive compensation packages that we provide to our executives, including the named executive officers, should reward performance. Each element of compensation is designed to achieve a specific purpose and to contribute to a total package that is competitive with similar packages provided by other institutions that compete for the services of individuals like our named executive officers.

### Base Salary

We provide each of our named executive officers with a competitive fixed annual base salary. The base salaries for our named executive officers are reviewed annually by the board of directors by taking into account the results achieved by each executive, his or her future potential, scope of responsibilities and experience and competitive pay practices. Based upon the comprehensive review, the board of directors has determined the base salaries to be equitable and competitive for our market.

### Bonuses

Our named executive officers receive incentive and/or bonus payments based on their employment agreements, as described below.

## Stock-Based Compensation Awards

Stock-based compensation awards may consist of options to acquire shares of our common stock, restricted stock awards, restricted stock units or performance stock units issued pursuant to the Amended and Restated T Acquisition, Inc. 2017 Equity Incentive Plan (the “Amended and Restated Equity Plan”), which, as described more fully below, allows the Compensation Committee to establish the terms and conditions of the awards, subject to the terms of the Amended and Restated Equity Plan.

## Other Benefits and Perquisites

The named executive officers participate in our broad-based employee welfare benefit plans, such as medical, dental, vision, supplemental disability and term life insurance. The named executive officers also participate in our 401(k) plans. Under the T Bank, N.A. Employees Savings Plan, in which Mr. Howard is a participant, we match 100% of an employee’s contribution up to the first 1% and 50% up to next 5% of such employee’s salary up to the 401(k) limit. Under the Tectonic Retirement Plan and Trust, in which Mr. Sherman and Mr. Clifford are participants, we match 100% of an employee’s contribution up to the first 1% and 50% up to next 5% of such employee’s salary up to the 401(k) limit, identical to the T Bank, N.A. Employees Savings Plan. The named executive officers are provided the same benefits, and participate in the cost at the same rate, as all other employees.

We provide our named executive officers with certain perquisites that we believe are reasonable and consistent with our overall compensation program to better enable us to attract and retain superior employees for key positions. The Compensation Committee will review the levels of perquisites and other personal benefits provided to named executive officers. Based on this periodic review, perquisites will be awarded or adjusted on an individual basis. The perquisites received by our named executive officers in 2023 and 2022 included \$2,839 for each year paid by the Company on behalf of Mr. Howard toward a \$3,000,000 key man life insurance policy for Mr. Howard. In accordance with his employment agreement, 50% of the death benefit of this policy is payable to Mr. Howard’s named beneficiaries.

## Employment Agreements and Arrangements

We have entered into an employment agreement with Mr. Sherman and amended and restated the employment agreement with Mr. Howard. The following is a summary of the material terms of each such agreement. The Company has not entered into any material plan, contract or arrangement to which Mr. Clifford is a party.

**Haag Sherman.** Mr. Sherman’s employment agreement has an initial term of four years and automatic one-year renewals thereafter unless either party provides written notice of its intent not to renew at least 90 days prior to the renewal date. Under Mr. Sherman’s employment agreement, he is entitled to an annual base salary that is currently \$375,000 and is eligible to receive an annual performance-based bonus payment to the extent the applicable performance criteria are satisfied.

Mr. Sherman is also eligible to receive certain other employee benefits and perquisites in accordance with our established policies, as described above. In addition, Mr. Sherman’s employment agreement provides for certain restrictive covenants and severance benefits in the event of a qualifying termination of employment and certain payments in connection with a “change in control” of the Company. See “—Potential Payments upon a Termination of Employment or a Change in Control.”

**Patrick Howard.** As amended and restated, the employment agreement is for a term expiring on May 14, 2024 and automatic one-year renewals thereafter unless either party provides written notice of its intent not to renew at least 90 days prior to the renewal date. Under Mr. Howard’s amended and restated employment agreement, he is entitled to an annual base salary that is currently \$350,000 and is eligible to receive an annual performance-based bonus payment to the extent the applicable performance criteria are satisfied.

In connection with the execution of his original employment agreement, Mr. Howard received options to purchase 50,000 shares of our common stock with an exercise price equal to \$2.15, which vested on May 15, 2020 (the “3-Year Tectonic Financial Options”), and options to purchase 50,000 shares of our common stock with an exercise price equal to \$2.15, which vested on May 15, 2021 (the “4-Year Tectonic Financial Options”). In addition, Mr. Howard entered into a unit option agreement with Tectonic Holdings and received options to purchase 50,000 membership units of Tectonic Holdings with an exercise price equal to \$3.55, which vested on May 15, 2020 (the “3-Year Tectonic Holdings Options”), and he received options to purchase 50,000 membership units of Tectonic Holdings with an exercise price equal to \$3.55, which vested on May 15, 2021 (the “4-Year Tectonic Holdings Options”). As a result of the Tectonic Holdings Merger and the 1-for-2 reverse stock split of the Company’s common stock, the 3-Year Tectonic Holding Options were converted into options to purchase 25,000 shares of the Company’s common stock at an exercise price of \$5.70, which is the sum of the exercise prices of the 3-Year Tectonic Holdings Options and the 3-Year Tectonic Financial Options, and the 4-Year Tectonic Holding Options were converted into options to purchase 25,000 shares of the Company’s common stock at an exercise price of \$5.70, which is the sum of the exercise prices of the 4-Year Tectonic Holdings Options and the 4-Year Tectonic Financial Options. Additionally, as a result of the Tectonic Holdings Merger and the 1-for-2 reverse stock split of the Company’s common stock, the 3-Year Tectonic Financial Options became exercisable for 25,000 shares of the Company’s common stock at an exercise price of \$5.70 and the 4-Year Tectonic Financial Options became exercisable for 25,000 shares of the Company’s common stock at an exercise price of \$5.70.

Mr. Howard is also eligible to receive certain other employee benefits and perquisites in accordance with our established policies, as described above. In addition, Mr. Howard’s amended and restated employment agreement provides for certain restrictive covenants and severance benefits in the event of a qualifying termination of employment and certain payments in connection with a “change in control” of the Company. See “—Potential Payments upon a Termination of Employment or a Change in Control.”

**David Clifford.** Under Mr. Clifford’s employment arrangement, he is entitled to an annual base salary that is currently \$375,000 and is eligible to receive an annual performance-based bonus payment to the extent the applicable performance criteria are satisfied.

Mr. Clifford is also eligible to receive certain other employee benefits and perquisites in accordance with our established policies, as described above.

#### **Amended and Restated T Acquisition, Inc. 2017 Equity Incentive Plan**

The board of directors and Company shareholders have adopted the Amended and Restated Equity Plan. The Amended and Restated Equity Plan is intended to enable the Company to remain competitive and innovative in its ability to attract, motivate, reward, and retain the services of key employees and outside directors. The Amended and Restated Equity Plan allows for the granting of incentive stock options, non-qualified stock options, stock appreciation rights (“SARs”), restricted stock, restricted stock units, performance awards, dividend equivalent rights, and other awards which may be granted singly, in combination, or in tandem. The Amended and Restated Equity Plan is expected to provide flexibility to the Company’s compensation methods in order to adapt the compensation of key employees and outside directors to a changing business environment (after giving due consideration to competitive conditions and the impact of accounting rules and federal tax laws).

The following is a brief description of the Amended and Restated Equity Plan and is qualified in its entirety by reference to the Amended and Restated Equity Plan that is filed as an exhibit to this Form 10-K.

**Purpose.** The purpose of our Amended and Restated Equity Plan is to attract, motivate, reward, and retain the services of key employees and outside directors by providing them with additional incentives, and to promote the success of our Company’s business.

**Administration.** Our board of directors or one or more committees appointed by our board of directors will administer the Amended and Restated Equity Plan.

**Eligibility.** Persons eligible to receive awards under the Amended and Restated Equity Plan include our officers, employees, consultants and members of our board of directors. Our board of directors or one or more committees appointed by our board of directors will determine from time to time the participants to whom awards will be granted.



***Authorized Shares; Limits on Awards.*** The maximum number of common shares that may be issued or transferred pursuant to awards under the Amended and Restated Equity Plan equals 750,000 shares, all of which may be subject to incentive stock option treatment. The Current Plan reserves 750,000 shares of our common stock, of which 230,000 stock options and 210,000 restricted stock grants have been awarded, however 30,000 were forfeited and thus returned to the reserve under the Amended and Restated Equity Plan, leaving 340,000 remaining available for issuance.

The maximum aggregate number of common shares that may be issued pursuant to all awards under the Amended and Restated Equity Plan shall increase annually on the first day of each fiscal year following the adoption of the Amended and Restated Equity Plan by the number of common shares equal to the lesser of (i) three percent of the total issued and outstanding common shares on the first day of such fiscal year, or (ii) such lesser amount determined by our board of directors.

***Adjustments or Changes in Capitalization.*** In the event of any change in the outstanding common shares by reason of a stock split, stock dividend or other non-recurring dividends or distributions, recapitalization, merger, consolidation, spin-off, combination, repurchase or exchange of stock, reorganization, liquidation, dissolution or other similar corporate transaction that affects our common stock, the aggregate number of shares of common stock available under the Amended and Restated Equity Plan or subject to outstanding awards (including the exercise price of any awards) shall be adjusted as our board of directors deems necessary or appropriate.

***Incentive Awards.*** The Amended and Restated Equity Plan authorizes stock options, SARs, restricted stock, restricted stock units, performance-based awards, as well as other awards (described in the Amended and Restated Equity Plan) that are responsive to changing developments in management compensation. The Amended and Restated Equity Plan retains the flexibility to offer competitive incentives and to tailor benefits to specific needs and circumstances. Any award may be paid or settled in cash. An option or SAR will expire, or other award will vest, in accordance with the schedule set forth in the applicable award agreement.

***Stock Option.*** A stock option is the right to purchase common shares at a future date at a specified price per share generally equal to, but no less than, the fair market value of a share on the date of grant. An option may either be an Incentive Stock Option, or ISO, or a nonstatutory stock option, or NSO. ISO benefits are taxed differently from NSOs, and are subject to more restrictive terms and are limited in amount by the Code and the Amended and Restated Equity Plan. Full payment for shares purchased on the exercise of any option must be made at the time of such exercise in a manner approved by our board of directors.

***SARs.*** A SAR is the right to receive payment of an amount equal to the excess of the fair market value of a common share on the date of exercise of the SAR over the base price of the SAR. The base price will be established by our board of directors at the time of grant of the SAR but will not be less than the fair market value of a share on the date of grant. SARs may be granted in connection with other awards or independently.

***Restricted Stock.*** A restricted stock award is typically for a fixed number of common shares subject to restrictions. Our board of directors specifies the price, if any, the participant must pay for such shares and the restrictions (which may include, for example, continued service and/or performance standards) imposed on such shares. A stock bonus may be granted by our board of directors to any eligible person to reward exceptional or special services, contributions or achievements in the manner and on such terms and conditions (including any restrictions on such shares) as determined from time to time by our board of directors. The number of shares so awarded shall be determined by our board of directors and may be granted independently or in lieu of a cash bonus.

***Restricted Stock Units.*** A restricted stock unit is similar to a SAR except that it entitles the recipient to receive an amount equal to the fair market value of a common share.

***Performance-Based Awards.*** Our board of directors may designate any award, the exercisability or settlement of which is subject to the achievement of performance conditions, as a performance-based award. In order to qualify as performance-based compensation, the performance objective(s) used for the performance-based award must be from the list of performance objectives set forth in the Amended and Restated Equity Plan. The performance objectives set forth in the Amended and Restated Equity Plan are: interest income and expense; net earnings or net income; net interest margin; efficiency ratio; reduction in non-accrual loans and non-interest expense; growth in non-interest income and ratios to earnings assets; net revenue growth and ratio to earning assets; capital ratios; asset or liability interest rate sensitivity and gap; effective tax rate; deposit growth and composition; liquidity management; securities portfolio (value, yield, spread, maturity, or duration); asset growth and composition (loans, securities); non-interest income (e.g., fees, premiums and commissions, loans, wealth management, treasury management, insurance, funds management) and expense; overhead ratios, productivity ratios; credit quality measures; return on assets; return on equity; economic value of equity; compliance and CAMELS or other regulatory ratings; internal controls; enterprise risk measures (e.g., interest rate, loan concentrations, portfolio composition, credit quality, operational measures, compliance ratings, balance sheet, liquidity, insurance); volume in production or loans; non-performing asset or non-performing loan levels or ratios or loan delinquency levels; provision for credit losses or net charge-offs; cash flow; cost; revenues; sales; ratio of debt to debt plus equity; net borrowing, credit quality or debt ratings; profit before tax; economic profit; earnings before interest and taxes; earnings before interest, taxes, depreciation and amortization; gross margin; profit margin; earnings per share; operating earnings; capital expenditures; expenses or expense levels; economic value added; ratio of operating earnings to capital spending or any other operating ratios; free cash flow; net profit; net sales; net asset value per share; the accomplishment of mergers, acquisitions, dispositions, public offerings or similar extraordinary business transactions; sales growth; price of the Company's stock; return on investment; equity or shareholders' equity; market share; inventory levels, inventory turn or shrinkage; customer satisfaction; or total shareholder return. Our board of directors may select any number of performance objectives from this list of performance objectives when establishing the performance measures of a performance-based award, but such objectives must be set no later than 90 days after the beginning of the applicable performance period. The Amended and Restated Equity Plan allows performance objectives to be described in terms of objectives that are related to an individual participant or objectives that are company-wide or related to a subsidiary, division, department, region, function or business unit and may be measured on an absolute or cumulative basis or on the basis of percentage of improvement over time, and may be measured in terms of company performance (or performance of the applicable subsidiary, division, department, region, function or business unit) or measured relative to selected peer companies or a market index.

***Acceleration of Awards; Possible Early Termination of Awards.*** Upon a change in control of our Company, outstanding awards under the Amended and Restated Equity Plan will be assumed or substituted on the same terms. However, if the successor corporation does not assume or substitute the outstanding awards, then vesting of these awards will fully accelerate, and in the case of options or SARs, will become immediately exercisable. For this purpose, a change in control is defined to include certain changes in the majority of our board of directors, the sale of all or substantially all of our Company's assets, and the consummation of certain mergers or consolidations.

***Transfer Restrictions.*** Subject to certain exceptions, awards under the Amended and Restated Equity Plan are not transferable by the recipient other than by will or the laws of descent and distribution and are generally exercisable, during the recipient's lifetime, only by him or her.

***Termination of or Changes to the Amended and Restated Equity Plan.*** Our board of directors may amend or terminate the Amended and Restated Equity Plan at any time and in any manner. Unless required by applicable law or listing agency rule, stockholder approval for any amendment will not be required. Unless previously terminated by our board of directors, the Amended and Restated Equity Plan will terminate on March 27, 2029. Generally speaking, outstanding awards may be amended, subject, however, to the consent of the holder if the amendment materially and adversely affects the holder.

## Federal Income Tax Treatment of Awards under the Amended and Restated Equity Plan

Federal income tax consequences (subject to change) relating to awards under the Amended and Restated Equity Plan are summarized in the following discussion. This summary is not intended to be exhaustive and, among other considerations, does not describe the deferred compensation provisions of Section 409A of the Code to the extent an award is subject to and does not satisfy those rules, nor does it describe state, local, or international tax consequences.

For NSOs, the Company is generally entitled to deduct (and the optionee recognizes taxable income in) an amount equal to the difference between the option exercise price and the fair market value of the shares at the time of exercise. For ISOs, our Company is generally not entitled to a deduction nor does the participant recognize income at the time of exercise. The current federal income tax consequences of other awards authorized under the Amended and Restated Equity Plan generally follow certain basic patterns: SARs are taxed and deductible in substantially the same manner as NSOs; nontransferable restricted stock subject to a substantial risk of forfeiture results in income recognition equal to the excess of the fair market value over the price paid (if any) only at the time the restrictions lapse (unless the recipient elects to accelerate recognition as of the date of grant); bonuses and performance share awards are generally subject to tax at the time of payment; cash-based awards are generally subject to tax at the time of payment; and compensation otherwise effectively deferred is taxed when paid. Our Company will generally have a corresponding deduction at the time the participant recognizes income. However, as for those awards subject to ISO treatment, our Company would generally have no corresponding compensation deduction.

## Outstanding Equity Awards at Fiscal Year End

The following table sets forth our outstanding equity awards as of December 31, 2023:

Name	Option Awards				Stock Awards	
	Number of Securities Underlying Unexercised Options Exercisable (#)	Number of Securities Underlying Unexercised Options Unexercisable (#)	Option Exercise Price	Option Expiration Date	Number of Shares or Units of Stock That Have Not Vested (#)	Market Value of Shares or Units of Stock That Have Not Vested (\$)
A. Haag Sherman	—	—	\$ —	—	—	—
Patrick Howard	50,000 (1)(2)	—	\$ 5.70 (2)	05/15/2027	30,000 (4)	\$ 564,000
	50,000 (1)(3)	—	5.70 (3)	05/15/2027	—	—
David Clifford	—	—	\$ —	—	20,000 (5)	\$ 376,000

- (1) 25,000 stock options vested on May 15, 2020, and 25,000 stock options vested May 15, 2021.
- (2) Represents 3-Year Tectonic Holding Options to purchase 25,000 shares of the Company's common stock at an exercise price of \$5.70 and 3-Year Tectonic Financial Options to purchase 25,000 shares of the Company's common stock at an exercise price of \$5.70.
- (3) Represents 3-Year Tectonic Holding Options to purchase 25,000 shares of the Company's common stock at an exercise price of \$5.70 and 3-Year Tectonic Financial Options to purchase 25,000 shares of the Company's common stock at an exercise price of \$5.70.
- (4) 30,000 stock awards vested on December 31, 2023, and the remaining 30,000 stock awards vest on December 31, 2024.
- (5) 30,000 stock awards vested on December 31, 2023, and the remaining 20,000 stock awards vest: 10,000 on December 31, 2024 and 10,000 on December 31, 2025.

## Potential Payments Upon a Termination of Employment or a Change in Control

Below we have described the severance and other change in control benefits to which Mr. Sherman and Mr. Howard would be entitled upon a termination of employment and in connection with certain terminations of their employment or a change in control.

**Severance.** If we terminate Mr. Sherman’s employment for any reason other than for “cause” (as defined in each respective employment agreement), or the executive terminates his employment for “good reason” (as defined in each respective employment agreement), the executive shall be entitled to (A) receive base salary through the date of such termination, (B) pay in lieu of any unused vacation in accordance with our normal practice, (C) any health benefits to which the executive is receiving immediately prior to such termination at the same expense as other employees for such selected employee benefit plans and programs for a period of 24 months (unless otherwise covered by another plan), and (D) a severance payment to be paid in 24 equal monthly installments, which equals an amount of cash equal to two times the sum of (x) the executive’s base salary at the time of termination, (y) the average annual bonus (excluding change of control payments) paid to the executive with respect to each of the three prior fiscal years, plus (z) a pro-rated annual bonus for the year in which the executive’s employment terminates. All of the amounts and benefits described above are conditioned upon the executive executing a general release and waiver of claims in a form provided by us at the time of termination.

If we terminate Mr. Howard’s employment for any reason other than for “cause,” or the executive terminates his employment for “good reason,” the executive shall be entitled to (A) receive base salary through the date of such termination, (B) pay in lieu of any unused vacation in accordance with our normal practice, (C) any health benefits to which the executive is receiving immediately prior to such termination at the same expense as other employees for such selected employee benefit plans and programs for a period of 24 months (unless otherwise covered by another plan), and (D) a severance payment to be paid in 24 equal monthly installments, which equals an amount of cash equal to two times the sum of (x) the executive’s base salary at the time of termination, (y) the average annual bonus (excluding change of control payments) paid to the executive with respect to each of the three prior fiscal years, plus (z) a pro-rated annual bonus for the year in which the executive’s employment terminates. All of the amounts and benefits described above are conditioned upon the executive executing a general release and waiver of claims in a form provided by us at the time of termination.

**Change in Control.** Subject to the terms of the respective employment agreements, in the event of a change in control (as defined in the employment agreement of Mr. Howard, Mr. Howard will be eligible to receive a cash lump sum payment equal to 2.99 times his base amount (as defined in Section 280G(b)(3) of the Code) payable by us within 30 days upon a change in control or under such other terms as may be mutually agreed. In the event that Mr. Howard is also entitled to any of the severance payments and benefits discussed above, any change in control will be offset by such amount.

## Director Compensation

The following table shows compensation paid to members of our board of directors and the board of directors of the Company and the Bank during 2023. The Company’s non-employee directors received a fee of \$3,750 per meeting paid in cash. For the joint board meetings held by the Company and the Bank, non-employee directors received a fee of \$1,000 per meeting paid in cash, as well as the following committee meeting fees: \$250 per Audit Committee meeting, \$250 per Asset Liability Committee meeting, \$250 per Technology Committee meeting, \$250 per Trust Committee meeting, \$125 per Loan Committee meeting, \$125 per Executive Committee meeting and \$125 per Compensation Committee meeting, all paid in cash.

	Fees Earned or Paid in Cash	Stock/Option Awards(1)	Total
George L. Ball	\$ —	\$ —	\$ —
Barb Bomersbach	30,000	—	30,000
Darrell W. Cain	—	—	—
Steven B. Clapp	10,250 (2)	—	10,250
Patrick Howard	—	—	—
Eric Langford	35,000 (3)	—	35,000 (3)
Thomas McDougal	35,500 (4)	—	35,500 (4)
Thomas R. Sanders	11,000 (5)	—	11,000 (5)
A. Haag Sherman	—	—	—
Daniel C. Wicker	11,875 (6)	—	11,875 (6)

(1) No stock/option awards were made to the directors during 2023.

(2) Represents fees paid in cash for serving on the boards of directors of the Company and the Bank.

(3) Includes \$10,000 in fees paid in cash for serving on the boards of directors of the Company and the Bank.

(4) Includes \$10,500 in fees paid in cash for serving on the boards of directors of the Company and the Bank.

(5) Represents fees paid in cash for serving on the boards of directors of the Company and the Bank.

(6) Represents fees paid in cash for serving on the boards of directors of the Company and the Bank.

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

The following table provides information regarding the beneficial ownership of our capital stock as of March 27, 2023 for:

- each of our directors;
- each of our named executive officers;
- all of our directors and executive officers as a group; and
- each shareholder who beneficially owns more than 5% of our common stock.

We have determined beneficial ownership in accordance with the rules of the SEC. These rules generally provide that a person is the beneficial owner of securities if such person has or shares the power to vote or direct the voting of securities, or to dispose or direct the disposition of securities, or has the right to acquire such powers within 60 days. Shares of common stock that may be acquired by an individual or group within sixty days of March 27, 2024, pursuant to the exercise of options, warrants or other rights, are deemed to be outstanding for the purpose of computing the percentage ownership of such individual or group, but are not deemed to be outstanding for the purpose of computing the percentage ownership of any other person shown in the table. The table below calculates the percentage of beneficial ownership of our common stock based on 7,102,680 shares of voting common stock and 1,725,000 shares of non-voting Series B preferred stock outstanding as of March 27, 2024. Except as disclosed in the footnotes to this table and subject to applicable community property laws, we believe that each person identified in the table has sole voting and investment power over all of the shares shown opposite such person's name.

Except as indicated below, the address for each shareholder listed in the table below is: 16200 Dallas Parkway, Suite 190, Dallas, Texas 75248.

Name of Beneficial Owner	Common Stock Beneficially Owned		Series B Preferred Stock Beneficially Owned	
	Number(7)	Percentage	Number	Percentage
<b>Directors and Named Executive Officers:</b>				
George L. Ball	208,457	2.93%	500	*
Barb Bomersbach	-	-	2,500	*
Darrell W. Cain <sup>(1)</sup>	215,100	3.03%	7,000	*
Steven B. "Brad" Clapp <sup>(1),(2)</sup>	215,100	3.03%	-	-
David Clifford	60,000	*	-	-
Patrick Howard	118,445 (3),(4)	1.64%	7,500	*
Eric Langford	250 (4)	*	-	-
Thomas McDougal	250 (4)	*	29,967	1.74%
Thomas R. Sanders	215,100	3.03%	-	-
A. Haag Sherman <sup>(5)</sup>	2,121,000	29.86%	5,000	*
Daniel C. Wicker	215,100	3.03%	5,000	*
<b>Directors and Executive Officers as a Group (12 Persons)</b>	<b>3,388,008</b>	<b>47.04%</b>	<b>57,467</b>	<b>3.33%</b>
<b>Greater than 5% Shareholders:</b>				
Tracey Bolt <sup>(6)</sup>	405,173	5.70%	-	-

\* Represents beneficial ownership of less than 1%.

(1) All shares of common stock are pledged to a third party bank under the terms of a loan agreement, which loan is current.

(2) Includes 5,000 shares held in an IRA for the benefit of Mr. Clapp's spouse.

(3) Includes options covering 100,000 shares of our common stock, 50,000 of which vested on May 15, 2020 and 50,000 of which vested on May 15, 2021.

(4) 250 of these shares are subject to a repurchase right by the Company upon (i) the retirement of such individual as a director of the Bank, (ii) notice by either party of its desire to sell or repurchase the shares, as the case may be, or (iii) the filing of a bankruptcy petition affecting the director.

(5) Includes 1,739,000 shares held by The Sherman 2018 Irrevocable Trust for which Mr. Sherman serves as trustee and 370,000 shares held by Sherman Tectonic FLP LP for which Mr. Sherman serves as the Chief Executive Officer of the general partner. Mr. Sherman has granted an option to certain other employees of Cain Watters to purchase from him or one of his affiliates up to 25,000 shares of our common stock at an exercise price of \$2.15.

(6) Includes 27,878 shares held by The Crane Basin Irrevocable Trust and 27,878 shares held by The Hamilton Irrevocable Trust.

(7) Included in the beneficial ownership tabulations are options to purchase 100,000 shares of common stock for Mr. Howard and 10,000 shares of common stock for Mr. Bramlage.

## **Item 13. Certain Relationships and Related Transactions and Director Independence**

### **Controlled Company**

We are a “controlled company” within the meaning of the NASDAQ corporate governance standards. As a result, although the members of our Audit Committee are required to be independent, we are not required to have a majority of our board of directors be independent, nor are we required to have a compensation committee or an independent nominating function under the NASDAQ rules. We intend to avail ourselves of the controlled company exemptions while we remain a controlled company.

### **Director Independence**

Our Series B preferred stock is listed on the NASDAQ Global Market and, consequently, we are required to comply with the rules of the NASDAQ Stock Market with respect to the independence of directors who serve on our board of directors and its committees. Under the rules of NASDAQ, a majority of the members of the board of directors must be “independent directors” by the one-year anniversary of the time we cease to be a controlled company. The rules of NASDAQ, as well as those of the SEC, impose several other requirements with respect to the independence of our directors. Applying these standards, our board of directors has determined that each of Eric Langford, Thomas McDougal and Barb Bomersbach is an “independent director” as that term is defined in Rule 5605(a)(2) of the NASDAQ rules. The board of directors has also determined that the members of the Audit Committee are independent under the heightened standards of independence required by Section 5605(c)(2)(A) of the NASDAQ rules. In making these determinations, the board of directors considered the banking relationships with directors and their related interests which we enter into in the ordinary course of our business, the arrangements which are disclosed below in this Item 13 and the compensation arrangements described in Item 12 of this Form 10-K.

### **Certain Relationships and Related Party Transactions**

#### **Policies and Procedures Regarding Related Person Transactions**

Transactions by us or the Bank with related persons are subject to regulatory requirements and restrictions. These requirements and restrictions include the Affiliates Act and the Federal Reserve’s Regulation W (which governs certain transactions by the Bank with its affiliates) and the Federal Reserve’s Regulation O (which governs certain loans by the Bank to its executive officers, directors and principal shareholders). We have adopted policies to comply with these regulatory requirements and restrictions.

In addition, our board of directors has adopted a written policy governing the approval of related person transactions that complies with all applicable requirements of the SEC and NASDAQ concerning related person transactions. Related person transactions are transactions in which we are a participant, the amount involved exceeds \$120,000 and a related person has or will have a direct or indirect material interest. Related persons of the Company include directors (including nominees for election as directors), executive officers, beneficial holders of more than 5% of our capital stock and the immediate family members of these persons. Our executive management team, in consultation with outside counsel, as appropriate, will review potential related person transactions to determine if they are subject to the policy. In determining whether to approve a related person transaction, that committee will consider, among other factors, the fairness of the proposed transaction, the direct or indirect nature of the related person’s interest in the transaction, the appearance of an improper conflict of interest for any director or executive officer taking into account the size of the transaction and the financial position of the related person, whether the transaction would impair an outside director’s independence, the acceptability of the transaction to our regulators and the potential violations of other corporate policies.

In addition to the compensation arrangements with directors and executive officers described in “Executive Compensation” above, the following is a description of each transaction since January 1, 2022, and each proposed transaction in which:

- we have been or are to be a participant;
- the amount involved exceeds or will exceed \$120,000; and
- any of our directors, executive officers or beneficial holders of more than five percent of our capital stock, or any immediate family member, or person sharing the household with, any of these individuals (other than tenants or employees), had or will have a direct or indirect material interest.

## Other Transactions

**The Company.** The following are related party agreements and transactions to which the Company and/or any of its subsidiaries are a party and which are discussed in the next section.

**Cain Watters Services Agreement.** Darrell W. Cain, the founder of Cain Watters, was a co-founder of T Bancshares, the predecessor, and served on the board of directors of T Bancshares when it was founded in 2003. At his request, the Bank established the trust department to serve clients of Cain Watters, which was accomplished in 2006. Since that time, the Bank has served as a fiduciary and custodian on behalf of clients referred by Cain Watters and, given the importance of this strategic relationship for both parties, partners of Cain Watters currently occupy four board seats of the Company and own approximately 31.20% of the issued and outstanding common stock of the Company. Notwithstanding the foregoing, the Company and Cain Watters have sought to have their relationship, as it relates to the trust services provided by the Bank, to be defined by an agreement. The Cain Watters – T Bank Agreement (the “Cain Watters Services Agreement”) was entered into as of August 23, 2012 by and between the Bank and Cain Watters. Under this agreement, each party agrees to preserve one another’s business relationships with their respective clients, including mutual clients, and agrees not to solicit or otherwise encourage clients to change service providers with respect to the services provided to such clients by one another. This provision includes Cain Watters’ best efforts to preserve the Bank’s business relationships with clients of Cain Watters with respect to the Bank CIFs. This agreement provided for automatic one-year renewals, and was amended effective January 31, 2023 such that the termination clause coincides with the Support Services Agreement (see below). The Cain Watters Service Agreement can be terminated earlier, among other events, upon the termination of the Tectonic Advisors Agreement, which can be terminated upon (among other things) a change of control of the Bank. No fee is payable under this agreement.

**As Successor in Interest to Tectonic Holdings.** The following are related party agreements and transactions to which Tectonic Holdings and/or each of its subsidiaries (Tectonic Advisors, Sanders Morris, HWG and/or Miller-Green) were a party and which are not previously described in the preceding section.

**Due Diligence Agreement.** On February 15, 2006, III:I Financial Management Research, L.P. (since renamed Tectonic Advisors) and Cain Watters entered into an agreement pursuant to which Tectonic Advisors would provide the following services to Cain Watters: (a) research on investments and securities, (b) asset selection and allocation analysis, (c) due diligence on asset management companies and managers, (d) research on long and short-term prospects for investments in all markets and in all forms, (e) capital market analysis, (f) research on anticipated national and global economic issues and outlooks, (g) research on the economic environment, investments and securities of other countries, (h) assistance in coordination, implementation, and management of investment solutions, (i) performance of a defined list of investment related “global services,” specifically for pension clients of Cain Watters and (j) certain other services. In addition, Tectonic Advisors provides certain reporting and other information. The fees paid under this agreement are set forth in the Support Services Agreement described below. The term of this agreement is through January 14, 2026, with automatic one-year renewals unless terminated by either party.

**Support Services Agreement.** The Support Services Agreement, dated February 5, 2015 (the “Support Services Agreement”), was entered into by and between Tectonic Advisors and Cain Watters. Pursuant to the Support Services Agreement, Tectonic Advisors provides certain financial advisory and research services to CWA, including: asset management services, investment management oversight and management and trading of model portfolios and shall be paid a fee from revenues (“CWA Revenues”) generated from all CWA assets under management (“CWA Asset Base”). The CWA Revenue split shall be as follows: (i) Tectonic Advisors shall be entitled to receive an asset based fee of 35 basis points on the CWA Asset Base and (ii) CWA shall be entitled to receive the remainder; provided, however, that 25 basis points on the CWA Asset Base above \$2.5 billion shall be taken ratably from Tectonic Advisors and CWA and shall be allocated to CWA, consistent with past practices. During the year ended December 31, 2023, Tectonic Advisors earned \$257,000 under the Support Services Agreement. These fees are included in investment advisory and other related services in the accompanying consolidated statements of operations. Tectonic Advisors had \$95,000 in fees payable related to these services at December 31, 2023.

**Fee Allocation Agreement.** In January 2006, Tectonic Advisors entered into an agreement with Cain Watters with reference to its advisory agreement with the Bank. Tectonic Advisors had \$215,000 payable to Cain Watters related to this agreement at December 31, 2023, which is included in the accounts payable, related parties line items in the consolidated balance sheet. This agreement was amended effective January 31, 2023 such that the termination clause coincides with the Support Services Agreement (see below).

**Other Related Transactions.** Other miscellaneous related party transactions resulted in other amounts due from related parties of less than \$1,000, included within accounts receivable, related parties on the consolidated balance sheet as of December 31, 2023.



## Ordinary Banking Relationships

Certain of our officers, directors and principal shareholders, as well as their immediate family members and affiliates, are customers of, or have or have had transactions with us or the Bank in the ordinary course of business. These transactions include deposits, loans, wealth management products and other financial services related transactions. Related party transactions are made in the ordinary course of business, on substantially the same terms, including interest rates and collateral (where applicable), as those prevailing at the time for comparable transactions with persons not related to us, and do not involve more than normal risk of collectability or present other features unfavorable to us. Any loans we originate with officers, directors and principal shareholders, as well as their immediate family members and affiliates, are approved by our board of directors in accordance with the Bank's regulatory requirements.

As of the date of this Form 10-K, no related party loans were categorized as nonaccrual, past due, restructured or potential problem loans. We expect to continue to enter into transactions in the ordinary course of business on similar terms with our officers, directors and principal shareholders, as well as their immediate family members and affiliates.

## Item 14. Principal Accountant Fees and Services

### Audit Committee Pre-Approval

The Audit Committee's charter authorizes the Audit Committee to approve, in advance, all auditing services and non-audit services that are otherwise permitted by law that are provided to the Company by its independent auditors. In addition, the Audit Committee has the authority to review and, in its sole discretion, approve in advance the Company's independent auditors' annual engagement letter, including the proposed fees contained therein.

### Fees Billed by Independent Registered Public Accounting Firm

The Audit Committee has reviewed the following audit and non-audit fees billed to the Company by Whitley Penn LLP for 2023 and 2022 for purposes of considering whether such fees are compatible with maintaining the auditor's independence, and concluded that such fees did not impair Whitley Penn LLP's independence. The policy of the Audit Committee is to pre-approve all audit and non-audit services performed by Whitley Penn LLP before the services are performed, including all of the services described under "Audit Fees", "Tax Fees" and "All Other Fees" below. The Audit Committee has pre-approved all of the services provided by Whitley Penn LLP in accordance with the policies and procedures described in the section titled "—Audit Committee Pre-Approval."

	For the Year Ended December 31,	
	2023	2022
Audit Fees <sup>(1)</sup>	\$ 217,624	\$ 223,647
Tax Fees <sup>(2)</sup>	46,760	55,020
All Other Fees <sup>(3)</sup>	52,314	23,400
Total Fees	<u>\$ 316,698</u>	<u>\$ 302,067</u>

- (1) Audit fees consist of the aggregate fees billed for professional services rendered for the audit of our annual financial statements included in our Annual Report on Form 10-K and a review of financial statements included in our Quarterly Reports on Form 10-Q.
- (2) Tax compliance fees consisted of tax return filing fees and miscellaneous state and federal income tax related issues. Tax consulting services include routine tax advice and consultation.
- (3) Other fees are those associated with services not captured in the other categories, such as operational reviews.



**PART IV**
**Item 15. Exhibits and Financial Statement Schedules**

<b>Exhibit No.</b>	<b>Description of Exhibit</b>
<a href="#">2.1</a>	Amended and Restated Agreement and Plan of Merger by and between T Acquisition, Inc. and Tectonic Holdings, LLC, dated March 28, 2019 (schedules and exhibits have been omitted pursuant to Item 601(a)(5) of Regulation S-K; however, the registrant hereby agrees to furnish a copy of any omitted schedule or similar attachment to the SEC upon request)(incorporated by reference from Exhibit 2.1 to the Registration Statement on Form S-1 filed with the SEC on April 18, 2019 (File No. 333-230949))
<a href="#">2.2</a>	Purchase and Sale Agreement by and between Tectonic Holdings, LLC and Summer Wealth Management, LLC, dated August 3, 2016, as amended (schedules and exhibits have been omitted pursuant to Item 601(a)(5) of Regulation S-K; however, the registrant hereby agrees to furnish a copy of any omitted schedule or similar attachment to the SEC upon request)(incorporated by reference from Exhibit 2.2 to the Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 230949))
<a href="#">2.3</a>	Agreement and Plan of Merger by and among Tectonic Financial, Inc., T Bancshares, Inc. and Integra Funding Solutions, LLC, and joined in by The Bolt Family Irrevocable Trust, IF Holdings, LLC, Doug Waidelich, The Crane Basin Irrevocable Trust, The Hamilton Irrevocable Trust, Tracy A. Bolt, and Randall W. Woods, dated June 18, 2021 (schedules and exhibits have been omitted pursuant to Item 601(a)(5) of Regulation S-K; however, the registrant hereby agrees to furnish a copy of any omitted schedule or similar attachment to the SEC upon request.) (incorporated by reference from Exhibit 2.1 to the Current Report on Form 8-K filed with the SEC on June 24, 2021 (File No. 001-38910))
<a href="#">3.1</a>	Amended and Restated Certificate of Formation (incorporated by reference from Exhibit 3.1 to Amendment No. 2 to the Registration Statement on Form S-1/A filed with the SEC on May 9, 2019 (File No. 333-230949))
<a href="#">3.2</a>	Certificate of Designation of 10.0% Series A Non-Cumulative Perpetual Preferred Stock (incorporated by reference from Exhibit 3.1 to the Current Report on Form 8-K filed with the SEC on May 16, 2019 (File No. 001-38910))
<a href="#">3.3</a>	Certificate of Designation of 9.00% Fixed-to-Floating Rate Series B Non-Cumulative Perpetual Preferred Stock (incorporated by reference from Exhibit 3.2 to the Current Report on Form 8-K filed with the SEC on May 16, 2019 (File No. 001-38910))
<a href="#">3.4</a>	Certificate of Amendment to effect Reverse Stock Split (incorporated by reference from Exhibit 3.3 to the Current Report on Form 8-K filed with the SEC on May 16, 2019 (File No. 001-38910))
<a href="#">3.5</a>	Amended and Restated Bylaws (incorporated by reference from Exhibit 3.5 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">4.1</a>	Specimen common stock certificate of Tectonic Financial, Inc. (incorporated by reference from Exhibit 4.1 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">4.2</a>	Subordinated Note Purchase Agreement for 7.125% Fixed-to-Floating Subordinated Notes due 2027, dated July 17, 2017 (incorporated by reference from Exhibit 4.2 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">4.3</a>	Description of Series B Preferred Stock (incorporated by reference from Exhibit 4.3 to the Company's Annual Report on Form 10-K for the year ended December 31, 2019 filed with the SEC on March 31, 2020 (File No. 001-38910))
<a href="#">10.1†</a>	Employment Agreement of A. Haag Sherman, dated May 1, 2019 (incorporated by reference from Exhibit 10.1 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.2†</a>	Amended and Restated Employment Agreement of Patrick Howard, dated May 1, 2019 (incorporated by reference from Exhibit 10.2 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.3†</a>	Amended and Restated Employment Agreement of Ken Bramlage, dated May 1, 2019 (incorporated by reference from Exhibit 10.4 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.4†</a>	T Acquisition, Inc. Amended and Restated 2017 Equity Incentive Plan (incorporated by reference from Exhibit 10.4 to the Registration Statement on Form S-1 filed with the SEC on April 18, 2019 (File No. 333-230949))
<a href="#">10.5†</a>	Form Notice of Stock Option Award and of Stock Option Award Agreement under T Acquisition, Inc. 2017 Equity Incentive Plan (incorporated by reference from Exhibit 10.5 to the Registration Statement on Form S-1 filed with the SEC on April 18, 2019 (File No. 333-230949))
<a href="#">10.6</a>	Advances and Security Agreement by and between the Federal Home Loan Bank of Dallas and T Bank, N.A., dated June 29, 2006 (incorporated by reference from Exhibit 10.6 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.7</a>	Fee Allocation Agreement by and between Cain Watters & Associates, P.L.L.C. and Tectonic Advisors, LLC (f/k/a III: I Financial Management Research, L.P.), dated July 17, 2008 (incorporated by reference from Exhibit 10.7 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.7.1</a>	First Amendment to the Fee Allocation Agreement by and between Cain Watters & Associates, P.L.L.C. and Tectonic Advisors, LLC (f/k/a III: I Financial Management Research, L.P.), effective January 31, 2023 (incorporated by reference from Exhibit 10.7.1 to the Company's Annual Report on Form 10-K for the year ended December 31, 2022 filed with the SEC on March 31, 2023 (File No. 001-38910))

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<a href="#">10.8</a>	Due Diligence Agreement by and between Cain Watters & Associates, P.L.L.C. and Tectonic Advisors, LLC (f/k/a III:I Financial Management Research, L.P.), dated February 15, 2006 (incorporated by reference from Exhibit 10.8 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.8.1</a>	Supplement to Due Diligence Agreement by and between Cain, Watters & Associates, P.L.L.C. and Tectonic Advisors, LLC (f/k/a III:I Financial Management Research, L.P.), dated November 5, 2007 (incorporated by reference from Exhibit 10.8.1 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.8.2</a>	First Amendment to the Due Diligence Agreement by and between Cain Watters & Associates, P.L.L.C. and Tectonic Advisors, LLC (f/k/a III:I Financial Management Research, L.P.), effective January 31, 2023 (incorporated by reference from Exhibit 10.8.2 to the Company's Annual Report on Form 10-K for the year ended December 31, 2022 filed with the SEC on March 31, 2023 (File No. 001-38910))
<a href="#">10.10</a>	Agreement by and between T Bank, N.A. and Cain Watters & Associates, P.L.L.C., dated August 23, 2012 (incorporated by reference from Exhibit 10.10 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.10.1</a>	Second Amendment to the Agreement by and between T Bank, N.A. and Cain Watters & Associates, P.L.L.C., effective January 31, 2023 (incorporated by reference from Exhibit 10.10.1 to the Company's Annual Report on Form 10-K for the year ended December 31, 2022 filed with the SEC on March 31, 2023 (File No. 001-38910))
<a href="#">10.11</a>	Unit Option - Buy Down Agreement by and between A. Haag Sherman and the optionees named therein, dated February 5, 2015 (incorporated by reference from Exhibit 10.11 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.12</a>	Management Services Agreement by and between Tectonic Advisors, LLC and Tectonic Services, LLC, dated February 5, 2015 (incorporated by reference from Exhibit 10.12 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.13</a>	Amended and Restated Promissory Note payable to TIB The Independent BankersBank, N. A., dated May 11, 2017 (incorporated by reference from Exhibit 10.13 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.14</a>	Loan Agreement by and among Tectonic Merger Sub, Inc., T Bancshares, Inc. and TIB The Independent Bankers Bank, N.A., dated May 11, 2017 (incorporated by reference from Exhibit 10.14 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.15</a>	Guaranty Agreement by and between Sanders Morris Harris LLC and TIB The Independent BankersBank, N.A., dated May 11, 2017 (incorporated by reference from Exhibit 10.15 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.16</a>	Guaranty Agreement by and between Tectonic Advisors, LLC and TIB The Independent BankersBank, N.A., dated May 11, 2017 (incorporated by reference from Exhibit 10.16 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.17</a>	Guaranty Agreement by and between Tectonic Holdings, LLC and TIB The Independent BankersBank, N.A., dated May 11, 2017 (incorporated by reference from Exhibit 10.17 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.18</a>	Renewal, Extension, and Modification of Loan by and among Tectonic Merger Sub, Inc., T Bancshares, Inc. and TIB The Independent BankersBank, N.A., dated May 11, 2018 (incorporated by reference from Exhibit 10.18 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.19</a>	Management Services Agreement by and between Tectonic Holdings, LLC and Tectonic Services, LLC, dated February 5, 2015 (incorporated by reference from Exhibit 10.19 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.19.1</a>	Amendment to Management Services Agreement by and between Tectonic Advisors, LLC, Sanders Morris Harris LLC, Miller-Green Financial Services, LLC, HWG Insurance Agency, LLC and Tectonic Services, LLC, dated March 1, 2017 (incorporated by reference from Exhibit 10.19.1 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.19.2</a>	Second Amendment to Management Services Agreement by and between Tectonic Services, LLC, Tectonic Advisors, LLC, Sanders Morris Harris LLC, Miller-Green Financial Services LLC and HWG Insurance Agency LLC, dated October 1, 2017 (incorporated by reference from Exhibit 10.19.2 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.20</a>	Support Services Agreement by and between Cain Watters & Associates, P.L.L.C. and Tectonic Advisors, LLC, dated February 5, 2015 (schedules have been omitted pursuant to Item 601(b)(2) of Regulation S-K. Tectonic Financial agrees to furnish supplementally to the SEC a copy of any omitted schedule upon request) (incorporated by reference from Exhibit 10.20 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.20.1</a>	First Amendment to the Support Services Agreement by and between Cain Watters & Associates, P.L.L.C. and Tectonic Advisors, LLC (f/k/a III: I Financial Management Research, L.P.), effective January 31, 2023 (incorporated by reference from Exhibit 10.20.1 to the Company's Annual Report on Form 10-K for the year ended December 31, 2022 filed with the SEC on March 31, 2023 (File No. 001-38910))
<a href="#">10.21</a>	Insurance Contribution Agreement by and between Cain Watters & Associates, P.L.L.C. and Tectonic Holdings, LLC, dated February 5, 2015 (incorporated by reference from Exhibit 10.21 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.22</a>	Amended and Restated Investment Advisory Agreement by and between T Bank, N.A. and Tectonic Advisors, LLC, dated May 14, 2015 (incorporated by reference from Exhibit 10.22 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))

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<a href="#">10.22.1</a>	Third Amendment to the Amended and Restated Investment Advisory Agreement by and between T Bank, N.A. and Tectonic Advisors, LLC (f/k/a III: I Financial Management Research, L.P.), effective January 31, 2023 (incorporated by reference from Exhibit 10.22.1 to the Company's Annual Report on Form 10-K for the year ended December 31, 2022 filed with the SEC on March 31, 2023 (File No. 001-38910))
<a href="#">10.23</a>	Loan Agreement by and between Dental Community Financial Holdings, Ltd., and Tectonic Advisors, LLC, dated January 1, 2017 (incorporated by reference from Exhibit 10.23 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.23.1</a>	Promissory Note made payable to Dental Community Financial Holdings, Ltd. by Tectonic Advisors, LLC, dated January 1, 2017 (incorporated by reference from Exhibit 10.23.1 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.24</a>	Tax Sharing Agreement by and between T Acquisition, Inc., T Bancshares, Inc. and T Bank N.A., dated May 15, 2017 (incorporated by reference from Exhibit 10.24 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.25</a>	Tax Sharing Agreement by and between T Acquisition, Inc. and Tectonic Holdings, LLC, effective May 15, 2017 (incorporated by reference from Exhibit 10.25 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">10.26</a>	Expense Sharing Agreement by and between T Bank N.A. and Tectonic Holdings, LLC, effective May 15, 2017 (incorporated by reference from Exhibit 10.26 to Amendment No. 1 to the Registration Statement on Form S-1/A filed with the SEC on May 6, 2019 (File No. 333-230949))
<a href="#">21.1</a>	Subsidiaries of Tectonic Financial, Inc.*
<a href="#">31.1</a>	Rule 13a-14(a) Certification of Principal Executive Officer*
<a href="#">31.2</a>	Rule 13a-14(a) Certification of Principal Financial Officer*
<a href="#">32.1</a>	Section 1350 Certification**
<a href="#">97</a>	Compensation Recovery Policy, effective as of October 2, 2023.*
101.INS	XBRL Instance Document*
101.SCH	XBRL Taxonomy Extension Schema Document*
101.CAL	XBRL Taxonomy Extension Label Calculation Linkbase Document*
101.DEF	XBRL Taxonomy Definition Linkbase*
101.LAB	XBRL Taxonomy Extension Label Linkbase Document*
101.PRE	XBRL Taxonomy Extension Presentation Linkbase*
104	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101)

\* Filed herewith

\*\* Furnished herewith

† Management contract or compensatory plan or arrangement

### **Item 16. Form 10-K Summary.**

None.

**SIGNATURES**

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

**Tectonic Financial, Inc.**

Dated: April 1, 2024

By: /s/ A. Haag Sherman  
A. Haag Sherman  
Chief Executive Officer  
(Principal Executive Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this Form 10-K has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

<u>SIGNATURE</u>	<u>TITLE</u>	<u>DATE</u>
<u>/s/ A. Haag Sherman</u> A. Haag Sherman	Director, Chairman, Chief Executive Officer and Principal Executive Officer	April 1, 2024
<u>/s/ Ken Bramlage</u> Ken Bramlage	Executive Vice President, Chief Financial Officer and Principal Accounting Officer	April 1, 2024
<u>/s/ Patrick Howard</u> Patrick Howard	Director and President	April 1, 2024
<u>/s/ George L. Ball</u> George L. Ball	Director	April 1, 2024
<u>/s/ Barb Bomersbach</u> Barb Bomersbach	Director	April 1, 2024
<u>/s/ Darrell Cain</u> Darrell Cain	Director	April 1, 2024
<u>/s/ Steven B. Clapp</u> Steven B. Clapp	Director	April 1, 2024
<u>/s/ Eric Langford</u> Eric Langford	Director	April 1, 2024
<u>/s/ Thomas McDougal</u> Thomas McDougal, DDS	Director	April 1, 2024
<u>/s/ Thomas Sanders</u> Thomas Sanders	Director	April 1, 2024
<u>/s/ Daniel C. Wicker</u> Daniel C. Wicker	Director	April 1, 2024

Subsidiaries of Tectonic Financial, Inc.

Entity Name	State of Incorporation
T Bancshares, Inc.	Texas
Tectonic Advisors, LLC	Texas
Sanders Morris LLC	Texas
HWG Insurance LLC	Texas

Subsidiaries of T Bancshares, Inc.

Entity Name	State of Incorporation
T Bank, N.A.	a national banking association

## CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER

I, A. Haag Sherman, Chief Executive Officer of Tectonic Financial, Inc., certify that:

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

Date: April 1, 2024

By: /s/ A. Haag Sherman  
A. Haag Sherman  
Chief Executive Officer

## CERTIFICATION OF CHIEF FINANCIAL OFFICER

I, Ken Bramlage, Executive Vice President & Chief Financial Officer of Tectonic Financial, Inc., certify that:

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

Date: April 1, 2024

By: /s/ Ken Bramlage  
Ken Bramlage  
Executive Vice President & Chief Financial Officer

**CERTIFICATION OF CEO AND CFO PURSUANT TO  
18 U.S.C. §1350, AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Annual Report on Form 10-K of Tectonic Financial, Inc. (the “Company”) for the year ended December 31, 2023 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), A. Haag Sherman, as Chief Executive Officer of the Company, and Ken Bramlage, as Executive Vice President and Chief Financial Officer of the Company, each hereby certifies, pursuant to 18 U.S.C. § 1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that, to the best of his knowledge:

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

TECTONIC FINANCIAL, INC.

Date: April 1, 2024

By: /s/ A. Haag Sherman  
A. Haag Sherman  
Chief Executive Officer

Date: April 1, 2024

By: /s/ Ken Bramlage  
Ken Bramlage  
Executive Vice President & Chief Financial Officer



**TECTONIC FINANCIAL, INC.  
INCENTIVE AWARD RECOUPMENT POLICY**

This INCENTIVE AWARD RECOUPMENT POLICY (this "**Policy**") is adopted effective as of October 2, 2023 (the "**Effective Date**"), by the Board of Directors (the "**Board**") of Tectonic Financial, Inc., a Texas corporation (the "**Company**").

**WHEREAS**, in accordance with the applicable recoupment provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("**Dodd-Frank**"), and the requirements of Rule 10D-1 promulgated by the U.S. Securities and Exchange Commission (the "**SEC**") under the Securities Exchange Act of 1934, as amended (the "**Exchange Act**"), and Rule 5608 of the Nasdaq Listing Standards that companies adopt a compensation recovery policy, the Board desires to approve and adopt this Policy with respect to certain Incentive Compensation (as defined below) that is Received (as defined below) by a Covered Individual (as defined below) on or after October 2, 2023; and

**WHEREAS**, the Board believes it would be in the best interests of the Company and its shareholders to have this Policy adopted by the Board.

**NOW, THEREFORE**, the applicable provisions of this Policy are as follows:

1. **Definitions.** Except as otherwise provided above, terminology used in this Policy shall have the following meanings:

(a) "**Accounting Restatement**" means a requirement that the Company prepare an accounting restatement due to the material noncompliance of the Company with any financial reporting requirement under the U.S. federal securities laws, including any required accounting restatement to correct an error in previously issued financial statements that is material to the previously issued financial statements, or that would result in a material misstatement if the error were corrected in the current period or left uncorrected in the current period. Changes to the Company's financial statements that do not represent error corrections are not an Accounting Restatement, including: (i) retrospective application of a change in accounting principle; (ii) retrospective revision to reportable segment information due to a change in the structure of the Company's internal organization; (iii) retrospective reclassification due to a discontinued operation; (iv) retrospective application of a change in reporting entity, such as from a reorganization of entities under common control; and (v) retrospective revision for stock splits, reverse stock splits, stock dividends or other changes in capital structure.

(b) "**Covered Individual**" shall mean, whether former or current, the (i) named executive officers of our Company; (ii) each "executive officer" of our Company (as such term is defined under Section 16 of the Exchange Act); and (iii) any officer of our Company or any of its subsidiaries that is designated by the Board as being subject to this Policy.

(c) "**Erroneously Awarded Compensation**" means the amount of Incentive Compensation that was Received that exceeds the amount of Incentive Compensation that otherwise would have been Received had the amount of Incentive Compensation been determined based on the restated Financial Reporting Measures, computed without regard to any taxes paid by the Covered Individual or by the Company on the Covered Individual's behalf. For Incentive Compensation based on total shareholder return or Company stock price, where the amount of Erroneously Awarded Compensation is not subject to mathematical recalculation directly from the information in an accounting restatement, the amount of Erroneously Awarded Compensation will be based on a reasonable estimate by the Board of the effect of the Accounting Restatement on the stock price or total shareholder return upon which the Incentive Compensation was Received. The Company will maintain documentation of the determination of that reasonable estimate and provide such documentation to Nasdaq as required.

(d) "**Financial Reporting Measures**" means (i) measures that are determined and presented in accordance with the accounting principles used in preparing the Company's financial statements, and any measures that are derived wholly or in part from such measures (whether or not such measures are presented within the Company's financial statements or included in a filing made with the SEC), (ii) Company stock price and (iii) Company total shareholder return.

(e) **"Incentive Compensation"** shall mean a Covered Individual's cash bonus awarded under our Company's annual incentive plan and any equity-based awards granted pursuant to our Company's long-term incentive plans that are earned, paid/granted or vested wholly (or in part) upon the attainment of any Financial Reporting Measure of our Company.

(f) **"Look-Back Period"** shall mean the three completed fiscal years immediately preceding the earlier of: (i) the date the Board, a committee of the Board, or the officer or officers of the Company authorized to take such action if Board action is not required, concludes, or reasonably should have concluded, that the Company is required to prepare an Accounting Restatement; or (ii) the date a court, regulator, or other legally authorized body directs the Company to prepare an Accounting Restatement. In addition, if there is a change in the Company's fiscal year end, the Look-Back Period will also include any transition period to the extent required by Rule 5608 of the Nasdaq Listing Standards.

(g) **"Received"** means Incentive Compensation that is actually or deemed received by the Covered Individual in the fiscal year to which the Financial Reporting Measure is attained, irrespective of whether the Incentive Compensation is subject to additional time or non-financial performance vesting conditions.

2. **Recoupment of Incentive Compensation – Restatement of Financial Statements**. Subject to the terms of this Policy and the requirements of Rule 5608 of the Nasdaq Listing Standards, if the Company is required to prepare an Accounting Restatement, then the Company shall recover, reasonably promptly from each Covered Individual as set forth in Section 5, below, any Erroneously Awarded Compensation that was Received by such Covered Individual during the Look-Back Period. Notwithstanding anything herein to the contrary, this Policy shall be deemed automatically and unilaterally amended to the minimum extent necessary to comply with the applicable the listing standards of the national securities exchange on which the Company's securities are listed.

3. **Board Discretion**. The Board may, in determining appropriate remedial action, take into account the financial cost of penalties or punishments imposed by third parties, such as law enforcement agencies, regulators or other authorities; however, such determinations shall not mitigate or eliminate the Company's obligations to recover Erroneously Awarded Compensation pursuant to Section 2 of this Policy.

4. **Amendment, Termination and Interpretation**. The Board may at any time suspend, amend or terminate this Policy to the minimum extent necessary to comply with applicable laws. Pursuant to Section 5, below, the Board shall have the sole discretion to interpret and enforce this Policy.

5. **Enforcement and Impracticability**. The Board shall recover any Incentive Compensation in accordance with this Policy unless such recovery would be impracticable, as determined by the Board in accordance with Rule 10D-1 promulgated by the SEC under the Exchange Act and Rule 5608 of the Nasdaq Listing Standards. To the extent the Board determines to enforce recoupment, (i) the Board shall provide the Covered Individual written notice of its intent to recoup Incentive Compensation under this Policy, along with the timeline within which the Covered Individual must respond, (ii) to the extent the Covered Individual does not intend to comply with such recoupment efforts, he or she must respond to the Board in writing detailing the reasons why non-compliance is warranted and such response must be provided to the Board within fifteen (15) business days from the Covered Individual receiving the Board's initial notice, and (iii) if the Board disagrees with the Covered Individual's assertions, then the Board must respond to the Covered Individual in writing detailing such reasons within the fifteen (15) business days immediately following its receipt of the Covered Individual's written response.

6. **Determination of Means of Recovery**. With respect to recovery of Erroneously Awarded Compensation and subject to the requirement that recovery be made reasonably promptly, the Board will determine the appropriate means of recovery, which may vary, without limitation, between Covered Individuals or based on the nature of the applicable Incentive Compensation, and which may involve, without limitation, establishing a deferred repayment plan or set off against current or future compensation otherwise payable to the Covered Individual. Recovery of Erroneously Awarded Compensation will be made without regard to income taxes paid by the Covered Individual or by the Company on the Covered Individual's behalf in connection with such Erroneously Awarded Compensation.

7. Compensation Not Subject to this Policy. Section 2 of this Policy does not apply to Incentive Compensation that was Received before October 2, 2023, and does not apply to Incentive Compensation that was Received by a Covered Individual before beginning service as an executive officer.

8. No Indemnification or Company-Paid Insurance. The Company will not indemnify or reimburse any Covered Individual against or for the loss of Erroneously Awarded Compensation and will not pay or reimburse any Covered Individual for the purchase of a third-party insurance policy to fund potential recovery obligations.

9. Effective Date. This Policy shall apply to all Covered Individuals from and after the Effective Date.