National Bank Holdings Corp
Form 10-Q
May 09, 2014

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2014

OR

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

For the transition period from to

Commission File Number: 001-35654

NATIONAL BANK HOLDINGS CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	27-0563799
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

7800 East Orchard, Suite 300, Greenwood Village, Colorado 80111
(Address of principal executive offices) (Zip Code)
Registrant's telephone, including area code: (720) 529-3336

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý No ¨

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

Large accelerated filer x	Accelerated filer ¨
Non-accelerated filer ¨ (do not check if a smaller reporting company)	Smaller Reporting Company ¨

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

As of May 6, 2014, NBHC had outstanding 41,017,351 shares of Class A voting common stock and 3,027,774 shares of Class B non-voting common stock, each with $0.01 par value per share, excluding 1,118,727 shares of restricted Class A common stock issued but not yet vested.

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, notwithstanding that such statements are not specifically identified. Any statements about our expectations, beliefs, plans, predictions, forecasts, objectives, assumptions or future events or performance are not historical facts and may be forward-looking. These statements are often, but not always, made through the use of words or phrases such as “anticipate,” “believe,” “can,” “would,” “should,” “could,” “may,” “predict,” “seek,” “potential,” “will,” “estimate,” “t “continuing,” “ongoing,” “expect,” “intend” and similar words or phrases. These statements are only predictions and involve estimates, known and unknown risks, assumptions and uncertainties. We have based these statements largely on our current expectations and projections about future events and financial trends that we believe may affect our financial condition, liquidity, results of operations, business strategy and growth prospects.

Forward-looking statements involve certain important risks, uncertainties and other factors, any of which could cause actual results to differ materially from those in such statements and, therefore, you are cautioned not to place undue reliance on such statements. Factors that could cause actual results to differ from those discussed in the forward-looking statements include, but are not limited to:

- our ability to execute our business strategy, as well as changes in our business strategy or development plans;
- business and economic conditions generally and in the financial services industry;
- economic, market, operational, liquidity, credit and interest rate risks associated with our business;
- effects of any changes in trade, monetary and fiscal policies and laws, including the interest rate policies of the Federal Reserve Board;
- changes imposed by regulatory agencies to increase our capital to a level greater than the current level required for well-capitalized financial institutions (including the impact of the joint final rules promulgated by the Federal Reserve Board, Office of the Comptroller of the Currency and the FDIC revising certain regulatory capital requirements to align with the Basel III capital standards and meet certain requirements of the Dodd-Frank Wall Street Reform and Consumer Protection Act);
- effects of inflation, as well as, interest rate, securities market and monetary supply fluctuations;
- changes in the economy or supply-demand imbalances affecting local real estate values;
- changes in consumer spending, borrowings and savings habits;
- our ability to identify potential candidates for, obtain regulatory approval for, and consummate, acquisitions of financial institutions on attractive terms, or at all;
- our ability to integrate acquisitions and to achieve synergies, operating efficiencies and/or other expected benefits within expected time-frames, or at all, or within expected cost projections, and to preserve the goodwill of acquired financial institutions;
- our ability to achieve organic loan and deposit growth and the composition of such growth;
- changes in sources and uses of funds, including loans, deposits and borrowings;
- increased competition in the financial services industry, nationally, regionally or locally, resulting in, among other things, lower returns;
- the effect of changes in accounting policies and practices, as may be adopted by the regulatory agencies, as well as the Public Company Accounting Oversight Board, the Financial Accounting Standards Board and other accounting standard setters;
- continued consolidation in the financial services industry;
- our ability to maintain or increase market share and control expenses;
- costs and effects of changes in laws and regulations and of other legal and regulatory developments, including, but not limited to, changes in regulation that affect the fees that we charge, the resolution of legal proceedings or regulatory or other governmental inquiries, and the results of regulatory examinations, reviews or other inquiries.
- technological changes;
- the timely development and acceptance of new products and services and perceived overall value of these products and services by our clients;
- changes in our management personnel and our continued ability to hire and retain qualified personnel;
- ability to implement and/or improve operational management and other internal risk controls and processes and our reporting system and procedures;

- regulatory limitations on dividends from our bank subsidiary;
- changes in estimates of future loan reserve requirements based upon the periodic review thereof under relevant regulatory and accounting requirements;
- political instability, acts of war or terrorism and natural disasters;
- impact of reputational risk on such matters as business generation and retention; and
- our success at managing the risks involved in the foregoing items.

Any forward-looking statement speaks only as of the date on which it is made, and we undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date on which the statement is made or to reflect the occurrence of unanticipated events or circumstances, except as required by applicable law.

PART I: FINANCIAL INFORMATION
Item 1: FINANCIAL STATEMENTS
NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES
Consolidated Statements of Financial Condition (Unaudited)
(In thousands, except share and per share data)

	March 31, 2014	December 31, 2013
ASSETS		
Cash and due from banks	$65,785	$67,420
Due from Federal Reserve Bank of Kansas City	117,871	107,894
Interest bearing bank deposits	14,159	14,146
Cash and cash equivalents	197,815	189,460
Investment securities available-for-sale (at fair value)	1,720,840	1,785,528
Investment securities held-to-maturity (fair value of $614,123 and $636,405 at March 31, 2014 and December 31, 2013, respectively)	616,221	641,907
Non-marketable securities	31,109	31,663
Loans (including covered loans of $287,590 and $309,397 at March 31, 2014 and December 31, 2013, respectively)	1,961,592	1,854,094
Allowance for loan losses	(13,972)	(12,521)
Loans, net	1,947,620	1,841,573
Loans held for sale	2,143	5,787
Federal Deposit Insurance Corporation (“FDIC”) indemnification asset, net	56,677	64,447
Other real estate owned	65,983	70,125
Premises and equipment, net	112,534	115,219
Goodwill	59,630	59,630
Intangible assets, net	20,893	22,229
Other assets	82,122	86,547
Total assets	$4,913,587	$4,914,115
LIABILITIES AND SHAREHOLDERS’ EQUITY		
Liabilities:		
Deposits:		
Non-interest bearing demand deposits	$689,248	$674,989
Interest bearing demand deposits	398,429	386,762
Savings and money market	1,334,521	1,280,871
Time deposits	1,443,898	1,495,687
Total deposits	3,866,096	3,838,309
Securities sold under agreements to repurchase	91,065	99,547
Due to FDIC	33,309	41,882
Other liabilities	27,268	36,585
Total liabilities	4,017,738	4,016,323
Shareholders’ equity:		
Common stock, par value $0.01 per share: 400,000,000 shares authorized; 52,268,851 and 52,289,347 shares issued; 44,486,467 and 44,918,336 shares outstanding at March 31, 2014 and December 31, 2013, respectively	512	512
Additional paid in capital	990,700	990,216
Retained earnings	39,121	39,966
Treasury stock of 6,761,257 and 6,306,551 shares at March 31, 2014 and December 31, 2013, respectively, at cost	(134,953)	(126,146)
Accumulated other comprehensive income (loss), net of tax	469	(6,756)
Total shareholders’ equity	895,849	897,792

Total liabilities and shareholders’ equity	$4,913,587	$4,914,115

See accompanying notes to the unaudited consolidated interim financial statements.

NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES
Consolidated Statements of Operations (Unaudited)
(In thousands, except share and per share data)

	For the three months ended March 31, 2014	2013
Interest and dividend income:		
Interest and fees on loans	$33,247	$36,135
Interest and dividends on investment securities	13,168	13,248
Dividends on non-marketable securities	389	394
Interest on interest-bearing bank deposits	81	321
Total interest and dividend income	46,885	50,098
Interest expense:		
Interest on deposits	3,506	4,511
Interest on borrowings	32	18
Total interest expense	3,538	4,529
Net interest income before provision for loan losses	43,347	45,569
Provision for loan losses	1,769	1,417
Net interest income after provision for loan losses	41,578	44,152
Non-interest income (expense):		
FDIC indemnification asset amortization	(7,608)	(4,669)
FDIC loss sharing income (expense)	(957)	3,276
Service charges	3,540	3,687
Bank card fees	2,374	2,469
Gain on sales of mortgages, net	208	306
Gain on previously charged-off acquired loans	296	443
OREO related write-ups and other income	968	974
Other non-interest income	825	665
Total non-interest income (expense)	(354)	7,151
Non-interest expense:		
Salaries and benefits	20,774	22,956
Occupancy and equipment	6,474	5,965
Telecommunications and data processing	3,148	3,469
Marketing and business development	1,023	1,379
FDIC deposit insurance	1,045	1,047
ATM/debit card expenses	751	1,005
Professional fees	638	1,396
Other non-interest expense	2,409	2,908
Gain from the change in fair value of warrant liability	(898)	(627)
Intangible asset amortization	1,336	1,336
Other real estate owned expenses	1,633	4,719
Problem loan expenses	685	2,331
Total non-interest expense	39,018	47,884
Income before income taxes	2,206	3,419
Income tax expense	775	1,337
Net income	$1,431	$2,082
Income per share—basic	$0.03	$0.04
Income per share—diluted	$0.03	$0.04
Weighted average number of common shares outstanding:		
Basic	44,819,644	52,320,622

Diluted	44,863,138	52,346,525

See accompanying notes to the unaudited consolidated interim financial statements.

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NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES
Consolidated Statements of Comprehensive Income (Loss) (Unaudited)
(In thousands)

	For the three months ended	
	2014	2013
Net income	$1,431	$2,082
Other comprehensive income, net of tax:		
Securities available-for-sale:		
Net unrealized gains (losses) arising during the period, net of tax (expense) benefit of ($4,962) and $1,872 for the three months ended March 31, 2014 and 2013, respectively	8,070	(2,501)
	$8,070	$(2,501)
Net unrealized holding gains on securities transferred between available-for-sale to held-to-maturity:		
Less: amortization of net unrealized holding gains to income, net of tax benefit of $519 and $1,218 for the three months ended March 31, 2014 and 2013, respectively	(845)	(1,945)
	(845)	(1,945)
Other comprehensive income (loss)	7,225	(4,446)
Comprehensive income (loss)	$8,656	$(2,364)

See accompanying notes to the unaudited consolidated interim financial statements.

NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES
Consolidated Statements of Changes in Shareholders' Equity (Unaudited)
Three Months Ended March 31, 2014 and 2013
(In thousands, except share and per share data)

	Common stock	Additional paid-in capital	Retained earnings	Treasury stock	Accumulated other comprehensive income (loss), net	Total
Balance, December 31, 2012	$523	$1,006,194	$43,273	$(4)	$ 40,573	$1,090,559
Net income	—	—	2,082	—	—	2,082
Stock-based compensation	—	1,441	—	—	—	1,441
(Repurchase of 13,003 shares)/retirement of 240 treasury shares	—	(234)	—	4	—	(230)
Dividends paid ($.05 per share)	—	—	(2,663)	—	—	(2,663)
Other comprehensive loss	—	—	—	—	(4,446)	(4,446)
Balance, March 31, 2013	523	1,007,401	42,692	—	36,127	1,086,743
Balance, December 31, 2013	512	990,216	39,966	(126,146)	(6,756)	897,792
Net income	—	—	1,431	—	—	1,431
Stock-based compensation	—	720	—	—	—	720
Issuance under equity compensation plan	—	(236)	—	—	—	(236)
Repurchase of shares (454,706 shares)	—	—	—	(8,807)	—	(8,807)
Dividends paid ($.05 per share)	—	—	(2,276)	—	—	(2,276)
Other comprehensive income	—	—	—	—	7,225	7,225
Balance, March 31, 2014	$512	$990,700	$39,121	$(134,953)	$ 469	$895,849

See accompanying notes to the unaudited consolidated interim financial statements.

NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES
Consolidated Statements of Cash Flows (Unaudited)
(In thousands)

	For the three months ended March 31, 2014	2013
Cash flows from operating activities:		
Net income	$1,431	$2,082
Adjustments to reconcile net income to net cash used in operating activities:		
Provision for loan losses	1,769	1,417
Depreciation and amortization	4,180	3,812
Current income tax receivable (payable)	6,017	(6,739)
Deferred income tax asset	(4,584)	(3,574)
Discount accretion, net of premium amortization	1,320	5,466
Loan accretion	(17,733)	(24,293)
Net gain on sale of mortgage loans	(208)	(306)
Origination of loans held for sale, net of repayments	(6,506)	(12,382)
Proceeds from sales of loans held for sale	9,742	11,227
Amortization of indemnification asset	7,608	4,669
Gain on the sale of other real estate owned, net	(587)	(1,805)
Impairment on other real estate owned	822	4,526
Stock-based compensation	720	1,441
Decrease in due to FDIC, net	(8,573)	(260)
(Increase) decrease in other assets	(1,451)	409
Decrease in other liabilities	(9,355)	(3,443)
Net cash provided by (used in) operating activities	(15,388)	(17,753)
Cash flows from investing activities:		
Sale of FHLB stock	554	49
Maturities of investment securities held-to-maturity	24,190	57,599
Maturities of investment securities available-for-sale	76,532	158,532
Purchase of investment securities available-for-sale	—	(554,355)
Net (increase) decrease in loans	(90,125)	50,634
Purchase of premises and equipment	(159)	(2,122)
Proceeds from sales of loans	422	19,755
Proceeds from sales of other real estate owned	4,143	25,726
Decrease in FDIC indemnification asset	162	55,287
Net cash used in investing activities	15,719	(188,895)
Cash flows from financing activities:		
Net increase (decrease) in deposits	27,787	(139,918)
Decrease in repurchase agreements	(8,482)	(575)
Issuance under equity compensation plan	(236)	—
Payment of dividends	(2,238)	(2,616)
Repurchase of shares	(8,807)	(230)
Net cash provided by (used in) financing activities	8,024	(143,339)
Increase (decrease) in cash and cash equivalents	8,355	(349,987)
Cash and cash equivalents at beginning of the year	189,460	769,180
Cash and cash equivalents at end of period	$197,815	$419,193
Supplemental disclosure of cash flow information:		
Cash paid during the period for interest	$3,484	$4,906
Cash (received) paid during the period for taxes	$(638)	$8,580

Supplemental schedule of non-cash investing activities:		
Loans transferred to other real estate owned at fair value	$236	$17,043
FDIC indemnification asset claims transferred to other assets	$29	$9,132

See accompanying notes to the unaudited consolidated interim financial statements.

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NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)
March 31, 2014

Note 1 Basis of Presentation

National Bank Holdings Corporation ("NBHC" or the "Company") is a bank holding company that was incorporated in the State of Delaware in June 2009 with the intent to acquire and operate financial services franchises and other complementary businesses in targeted markets. The Company is headquartered immediately south of Denver, in Greenwood Village, Colorado, and its primary operations are conducted through its wholly owned subsidiary, NBH Bank, N.A. The Company provides a variety of banking products to both commercial and consumer clients through a network of 97 banking centers located in Colorado, the greater Kansas City area and Texas, and through on-line and mobile banking products.

These interim consolidated financial statements serve to update the National Bank Holdings Corporation Annual Report on Form 10-K for the year ended December 31, 2013. The accompanying consolidated financial statements include the accounts of the Company and its wholly owned subsidiary, NBH Bank, N.A. The accompanying consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) and where applicable, with general practices in the banking industry or guidelines prescribed by bank regulatory agencies. However, they may not include all information and notes necessary to constitute a complete set of financial statements under GAAP applicable to annual periods and accordingly should be read in conjunction with the financial information contained in the Form 10-K. The consolidated financial statements reflect all adjustments which are, in the opinion of management, necessary for a fair statement of the results presented. All such adjustments are of a normal recurring nature. All significant intercompany balances and transactions have been eliminated in consolidation. Certain reclassifications of prior years' amounts are made whenever necessary to conform to current period presentation. The results of operations for the interim period is not necessarily indicative of the results that may be expected for the full year or any other interim period.

The Company's significant accounting policies followed in the preparation of the consolidated financial statements are disclosed in note 2 of the audited financial statements and notes for the year ended December 31, 2013 and are contained in the Company's Annual Report on Form 10-K. There have not been any significant changes to the application of significant accounting policies since December 31, 2013. GAAP requires management to make estimates that affect the reported amounts of assets, liabilities, revenues and expenses, and disclosures of contingent assets and liabilities. By their nature, estimates are based on judgment and available information. Management has made significant estimates in certain areas, such as the amount and timing of expected cash flows from assets, the valuation of the FDIC indemnification asset and clawback liability, the valuation of other real estate owned (“OREO”), the fair value adjustments on assets acquired and liabilities assumed, the valuation of core deposit intangible assets, the evaluation of investment securities for other-than-temporary impairment (“OTTI”), the valuation of stock-based compensation, the fair values of financial instruments, the allowance for loan losses (“ALL”), and contingent liabilities. Because of the inherent uncertainties associated with any estimation process and future changes in market and economic conditions, it is possible that actual results could differ significantly from those estimates.

Note 2 Recent Accounting Pronouncements

Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure - In January 2014, the FASB issued ASU 2014-04, “Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure.” This update amends ASC Topic 310-40 and clarifies that an “in substance repossession or foreclosure” has occurred upon the creditor obtaining either legal title to the property upon completion of foreclosure, or the borrower conveying all interest in the property through completion of a deed in lieu of foreclosure. Upon occurrence, the creditor derecognizes the loan receivable and recognizes the collateralized real estate property. The amendments in the ASU will be effective for the Company for interim and annual periods beginning after December 15, 2014. Early adoption is permitted. Adoption of this amendment can be made using either a modified retrospective transition method or a prospective transition method. The adoption of this standard is not expected to have a material impact on the Company's consolidated financial statements, results of operations or liquidity.

Note 3 Investment Securities

The Company's investment securities portfolio is comprised of available-for-sale and held-to-maturity investment securities. These investment securities totaled $2.3 billion at March 31, 2014 and $2.4 billion at December 31, 2013. Included in the aforementioned $2.3 billion was $1.7 billion of available-for-sale securities and $0.6 billion of held-to-maturity securities.

NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)
March 31, 2014

Available-for-sale
Available-for-sale investment securities are summarized as follows as of the dates indicated (in thousands):

	March 31, 2014			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
Asset backed securities	$2,066	$2	$—	$2,068
Mortgage-backed securities ("MBS"):				
Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises	465,901	8,422	(1,367)	472,956
Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises	1,270,165	11,020	(35,788)	1,245,397
Other securities	419	—	—	419
Total	$1,738,551	$19,444	$(37,155)	$1,720,840

	December 31, 2013			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
Asset backed securities	4,534	3	—	4,537
Mortgage-backed securities ("MBS"):				
Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises	490,321	7,670	(3,001)	494,990
Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises	1,320,998	10,764	(46,180)	1,285,582
Other securities	419	—	—	419
Total	$1,816,272	$18,437	$(49,181)	$1,785,528

At March 31, 2014 and December 31, 2013, mortgage-backed securities represented 99.9% and 99.7%, respectively, of the Company's available-for-sale investment portfolio and all mortgage-backed securities were backed by government sponsored enterprises ("GSE") collateral such as Federal Home Loan Mortgage Corporation ("FHLMC") and Federal National Mortgage Association ("FNMA"), and the government sponsored agency Government National Mortgage Association ("GNMA").

The table below summarizes the unrealized losses as of the dates shown, along with the length of the impairment period (in thousands):

	March 31, 2014					
	Less than 12 months		12 months or more		Total	
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
Mortgage-backed securities ("MBS"):						
Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises	$252,142	$(1,366)	$11	$(1)	$252,153	$(1,367)

Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises	601,345	(21,735)	286,886	(14,053)	888,231	(35,788)
Total	$853,487	$(23,101)	$286,897	$(14,054)	$1,140,384	$(37,155)

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NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)
March 31, 2014

	December 31, 2013					
	Less than 12 months		12 months or more		Total	
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
Mortgage-backed securities ("MBS"):						
Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises	$283,177	$(3,000)	$13	$(1)	$283,190	$(3,001)
Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises	876,225	(44,101)	40,740	(2,079)	916,965	(46,180)
Total	$1,159,402	$(47,101)	$40,753	$(2,080)	$1,200,155	$(49,181)

Management evaluated all of the securities in an unrealized loss position and concluded that no other-than-temporary-impairment existed at March 31, 2014 or December 31, 2013. The unrealized losses in the Company's investments issued or guaranteed by U.S. government agencies or sponsored enterprises at March 31, 2014 were caused by changes in interest rates. The Company had no intention to sell these securities before recovery of their amortized cost and believes it will not be required to sell the securities before the recovery of their amortized cost.

The Company pledges certain securities as collateral for public deposits, securities sold under agreements to repurchase and to secure borrowing capacity at the Federal Reserve Bank, if needed. The fair value of available-for-sale investment securities pledged as collateral totaled $191.9 million at March 31, 2014 and $177.6 million December 31, 2013. The increase in pledged available-for-sale investment securities was primarily attributable to an increase in deposit account balances during the three months ended March 31, 2014. Certain investment securities may also be pledged as collateral should the Company utilize its line of credit at the FHLB of Des Moines; however, no investment securities were pledged for this purpose at March 31, 2014 or December 31, 2013.

The table below summarizes the contractual maturities, as of the last scheduled repayment date, of the available-for-sale investment portfolio as of March 31, 2014 (in thousands):

	Amortized cost	Fair value
Due in one year or less	$—	$—
Due after one year through five years	2,074	2,076
Due after five years through ten years	185,658	185,373
Due after ten years	1,550,400	1,532,972
Other securities	419	419
Total investment securities available-for-sale	$1,738,551	$1,720,840

Actual maturities of mortgage-backed securities may differ from contractual maturities depending on the repayment characteristics and experience of the underlying financial instruments. The estimated weighted average life of the available-for-sale mortgage-backed securities portfolio was 3.8 years as of March 31, 2014 and 3.9 years as of December 31, 2013. This estimate is based on assumptions and actual results may differ. Other securities of $0.4 million have no stated contractual maturity date as of March 31, 2014.

Held-to-maturity

At March 31, 2014 and December 31, 2013 the Company held $616.2 million and $641.9 million of held-to-maturity investment securities, respectively. Held-to-maturity investment securities are summarized as follows as of the dates indicated (in thousands):

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NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)
March 31, 2014

	March 31, 2014			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
Mortgage-backed securities ("MBS"):				
Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises	$492,294	$1,537	$(862)	$492,969
Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises	123,927	320	(3,093)	121,154
Total investment securities held-to-maturity	$616,221	$1,857	$(3,955)	$614,123

	December 31, 2013			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
Mortgage-backed securities ("MBS"):				
Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises	$513,090	$175	$(1,776)	$511,489
Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises	128,817	104	(4,005)	124,916
Total investment securities held-to-maturity	$641,907	$279	$(5,781)	$636,405

The table below summarizes the contractual maturities, as of the last scheduled repayment date, of the held-to-maturity investment portfolio at March 31, 2014 (in thousands):

	Amortized cost	Fair value
Due in one year or less	$—	$—
Due after one year through five years	—	—
Due after five years through ten years	17,597	17,760
Due after ten years	598,624	596,363
Total investment securities held-to-maturity	$616,221	$614,123

The carrying value of held-to-maturity investment securities pledged as collateral totaled $58.9 million and $68.5 million at March 31, 2014 and December 31, 2013, respectively. All of the held-to-maturity investment securities in unrealized loss positions at March 31, 2014 and December 31, 2013 had been in continuous unrealized loss positions for less than 12 months at the respective reporting dates. Actual maturities of mortgage-backed securities may differ from scheduled maturities depending on the repayment characteristics and experience of the underlying financial instruments. The estimated weighted average expected life of the held-to-maturity mortgage-backed securities portfolio as of March 31, 2014 and December 31, 2013 was 3.8 years. This estimate is based on assumptions and actual results may differ.

Note 4 Loans

The loan portfolio is comprised of loans originated by the Company and loans that were acquired in connection with the Company's acquisitions of Bank of Choice and Community Banks of Colorado in 2011, and Hillcrest Bank and Bank Midwest in 2010. The majority of the loans acquired in the Hillcrest Bank and Community Banks of Colorado transactions are covered by loss sharing agreements with the FDIC, and covered loans are presented separately from non-covered loans due to the FDIC loss-sharing agreements associated with these loans. Covered loans comprised

14.7% of the total loan portfolio at March 31, 2014, compared to 16.7% of the total loan portfolio at December 31, 2013.

The table below shows the loan portfolio composition including carrying value by segment of loans accounted for under ASC Topic 310-30 Receivables—Loans and Debt Securities Acquired with Deteriorated Credit Quality and loans not accounted for under this guidance, which includes our originated loans. The table also shows the amounts covered by the FDIC loss-sharing agreements as of March 31, 2014 and December 31, 2013. The carrying value of loans are net of discounts on loans excluded

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from Accounting Standards Codification ("ASC") Topic 310-30, and fees and costs of $12.9 million and $13.3 million as of March 31, 2014 and December 31, 2013, respectively (in thousands):

	March 31, 2014				
	ASC 310-30 loans	Non 310-30 loans	Total loans	% of total	
Commercial	$52,107	$530,462	$582,569	29.7	%
Commercial real estate	263,608	317,137	580,745	29.6	%
Agriculture	23,545	131,586	155,131	7.9	%
Residential real estate	60,467	548,758	609,225	31.1	%
Consumer	6,819	27,103	33,922	1.7	%
Total	$406,546	$1,555,046	$1,961,592	100.0	%
Covered	$244,322	$43,268	$287,590	14.7	%
Non-covered	162,224	1,511,778	1,674,002	85.3	%
Total	$406,546	$1,555,046	$1,961,592	100.0	%

	December 31, 2013				
	ASC 310-30 loans	Non 310-30 loans	Total loans	% of total	
Commercial	$61,511	$421,984	$483,495	26.1	%
Commercial real estate	291,198	283,022	574,220	31.0	%
Agriculture	27,000	132,952	159,952	8.6	%
Residential real estate	63,011	536,913	599,924	32.3	%
Consumer	8,160	28,343	36,503	2.0	%
Total	$450,880	$1,403,214	$1,854,094	100.0	%
Covered	$259,364	$50,033	$309,397	16.7	%
Non-covered	191,516	1,353,181	1,544,697	83.3	%
Total	$450,880	$1,403,214	$1,854,094	100.0	%

Loans are considered past due or delinquent when the contractual principal or interest due in accordance with the terms of the loan agreement remains unpaid after the due date of the scheduled payment. During 2013, the Company determined that the cash flows of one covered commercial and industrial loan pool were no longer reasonably estimable, and in accordance with the guidance in ASC 310-30, this pool was put on non-accrual status. During the three months ended March 31, 2014, this loan pool was returned to accrual status due to improved performance and predictability of cash flows within that pool. At March 31, 2014, this loan pool had a carrying value of $14.7 million. Interest income was recognized on all accruing loans accounted for under ASC 310-30 through accretion of the difference between the carrying value of the loans and the expected cash flows.

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Pooled loans accounted for under ASC 310-30 that are 90 days or more past due and still accreting are generally considered to be performing and are included in loans 90 days or more past due and still accruing. At March 31, 2014 and December 31, 2013, $9.7 million and $9.5 million, respectively, of loans excluded from the scope of ASC 310-30 were on non-accrual and $14.8 million of loans accounted for under ASC 310-30 were on non-accrual status at December 31, 2013. Loan delinquency for all loans is shown in the following tables at March 31, 2014 and December 31, 2013, respectively (in thousands):

	Total Loans March 31, 2014							
	30-59 days past due	60-89 days past due	Greater than 90 days past due	Total past due	Current	Total loans	Loans > 90 days past due and still accruing	Non-accrual
Loans excluded from ASC 310-30								
Commercial	$1,210	$1,020	$282	$2,512	$527,950	$530,462	$25	$992
Commercial real estate								
Construction	—	—	—	—	4,957	4,957	—	—
Acquisition/development	44	—	—	44	8,225	8,269	—	—
Multifamily	99	—	—	99	10,294	10,393	—	1,059
Owner-occupied	255	387	52	694	109,089	109,783	—	956
Non owner-occupied	113	38	203	354	183,381	183,735	—	203
Total commercial real estate	511	425	255	1,191	315,946	317,137	—	2,218
Agriculture	80	—	365	445	131,141	131,586	—	539
Residential real estate								
Senior lien	1,401	533	750	2,684	494,576	497,260	—	5,283
Junior lien	65	17	46	128	51,370	51,498	—	482
Total residential real estate	1,466	550	796	2,812	545,946	548,758	—	5,765
Consumer	764	11	29	804	26,299	27,103	28	224
Total loans excluded from ASC 310-30	$4,031	$2,006	$1,727	$7,764	$1,547,282	$1,555,046	$53	$9,738
Covered loans excluded from ASC 310-30	$174	$52	$351	$577	$42,691	$43,268	$—	$2,175
Non-covered loans excluded from ASC 310-30	3,857	1,954	1,376	7,187	1,504,591	1,511,778	53	7,563
Total loans excluded from ASC 310-30	$4,031	$2,006	$1,727	$7,764	$1,547,282	$1,555,046	$53	$9,738
Loans accounted for under ASC 310-30								
Commercial	$15,819	$538	$4,372	$20,729	$31,378	$52,107	$4,372	$—
Commercial real estate	4,425	2,636	41,218	48,279	215,329	263,608	41,219	—
Agriculture	43	—	51	94	23,451	23,545	51	—
Residential real estate	1,997	242	1,968	4,207	56,260	60,467	1,968	—
Consumer	166	7	179	352	6,467	6,819	179	—
Total loans accounted for under ASC 310-30	$22,450	$3,423	$47,788	$73,661	$332,885	$406,546	$47,789	—

Covered loans accounted for under ASC 310-30	$18,589	$2,501	$37,198	$58,288	$186,034	$244,322	$37,199	$—
Non-covered loans accounted for under ASC 310-30	3,861	922	10,590	15,373	146,851	162,224	10,590	—
Total loans accounted for under ASC 310-30	$22,450	$3,423	$47,788	$73,661	$332,885	$406,546	$47,789	$—
Total loans	$26,481	$5,429	$49,515	$81,425	$1,880,167	$1,961,592	$47,842	$9,738
Covered loans	$18,763	$2,553	$37,549	$58,865	$228,725	$287,590	$37,199	$2,175
Non-covered loans	7,718	2,876	11,966	22,560	1,651,442	1,674,002	10,643	7,563
Total loans	$26,481	$5,429	$49,515	$81,425	$1,880,167	$1,961,592	$47,842	$9,738

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	Total Loans December 31, 2013							
	30-59 days past due	60-89 days past due	Greater than 90 days past due	Total past due	Current	Total loans	Loans > 90 days past due and still accruing	Non-accrual
Loans excluded from ASC 310-30								
Commercial	$897	$156	$555	$1,608	$420,376	$421,984	$115	$1,280
Commercial real estate								
Construction	316	—	—	316	5,023	5,339	—	—
Acquisition/development	45	—	—	45	7,975	8,020	—	1
Multifamily	1,003	—	—	1,003	9,681	10,684	—	1,096
Owner-occupied	52	7	21	80	93,367	93,447	—	692
Non owner-occupied	329	—	203	532	165,000	165,532	—	203
Total commercial real estate	1,745	7	224	1,976	281,046	283,022	—	1,992
Agriculture	188	7	—	195	132,757	132,952	—	153
Residential real estate								
Senior lien	733	415	1,062	2,210	482,381	484,591	—	5,326
Junior lien	204	—	80	284	52,038	52,322	—	519
Total residential real estate	937	415	1,142	2,494	534,419	536,913	—	5,845
Consumer	191	21	23	235	28,108	28,343	14	247
Total loans excluded from ASC 310-30	$3,958	$606	$1,944	$6,508	$1,396,706	$1,403,214	$129	$9,517
Covered loans excluded from ASC 310-30	194	60	155	409	49,624	50,033	115	1,944
Non-covered loans excluded from ASC 310-30	3,764	546	1,789	6,099	1,347,082	1,353,181	14	7,573
Total loans excluded from ASC 310-30	$3,958	$606	$1,944	$6,508	$1,396,706	$1,403,214	$129	$9,517
Loans accounted for under ASC 310-30								
Commercial	$582	$322	$4,505	$5,409	$56,102	$61,511	$4,505	$14,827
Commercial real estate	1,902	5,179	49,228	56,309	234,889	291,198	49,227	—
Agriculture	714	—	296	1,010	25,990	27,000	296	—
Residential real estate	977	977	1,817	3,771	59,240	63,011	1,817	—
Consumer	327	265	19	611	7,549	8,160	19	—
Total loans accounted for under ASC 310-30	$4,502	$6,743	$55,865	$67,110	$383,770	$450,880	$55,864	$14,827
Covered loans accounted for under ASC 310-30	$1,471	$4,949	$42,356	$48,776	$210,588	$259,364	$42,355	$14,827
Non-covered loans accounted for under ASC 310-30	3,031	1,794	13,509	18,334	173,182	191,516	13,509	—
Total loans accounted for under ASC 310-30	$4,502	$6,743	$55,865	$67,110	$383,770	$450,880	$55,864	$14,827

Total loans	$8,460	$7,349	$57,809	$73,618	$1,780,476	$1,854,094	$55,993	$24,344
Covered loans	$1,665	$5,009	$42,511	$49,185	$260,212	$309,397	$42,470	$16,771
Non-covered loans	6,795	2,340	15,298	24,433	1,520,264	1,544,697	13,523	7,573
Total loans	$8,460	$7,349	$57,809	$73,618	$1,780,476	$1,854,094	$55,993	$24,344

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Credit exposure for all loans as determined by the Company's internal risk rating system was as follows as of March 31, 2014 and December 31, 2013, respectively (in thousands):

	Total Loans March 31, 2014				
	Pass	Special mention	Substandard	Doubtful	Total
Loans excluded from ASC 310-30					
Commercial	$489,203	$5,394	$35,681	$184	$530,462
Commercial real estate					
Construction	4,957	—	—	—	4,957
Acquisition/development	1,558	2,248	4,463	—	8,269
Multifamily	9,334	—	1,034	25	10,393
Owner-occupied	104,127	166	5,490	—	109,783
Non owner-occupied	161,381	18,140	4,214	—	183,735
Total commercial real estate	281,357	20,554	15,201	25	317,137
Agriculture	121,436	331	9,819	—	131,586
Residential real estate					
Senior lien	488,132	1,223	7,497	408	497,260
Junior lien	49,119	197	2,182	—	51,498
Total residential real estate	537,251	1,420	9,679	408	548,758
Consumer	26,876	—	227	—	27,103
Total loans excluded from ASC 310-30	$1,456,123	$27,699	$70,607	$617	$1,555,046
Covered loans excluded from ASC 310-30	$16,698	$2,920	$23,177	$473	$43,268
Non-covered loans excluded from ASC 310-30	1,439,425	24,779	47,430	144	1,511,778
Total loans excluded from ASC 310-30	$1,456,123	$27,699	$70,607	$617	$1,555,046
Loans accounted for under ASC 310-30					
Commercial	$14,576	$3,732	$33,101	$698	$52,107
Commercial real estate	109,069	6,712	142,766	5,061	263,608
Agriculture	20,297	661	2,587	—	23,545
Residential real estate	42,810	916	16,741	—	60,467
Consumer	5,818	216	785	—	6,819
Total loans accounted for under ASC 310-30	$192,570	$12,237	$195,980	$5,759	$406,546
Covered loans accounted for under ASC 310-30	$89,706	$6,072	$142,785	$5,759	$244,322
Non-covered loans accounted for under ASC 310-30	102,864	6,165	53,195	—	162,224
Total loans accounted for under ASC 310-30	$192,570	$12,237	$195,980	$5,759	$406,546
Total loans	$1,648,693	$39,936	$266,587	$6,376	$1,961,592
Total covered	$106,404	$8,992	$165,962	$6,232	$287,590
Total non-covered	1,542,289	30,944	100,625	144	1,674,002
Total loans	$1,648,693	$39,936	$266,587	$6,376	$1,961,592

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	Total Loans December 31, 2013				
	Pass	Special mention	Substandard	Doubtful	Total
Loans excluded from ASC 310-30					
Commercial	$374,281	$9,882	$37,414	$407	$421,984
Commercial real estate					
Construction	5,339	—	—	—	5,339
Acquisition/development	1,366	2,247	4,407	—	8,020
Multifamily	9,588	—	1,068	28	10,684
Owner-occupied	87,984	169	5,294	—	93,447
Non owner-occupied	142,159	18,536	4,837	—	165,532
Total commercial real estate	246,436	20,952	15,606	28	283,022
Agriculture	123,216	9,049	687	—	132,952
Residential real estate					
Senior lien	475,041	1,495	7,620	435	484,591
Junior lien	49,874	200	2,248	—	52,322
Total residential real estate	524,915	1,695	9,868	435	536,913
Consumer	28,092	—	251	—	28,343
Total loans excluded from ASC 310-30	$1,296,940	$41,578	$63,826	$870	$1,403,214
Covered loans excluded from ASC 310-30	$22,175	$3,439	$24,005	$414	$50,033
Non-covered loans excluded from ASC 310-30	1,274,765	38,139	39,821	456	1,353,181
Total loans excluded from ASC 310-30	$1,296,940	$41,578	$63,826	$870	$1,403,214
Loans accounted for under ASC 310-30					
Commercial	$23,129	$3,221	$34,440	$721	$61,511
Commercial real estate	115,903	12,493	157,748	5,054	291,198
Agriculture	21,900	1,117	3,983	—	27,000
Residential real estate	43,904	1,098	18,009	—	63,011
Consumer	6,921	244	995	—	8,160
Total loans accounted for under ASC 310-30	$211,757	$18,173	$215,175	$5,775	$450,880
Covered loans accounted for under ASC 310-30	$100,050	$8,498	$145,041	$5,775	$259,364
Non-covered loans accounted for under ASC 310-30	111,707	9,675	70,134	—	191,516
Total loans accounted for under ASC 310-30	$211,757	$18,173	$215,175	$5,775	$450,880
Total loans	$1,508,697	$59,751	$279,001	$6,645	$1,854,094
Total covered	$122,225	$11,937	$169,046	$6,189	$309,397
Total non-covered	1,386,472	47,814	109,955	456	1,544,697
Total loans	$1,508,697	$59,751	$279,001	$6,645	$1,854,094

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Impaired Loans

Loans are considered to be impaired when it is probable that the Company will not be able to collect all amounts due in accordance with the contractual terms of the loan agreement. Impaired loans are comprised of loans excluded from ASC 310-30 on non-accrual status and troubled debt restructurings (“TDRs”) described below. If a specific allowance is warranted based on the borrower’s overall financial condition, the specific allowance is calculated based on discounted cash flows using the loan’s initial contractual effective interest rate or the fair value of the collateral less selling costs for collateral dependent loans. At March 31, 2014, the Company measured $7.3 million of impaired loans using discounted cash flows and the loan’s initial contractual effective interest rate and $16.2 million of impaired loans based on the fair value of the collateral less selling costs. Impaired loans totaling $9.6 million that individually were less than $250 thousand each, were measured through our general ALL reserves due to their relatively small size.

At March 31, 2014 and December 31, 2013, the Company’s recorded investments in impaired loans was $33.1 million and $21.6 million, respectively, of which $6.9 million and $7.7 million were covered by loss-sharing agreements, for the aforementioned periods. Impaired loans had a collective related allowance for loan losses allocated to them of $0.7 million and $0.9 million at March 31, 2014 and December 31, 2013, respectively. Additional information regarding impaired loans at March 31, 2014 and December 31, 2013 is set forth in the table below (in thousands):

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	Impaired Loans March 31, 2014			December 31, 2013		
	Unpaid principal balance	Recorded investment	Allowance for loan losses allocated	Unpaid principal balance	Recorded investment	Allowance for loan losses allocated
With no related allowance recorded:						
Commercial	$7,024	$7,015	$—	$4,981	$4,981	$—
Commercial real estate						
Construction	—	—	—	—	—	—
Acquisition/development	398	398	—	—	—	—
Multifamily	972	898	—	987	929	—
Owner-occupied	1,826	1,606	—	1,872	1,655	—
Non-owner occupied	548	475	—	561	488	—
Total commercial real estate	3,744	3,377	—	3,420	3,072	—
Agriculture	9,143	9,132	—	—	—	—
Residential real estate						
Senior lien	720	700	—	506	494	—
Junior lien	—	—	—	—	—	—
Total residential real estate	720	700	—	506	494	—
Consumer	—	—	—	—	—	—
Total impaired loans with no related allowance recorded	$20,631	$20,224	$—	$8,907	$8,547	$—
With a related allowance recorded:						
Commercial	$2,545	$2,046	$190	$2,529	$2,379	$416
Commercial real estate						
Construction	—	—	—	—	—	—
Acquisition/development	—	—	—	—	1	—
Multifamily	173	162	25	178	168	28
Owner-occupied	1,109	873	5	825	607	4
Non-owner occupied	634	623	2	640	628	4
Total commercial real estate	1,916	1,658	32	1,643	1,404	36
Agriculture	194	174	1	191	173	1
Residential real estate						
Senior lien	8,136	7,197	438	8,147	7,266	474
Junior lien	1,769	1,555	15	1,815	1,605	16
Total residential real estate	9,905	8,752	453	9,962	8,871	490
Consumer	270	249	3	290	273	3
Total impaired loans with a related allowance recorded	$14,830	$12,879	$679	$14,615	$13,100	$946
Total impaired loans	$35,461	$33,103	$679	$23,522	$21,647	$946

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The table below shows additional information regarding the average recorded investment and interest income recognized on impaired loans for the periods presented (in thousands):

	For the three months ended			
	March 31, 2014		March 31, 2013	
	Average recorded investment	Interest income recognized	Average recorded investment	Interest income recognized
With no related allowance recorded:				
Commercial	$7,562	$94	$11,033	$128
Commercial real estate				
Construction	—	—	—	—
Acquisition/development	398	5	—	—
Multifamily	908	—	—	—
Owner-occupied	1,622	26	5,036	80
Non owner-occupied	480	8	1,862	5
Total commercial real estate	3,408	39	6,898	85
Agriculture	9,132	119	—	—
Residential real estate				
Senior lien	701	4	364	1
Junior lien	—	—	—	—
Total residential real estate	701	4	364	1
Consumer	—	—	—	—
Total impaired loans with no related allowance recorded	$20,803	$256	$18,295	$214
With a related allowance recorded:				
Commercial	$2,113	$12	$3,172	$3
Commercial real estate				
Construction	—	—	—	—
Acquisition/development	—	—	15	—
Multifamily	165	—	196	—
Owner-occupied	879	3	763	4
Non owner-occupied	625	7	6,544	3
Total commercial real estate	1,669	10	7,518	7
Agriculture	177	—	240	—
Residential real estate				
Senior lien	7,243	27	6,791	21
Junior lien	1,566	15	1,096	11
Total residential real estate	8,809	42	7,887	32
Consumer	250	—	479	4
Total impaired loans with a related allowance recorded	$13,018	$64	$19,296	$46
Total impaired loans	$33,821	$320	$37,591	$260

Troubled debt restructurings
It is the Company's policy to review each prospective credit in order to determine the appropriateness and the adequacy of security or collateral prior to making a loan. In the event of borrower default, the Company seeks recovery in compliance with

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state lending laws, the respective loan agreements, and credit monitoring and remediation procedures that may include restructuring a loan to provide a concession by the Company to the borrower from their original terms due to borrower financial difficulties in order to facilitate repayment. Additionally, if a borrower's repayment obligation has been discharged by a court, and that debt has not been reaffirmed by the borrower, regardless of past due status, the loan is considered to be a troubled debt restructuring ("TDR"). At March 31, 2014 and December 31, 2013, the Company had $22.5 million and $11.6 million, respectively, of accruing TDRs that had been restructured from the original terms in order to facilitate repayment. Of these, $4.7 million and $5.7 million, respectively, were covered by FDIC loss-sharing agreements.

Non-accruing TDRs at March 31, 2014 and December 31, 2013 totaled $3.6 million. Of these, $1.7 million were covered by the FDIC loss-sharing agreements as of March 31, 2014 and December 31, 2013.

During the three months ended March 31, 2014, the Company restructured eight loans with a recorded investment of $12.5 million to facilitate repayment. Substantially all of the loan modifications were an extension of term. Loan modifications to loans accounted for under ASC 310-30 are not considered TDRs. The table below provides additional information related to accruing TDRs at March 31, 2014 and December 31, 2013 (in thousands):

	Accruing TDRs March 31, 2014			
	Recorded investment	Average year-to-date recorded investment	Unpaid principal balance	Unfunded commitments to fund TDRs
Commercial	$8,069	$8,631	$8,082	$—
Commercial real estate	2,818	2,839	3,075	—
Agriculture	8,767	8,767	8,778	105
Residential real estate	2,841	2,856	2,869	12
Consumer	25	25	25	—
Total	$22,520	$23,118	$22,829	$117

	Accruing TDRs December 31, 2013			
	Recorded investment	Average year-to-date recorded investment	Unpaid principal balance	Unfunded commitments to fund TDRs
Commercial	$6,079	$7,113	$6,084	$144
Commercial real estate	2,484	2,759	2,743	—
Agriculture	20	20	20	—
Residential real estate	2,995	3,055	3,023	12
Consumer	27	30	27	12
Total	$11,605	$12,977	$11,897	$168

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The following table summarizes the Company's carrying value of non-accrual TDRs as of March 31, 2014 and December 31, 2013 (in thousands):

	Non - Accruing TDRs			
	March 31, 2014		December 31, 2013	
	Covered	Non-covered	Covered	Non-covered
Commercial	$30	$497	$—	$535
Commercial real estate	283	92	296	98
Agriculture	—	18	—	—
Residential real estate	1,349	1,105	1,377	1,031
Consumer	—	224	—	237
Total	$1,662	$1,936	$1,673	$1,901

Accrual of interest is resumed on loans that were on non-accrual, only after the loan has performed sufficiently. The Company had two TDRs that had been modified within the past 12 months that defaulted on their restructured terms during the three months ended March 31, 2014. The defaulted TDRs were an agriculture loan and a consumer loan totaling $26 thousand.

During the three months ended March 31, 2013, the Company had three TDRs that had been modified within the past 12 months that defaulted on their restructured terms. The defaulted TDRs were a commercial loan, a commercial real estate loan, and a single family residential loan totaling $2.8 million. For purposes of this disclosure, the Company considers "default" to mean 90 days or more past due on principal or interest.

Loans accounted for under ASC Topic 310-30

Loan pools accounted for under ASC Topic 310-30 are periodically remeasured to determine expected future cash flows. In determining the expected cash flows, the timing of cash flows and prepayment assumptions for smaller homogeneous loans are based on statistical models that take into account factors such as the loan interest rate, credit profile of the borrowers, the years in which the loans were originated, and whether the loans are fixed or variable rate loans. Prepayments may be assumed on large loans if circumstances specific to that loan warrant a prepayment assumption. No prepayments were presumed for small homogeneous commercial loans; however, prepayment assumptions are made that consider similar prepayment factors listed above for smaller homogeneous loans. The re-measurement of loans accounted for under ASC 310-30 resulted in the following changes in the carrying amount of accretable yield during the three months ended March 31, 2014 and 2013 (in thousands):

	March 31, 2014	March 31, 2013
Accretable yield beginning balance	$130,624	$133,585
Reclassification from non-accretable difference	6,164	16,134
Reclassification to non-accretable difference	(590)	(1,202)
Accretion	(16,900)	(21,302)
Accretable yield ending balance	$119,298	$127,215

Below is the composition of the net book value for loans accounted for under ASC 310-30 at March 31, 2014 and December 31, 2013 (in thousands):

	March 31, 2014	December 31, 2013
Contractual cash flows	$922,774	$984,019
Non-accretable difference	(396,930)	(402,515)
Accretable yield	(119,298)	(130,624)
Loans accounted for under ASC 310-30	$406,546	$450,880

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Note 5 Allowance for Loan Losses
The tables below detail the Company's allowance for loan losses ("ALL") and recorded investment in loans as of and for the three months ended March 31, 2014 and 2013 (in thousands):

	Three months ended March 31, 2014					
	Commercial	Commercial real estate	Agriculture	Residential real estate	Consumer	Total
Beginning balance	$4,258	$2,276	$1,237	$4,259	$491	$12,521
Non 310-30 beginning balance	4,029	1,984	572	4,165	491	11,241
Charge-offs	(386)	—	—	(20)	(171)	(577)
Recoveries	58	37	—	90	76	261
Provision (reversal)	1,880	(44)	(24)	(66)	77	1,823
Non 310-30 ending balance	5,581	1,977	548	4,169	473	12,748
ASC 310-30 beginning balance	229	292	665	94	—	1,280
Charge-offs	(2)	—	—	—	—	(2)
Recoveries	—	—	—	—	—	—
Provision (reversal)	(84)	(56)	—	(29)	115	(54)
ASC 310-30 ending balance	143	236	665	65	115	1,224
Ending balance	$5,724	$2,213	$1,213	$4,234	$588	$13,972
Ending allowance balance attributable to:						
Non 310-30 loans individually evaluated for impairment	$190	$32	$1	$453	$3	$679
Non 310-30 loans collectively evaluated for impairment	5,391	1,945	547	3,716	470	12,069
ASC 310-30 loans	143	236	665	65	115	1,224
Total ending allowance balance	$5,724	$2,213	$1,213	$4,234	$588	$13,972
Loans:						
Non 310-30 individually evaluated for impairment	$9,061	$5,035	$9,306	$9,452	$249	$33,103
Non 310-30 collectively evaluated for impairment	521,401	312,102	122,280	539,306	26,854	1,521,943
ASC 310-30 loans	52,107	263,608	23,545	60,467	6,819	406,546
Total loans	$582,569	$580,745	$155,131	$609,225	$33,922	$1,961,592

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	Three months ended March 31, 2013					
	Commercial	Commercial real estate	Agriculture	Residential real estate	Consumer	Total
Beginning balance	$2,798	$7,396	$592	$4,011	$583	$15,380
Non 310-30 beginning balance	2,798	3,056	323	4,011	540	10,728
Charge-offs	(629)	(259)	—	(75)	(233)	(1,196)
Recoveries	9	—	—	14	77	100
Provision (reversal)	697	(305)	201	406	109	1,108
Non 310-30 ending balance	2,875	2,492	524	4,356	493	10,740
ASC 310-30 beginning balance	—	4,340	269	—	43	4,652
Charge-offs	—	(2,812)	—	—	—	(2,812)
Recoveries	—	—	—	—	—	—
Provision (reversal)	411	(1,045)	—	986	(43)	309
ASC 310-30 ending balance	411	483	269	986	—	2,149
Ending balance	$3,286	$2,975	$793	$5,342	$493	$12,889
Ending allowance balance attributable to:						
Non 310-30 loans individually evaluated for impairment	$1,125	$371	$1	$721	$13	$2,231
Non 310-30 loans collectively evaluated for impairment	1,750	2,121	523	3,635	480	8,509
ASC 310-30 loans	411	483	269	986	—	2,149
Total ending allowance balance	$3,286	$2,975	$793	$5,342	$493	$12,889
Loans:						
Non 310-30 individually evaluated for impairment	$13,381	$14,314	$227	$8,214	$469	$36,605
Non 310-30 collectively evaluated for impairment	172,421	241,818	117,930	437,971	28,456	998,596
ASC 310-30 loans	78,928	490,608	46,580	101,386	12,747	730,249
Total loans	$264,730	$746,740	$164,737	$547,571	$41,672	$1,765,450

In evaluating the loan portfolio for an appropriate ALL level, non-impaired loans that were not accounted for under ASC 310-30 were grouped into segments based on broad characteristics such as primary use and underlying collateral. Within the segments, the portfolio was further disaggregated into classes of loans with similar attributes and risk characteristics for purposes of applying loss ratios and determining applicable subjective adjustments to the ALL. The application of subjective adjustments was based upon qualitative risk factors, including economic trends and conditions, industry conditions, asset quality, loss trends, lending management, portfolio growth and loan review/internal audit results.

The Company charged-off $0.3 million, net of recoveries, of non 310-30 loans during the three months ended March 31, 2014, all of which had previously provided specific reserves. Strong credit quality trends of the non 310-30 loan portfolio continued during the three months ended March 31, 2014, and, through management's evaluation, resulted in a provision for loan losses on the non 310-30 loans of $1.8 million.

During the three months ended March 31, 2014, the Company re-estimated the expected cash flows of the loan pools accounted for under ASC 310-30 utilizing the same cash flow methodology used at the time of acquisition. The re-measurement resulted in a net reversal of impairment of $54.0 thousand for the three months ended March 31, 2014 which was comprised of reversals of previous valuation allowances of $84.0 thousand, $56.0 thousand and $29.0

thousand in the commercial, commercial real estate and residential real estate segments, respectively, and net impairments of $115.0 thousand in the consumer segment.
During the three months ended March 31, 2013, the Company recorded $1.1 million of provision for loan losses for loans not accounted for under ASC 310-30, primarily to provide for changes in credit risk inherent in new loan originations and provide for charge-offs. The Company charged off $1.1 million, net of recoveries, of non 310-30 loans during the three months ended

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March 31, 2013. Commercial charge-offs, net of recoveries, totaled $0.6 million, the commercial real estate segment experienced $0.3 million of net charge-offs, and net charge-offs on consumer loans totaled $0.2 million, for the three months ended March 31, 2013.

During the three months ended March 31, 2013, the Company's re-measurement of expected future cash flows of ASC 310-30 loans resulted in a net impairment of $0.3 million, which was primarily driven by impairments of $1.0 million in the residential real estate segment and $0.4 million in the commercial segment, offset by a reversal of $1.0 million of previously recognized impairment expense in the commercial real estate segment as a result of gross cash flow improvements.

Note 6 FDIC Indemnification Asset

Under the terms of the purchase and assumption agreement with the FDIC with regard to the Hillcrest Bank and Community Banks of Colorado acquisitions, the Company is reimbursed for a portion of the losses incurred on covered assets. Covered assets may be resolved through repayment, short sale of the underlying collateral, the foreclosure on and sale of collateral, or the sale or charge-off of loans or OREO. Any gains or losses realized from the resolution of covered assets reduce or increase, respectively, the amount recoverable from the FDIC. Covered gains or losses that are incurred in excess of the expected reimbursements (which are reflected in the FDIC indemnification asset balance), are recognized in the consolidated statements of operations as FDIC loss sharing income in the period in which they occur.

Below is a summary of the activity related to the FDIC indemnification asset during the three months ended March 31, 2014 and 2013 (in thousands):

	For the three months ended	
	March 31, 2014	March 31, 2013
Balance at beginning of period	$64,447	$86,923
Amortization	(7,608)	(4,669)
FDIC portion of (recoveries) charge-offs exceeding fair value marks	(133)	2,576
Reduction for claims filed	(29)	(9,132)
Balance at end of period	$56,677	$75,698

The $7.6 million of amortization of the FDIC indemnification asset recognized during the three months ended March 31, 2014 resulted from an overall increase in actual and expected cash flows of the underlying covered assets, resulting in lower expected reimbursements from the FDIC. The increase in overall expected cash flows from these underlying assets is reflected in increased accretion rates on covered loans and is being recognized over the expected remaining lives of the underlying covered loans as an adjustment to yield. The loss claims filed with the FDIC are subject to review and approval, including extensive audits by the FDIC or its assigned agents for compliance with the terms in the loss sharing agreements. During the three months ended March 31, 2014, the Company received $29 thousand in payments from the FDIC.

During the three months ended March 31, 2013, the Company recognized $4.7 million of amortization on the FDIC indemnification asset, and further reduced the carrying value of the FDIC indemnification asset by $9.1 million as a result of claims filed with the FDIC. During the three months ended March 31, 2013, the Company received $57.9 million in payments from the FDIC.

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Note 7 Other Real Estate Owned

A summary of the activity in the OREO balances during the three months ended March 31, 2014 and 2013 is as follows (in thousands):

	For the three months ended March 31,	
	2014	2013
Beginning balance	$70,125	$94,808
Transfers from loan portfolio, at fair value	236	17,043
Impairments	(822)	(4,600)
Sales	(4,143)	(25,726)
Gain on sale of OREO, net	587	1,805
Ending balance	$65,983	$83,330

Of the $66.0 million of OREO at March 31, 2014, $36.6 million, or 55.4%, was covered by loss sharing agreements with the FDIC. At December 31, 2013, $38.8 million, or 55.4%, of the $70.1 million of OREO was covered by loss sharing agreements. Any losses on these assets are substantially offset by a corresponding change in the FDIC indemnification asset.

The OREO balances include the interests of several outside participating banks totaling $4.2 million at March 31, 2014 and December 31, 2013, for which an offsetting liability is recorded in other liabilities. It excludes $10.6 million, for both of the respective periods, of the Company’s minority interests in OREO which are held by outside banks where the Company was not the lead bank and does not have a controlling interest, for which the Company maintains a receivable in other assets.

Note 8 Regulatory Capital

At March 31, 2014 and December 31, 2013, NBH Bank, N.A. and the consolidated holding company exceeded all capital ratio requirements under prompt corrective action or other regulatory requirements, as is detailed in the table below (in thousands):

	March 31, 2014					
	Actual		Required to be considered well capitalized (1)		Required to be considered adequately capitalized	
	Ratio	Amount	Ratio	Amount	Ratio	Amount
Tier 1 leverage ratio						
Consolidated	16.8 %	$814,857	N/A	N/A	4 %	$193,915
NBH Bank, N.A.	11.6 %	560,025	10 %	$482,407	4 %	192,963
Tier 1 risk-based capital ratio (2)						
Consolidated	36.8 %	$814,857	6 %	$132,791	4 %	$88,528
NBH Bank, N.A.	25.5 %	560,025	11 %	241,156	4 %	87,693
Total risk-based capital ratio (2)						
Consolidated	37.5 %	$829,230	10 %	$221,319	8 %	$177,055
NBH Bank, N.A.	26.2 %	574,398	12 %	263,079	8 %	175,386

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	December 31, 2013							
	Actual			Required to be considered well capitalized (1)			Required to be considered adequately capitalized		
	Ratio		Amount	Ratio		Amount	Ratio		Amount
Tier 1 leverage ratio									
Consolidated	16.6	%	$822,688	N/A		N/A	4	%	$197,906
NBH Bank, N.A.	11.3	%	556,876	10	%	$491,294	4	%	196,518
Tier 1 risk-based capital ratio (2)									
Consolidated	38.9	%	$822,688	6	%	$126,865	4	%	$84,577
NBH Bank, N.A.	26.6	%	556,876	11	%	230,334	4	%	83,758
Total risk-based capital ratio (2)									
Consolidated	39.5	%	$835,810	10	%	$211,442	8	%	$169,153
NBH Bank, N.A.	27.2	%	569,998	12	%	251,273	8	%	167,515

(1) These ratio requirements are reflective of the agreements the Company has made with its various regulators in connection with the approval of the de novo charter for NBH Bank, N.A.

(2) Due to the conditional guarantee represented by the loss sharing agreements, the FDIC indemnification asset and covered assets are risk-weighted at 20% for purposes of risk-based capital computations.

Note 9 FDIC Loss Sharing Income (Expense)

In connection with the loss sharing agreements that the Company has with the FDIC with regard to the Hillcrest Bank and Community Banks of Colorado transactions, the Company recognizes the actual reimbursement of costs of resolution of covered assets from the FDIC through the statements of operations. The table below provides additional details of the Company’s FDIC loss sharing income (expense) during the three months ended March 31, 2014 and 2013 (in thousands):

	For the three months ended			
	March 31, 2014		March 31, 2013	
Clawback liability amortization	$(328	)	$(313	)
Clawback liability remeasurement	(516	)	573	
Reimbursement to FDIC for gain on sale of and income from covered OREO	(918	)	(860	)
Reimbursement to FDIC for recoveries	(85	)	(15	)
FDIC reimbursement of covered asset resolution costs	890		3,891	
Total	$(957	)	$3,276	

Note 10 Stock-based Compensation and Benefits

The Company provides stock-based compensation in accordance with the NBH Holdings Corp. 2009 Equity Incentive Plan (the “Plan”). The Plan provides the compensation committee of the board of directors of the Company the authority to grant, from time to time, awards of options, stock appreciation rights, restricted stock, restricted stock units, stock awards, or stock bonuses to eligible persons. The aggregate number of shares of stock which may be granted under the Plan was 5,750,000 and the maximum number of restricted shares and restricted share units that may be granted was 1,725,000.

To date, the Company has issued stock options and restricted stock under the Plan. The compensation committee sets the option exercise price at the time of grant but in no case is the exercise price less than the fair market value of a share of stock at the date of grant. The Company used information provided by third parties, including independent valuation specialists, as required by the Plan, to assist in the determination of estimates regarding fair values associated with the Company's stock-based compensation issued prior to the Company's initial public offering and listing on a national exchange, including contemporaneous valuations of grant date fair values. The Company is responsible for the assumptions used therein and the resulting values.

The Company did not issue any stock options or restricted stock in accordance with the NBH Holdings Corp. 2009 Equity Incentive Plan (the "Plan") during the three months ended March 31, 2014. The following table summarizes stock option

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activity for the three months ended March 31, 2014:

	Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term in Years	Aggregate Intrinsic Value
Outstanding at December 31, 2013	3,515,486	$19.92	6.13	$5,183,567
Granted	—	—		
Forfeited	—	—		
Surrendered	(9,705)	20.00		
Exercised	(295)	20.00		
Expired	(2,083)	20.00		
Outstanding at March 31, 2014	3,503,403	$19.92	5.91	$520,681
Options fully vested and exercisable at March 31, 2014	2,887,166	$20.00	5.76	$202,102
Options expected to vest	573,660	$19.62	6.34	$459,678

Stock option expense is included in salaries and benefits in the accompanying consolidated statements of operations and totaled $0.3 million and $0.7 million for the three months ended March 31, 2014 and 2013, respectively. At March 31, 2014, there was $1.0 million of total unrecognized compensation cost related to non-vested stock options granted under the Plan. The cost is expected to be recognized over a weighted average period of 0.8 years.

Expense related to non-vested restricted stock totaled $0.4 million and $0.7 million during the three months ended March 31, 2014 and 2013, respectively, and is included in salaries and benefits in the Company's consolidated statements of operations. As of March 31, 2014, there was $1.3 million of total unrecognized compensation cost related to non-vested restricted shares granted under the Plan, which is expected to be recognized over a weighted average period of 1.2 years. The following table summarizes restricted stock activity for the three months ended March 31, 2014:

	Total Restricted Shares	Weighted Average Grant-Date Fair Value
Unvested at December 31, 2013	1,064,460	15.16
Vested	(22,542)	19.94
Granted	—	—
Forfeited	(10,000)	13.14
Surrendered	(10,791)	19.94
Unvested at March 31, 2014	1,021,127	15.02

Note 11 Warrants

At March 31, 2014 and December 31, 2013, the Company had 830,750 outstanding warrants to purchase Company stock. The warrants were granted to certain lead shareholders of the Company, all with an exercise price of $20.00 per share. The term of the warrants is for ten years from the date of grant and the expiration dates of the warrants range from October 20, 2019 to September 30, 2020. The fair value of the warrants was estimated to be $5.4 million and $6.3 million at March 31, 2014 and December 31, 2013, respectively. The fair value of the warrants was estimated using a Black-Scholes option pricing model utilizing the following assumptions at the indicated dates:

	March 31, 2014	December 31, 2013
Risk-free interest rate	1.99 %	2.16 %

Expected volatility	34.04	%	33.80	%
Expected term (years)	5-6		6-7	
Dividend yield	1.00	%	0.93	%

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The Company's shares became publicly traded on September 20, 2012 and prior to that, had limited private trading. Due to the limited historical volatility of the Company's own stock, expected volatility was calculated using a time-based weighted migration of the Company's own stock price volatility coupled with the median historical volatility, for a period commensurate with the expected term of the warrants, of those of a peer group. The risk-free rate for the expected term of the warrants was based on the U.S. Treasury yield curve and based on the expected term. The expected term was estimated based on the contractual term of the warrants.

The Company recorded a benefit of $0.9 million and $0.6 million for the three months ended March 31, 2014 and 2013, respectively, in the consolidated statements of operations resulting from the change in fair value of the warrant liability.

Note 12 Common Stock

On January 23, 2014, the Board of Directors authorized a new share repurchase program to repurchase up to $50 million of the Company's common stock through December 31, 2014. This new program replaced the previous $35 million share repurchase program approved during the fourth quarter of 2013. Under the new share repurchase program, shares may be acquired from time to time either in the open market or in privately negotiated transactions in accordance with applicable regulations of the Securities and Exchange Commission. During the three months ended March 31, 2014, the Company repurchased 454,706 shares for $8.8 million at a weighted average price of $19.35 per share.

The Company had 41,458,693 shares of Class A common stock and 3,027,774 shares of Class B common stock outstanding as of March 31, 2014, and 41,890,562 shares of Class A common stock and 3,027,774 shares of Class B common stock outstanding as of December 31, 2013. Additionally, as of March 31, 2014 and December 31, 2013, the Company had 1,021,127 and 1,064,460 shares, respectively, of restricted Class A common stock issued but not yet vested under the NBH Holdings Corp. 2009 Equity Incentive Plan.

Note 13 Income Per Share

The Company calculates income per share under the two-class method, as certain non-vested share awards contain non-forfeitable rights to dividends. As such, these awards are considered securities that participate in the earnings of the Company. Non-vested shares are discussed further in note 10.

The Company had 44,486,467 and 52,314,909 shares outstanding (inclusive of Class A and B) as of March 31, 2014 and 2013, respectively. Certain stock options and non-vested restricted shares are potentially dilutive securities, but are not included in the calculation of diluted earnings per share because to do so would have been anti-dilutive for three months ended March 31, 2014 and 2013, respectively.

The following table illustrates the computation of basic and diluted income per share for the three months ended March 31, 2014 and 2013 (in thousands, except share and earnings per share information):

	For the three months ended	
	March 31, 2014	March 31, 2013
Distributed earnings	$2,276	$2,663
Undistributed earnings (distributions in excess of earnings)	(845)	(581)
Net income	$1,431	$2,082
Less: earnings allocated to participating securities	(5)	—
Earnings allocated to common shareholders	$1,426	$2,082
Weighted average shares outstanding for basic earnings per common share	44,819,644	52,320,622
Dilutive effect of equity awards	35,827	25,903
Dilutive effect of warrants	7,667	—
Weighted average shares outstanding for diluted earnings per common share	44,863,138	52,346,525
Basic earnings per share	$0.03	$0.04

Diluted earnings per share	$0.03	$0.04

The Company had 3,503,403 and 3,478,665 outstanding stock options to purchase common stock at weighted average exercise prices of $19.92 and $19.98 per share at March 31, 2014 and 2013, respectively, which have time-vesting criteria, and as such,

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any dilution is derived only for the time frame in which the vesting criteria had been met and where the inclusion of those stock options is dilutive. Additionally, the Company had 830,750 outstanding warrants to purchase the Company's common stock as of March 31, 2014 and 2013. The warrants have an exercise price of $20.00, which was out-of-the-money for purposes of dilution calculations during the three months ended March 31, 2013. The Company had 1,021,127 and 951,668 unvested restricted shares outstanding as of March 31, 2014 and 2013, respectively, which have performance, market and time-vesting criteria, and as such, any dilution is derived only for the time frame in which the vesting criteria had been met and where the inclusion of those restricted shares is dilutive.

Note 14 Derivatives

Risk management objective of using derivatives

The Company is exposed to certain risks arising from both its business operations and economic conditions. The Company has established policies that neither carrying value nor fair value at risk should exceed established guidelines. The Company has designed strategies to confine these risks within the established limits and identify appropriate trade-offs in the financial structure of its balance sheet. These strategies include the use of derivative financial instruments to help achieve the desired balance sheet repricing structure while meeting the desired objectives of its clients. Currently the Company employs certain interest rate swaps that are designated as fair value hedges as well as economic hedges. The Company manages a matched book with respect to its derivative instruments in order to minimize its net risk exposure resulting from such transactions.

Fair values of derivative instrument of the balance sheet

The table below presents the fair value of the Company's derivative financial instruments as well as their classification on the Consolidated Statements of Financial Condition as of March 31, 2014 and December 31, 2013 (dollars in thousands).

Information about the valuation methods used to measure fair value is provided in note 15.

		Asset Derivatives			Liability Derivatives	
		Fair Value			Fair Value	
	Balance Sheet Location	March 31, 2014	December 31, 2013	Balance Sheet Location	March 31, 2014	December 31, 2013
Derivatives designated as hedging instruments						
Interest rate products	Other assets	$1	$ 129	Other liabilities	$485	$ —
Total derivatives designated as hedging instruments		$1	$ 129		$485	$ —
Derivatives not designated as hedging instruments						
Interest rate products	Other assets	$204	$ 73	Other liabilities	$219	$ 74
Total derivatives not designated as hedging instruments		$204	$ 73		$219	$ 74

Fair value hedges of interest rate risk

Interest rate swaps designated as fair value hedges involve the receipt of variable-rate amounts from a counterparty in exchange for the Company making fixed-rate payments over the life of the agreements without the exchange of the underlying notional amount. As of March 31, 2014, the Company had four interest rate swaps with a notional amount of $30.5 million that were designated as fair value hedges of interest rate risk associated with the Company's fixed-rate

loans. The Company had one outstanding interest rate swap with a notional amount of $10.0 million that was designated as a fair value hedge as of December 31, 2013.
For derivatives designated and that qualify as fair value hedges, the gain or loss on the derivative as well as the offsetting loss or gain on the hedged item attributable to the hedged risk are recognized in earnings. The Company includes the gain or loss on the hedged items in the same line item as the offsetting loss or gain on the related derivatives. During the three months ended March 31, 2014, the Company recognized a net loss of $72.9 thousand in non-interest expense related to hedge ineffectiveness. During the three months ended March 31, 2013, the Company did not participate in fair value hedges that would result in hedge ineffectiveness.

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Non-designated hedges

Derivatives not designated as hedges are not speculative and consist of interest rate swaps with commercial banking clients that facilitate their respective risk management strategies. Those interest rate swaps are simultaneously hedged by offsetting interest rate swaps that the Company executes with a third party, such that the Company minimizes its net risk exposure resulting from such transactions. As the interest rate swaps associated with this program do not meet the strict hedge accounting requirements, changes in the fair value of both the client swaps and the offsetting swaps are recognized directly in earnings. As of March 31, 2014, the Company had four matched interest rate swap transactions with an aggregate notional amount of $9.2 million related to this program. As of December 31, 2013, the Company had three matched interest rate swap transactions with an aggregate notional amount of $7.3 million related to this program.

Effect of Derivative Instruments on the Consolidated Statement of Operations

The tables below present the effect of the Company's derivative financial instruments on the consolidated statement of operations for the three months ended March 31, 2014 and 2013 (in thousands).

Derivatives in fair value hedging relationships	Location of gain or (loss) recognized in income on derivative	Amount of gain or (loss) recognized in income on derivative		Amount of gain or (loss) recognized in income on hedged item	
		For the three months ended March 31,		For the three months ended March 31,	
		2014	2013	2014	2013
Interest rate products	Interest income	$(614)	$—	$541	$—
Total		$(614)	$—	$541	$—

Derivatives not designated as hedging instruments	Location of gain or (loss) recognized in income on derivative	Amount of gain or (loss) recognized in income on derivative	
		For the three months ended March 31,	
		2014	2013
Interest rate products	Other non-interest income	$(14)	—
Total		$(14)	—

Credit-risk-related Contingent Features

The Company has agreements with its derivative counterparties that contain a provision where if the Company defaults on any of its indebtedness for reasons other than an error or omission of an administrative or operational nature, including default where repayment of the indebtedness has not been accelerated by the lender, then the Company could also be declared in default on its derivative obligations.

The Company also has agreements with certain of its derivative counterparties that contain a provision where if the Company fails to maintain its status as a well/adequately capitalized institution, then the counterparty has the right to terminate the derivative positions and the Company would be required to settle its obligations under the agreements. As of March 31, 2014, the termination value of derivatives in a net liability position related to these agreements was $1.0 million, which includes accrued interest but excludes any adjustment for nonperformance risk. The Company has minimum collateral posting thresholds with certain of its derivative counterparties and as of March 31, 2014, the Company had posted $0.9 million in eligible collateral.

Note 15 Fair Value Measurements

The Company uses fair value measurements to record fair value adjustments to certain assets and liabilities and to disclose the fair value of its financial instruments. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. For disclosure purposes, the Company groups its financial and non-financial assets and liabilities into three different levels based on the nature of the instrument and the availability and reliability of the information that is used to determine fair value. The three levels are defined as follows:

- Level 1—Includes assets or liabilities in which the inputs to the valuation methodologies are based on unadjusted quoted prices in active markets for identical assets or liabilities.

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- Level 2—Includes assets or liabilities in which the inputs to the valuation methodologies are based on similar assets or liabilities in inactive markets, quoted prices for identical or similar assets or liabilities in inactive markets, and inputs other than quoted prices that are observable, such as interest rates, yield curves, volatilities, prepayment speeds, and other inputs obtained from observable market input.
- Level 3—Includes assets or liabilities in which the inputs to the valuation methodology are based on at least one significant assumption that is not observable in the marketplace. These valuations may rely on management’s judgment and may include internally-developed model-based valuation techniques.

Level 1 inputs are considered to be the most transparent and reliable and level 3 inputs are considered to be the least transparent and reliable. The Company assumes the use of the principal market to conduct a transaction of each particular asset or liability being measured and then considers the assumptions that market participants would use when pricing the asset or liability. Whenever possible, the Company first looks for quoted prices for identical assets or liabilities in active markets (level 1 inputs) to value each asset or liability. However, when inputs from identical assets or liabilities on active markets are not available, the Company utilizes market observable data for similar assets and liabilities. The Company maximizes the use of observable inputs and limits the use of unobservable inputs to occasions when observable inputs are not available. The need to use unobservable inputs generally results from the lack of market liquidity of the actual financial instrument or of the underlying collateral. Although, in some instances, third party price indications may be available, limited trading activity can challenge the observability of these quotations.

Changes in the valuation inputs used for measuring the fair value of financial instruments may occur due to changes in current market conditions or other factors. Such changes may necessitate a transfer of the financial instruments to another level in the hierarchy based on the new inputs used. The Company recognizes these transfers at the end of the reporting period that the transfer occurs. During the three months ended March 31, 2014 and 2013, there were no transfers of financial instruments between the hierarchy levels.

The following is a description of the valuation methodologies used for assets and liabilities measured at fair value, as well as the general classification of each instrument under the valuation hierarchy:

Fair Value of Financial Instruments Measured on a Recurring Basis

Investment securities available-for-sale—Investment securities available-for-sale are carried at fair value on a recurring basis. To the extent possible, observable quoted prices in an active market are used to determine fair value and, as such, these securities are classified as level 1. At March 31, 2014 and December 31, 2013, the Company did not hold any level 1 securities. When quoted market prices in active markets for identical assets or liabilities are not available, quoted prices of securities with similar characteristics, discounted cash flows or other pricing characteristics are used to estimate fair values and the securities are then classified as level 2. At March 31, 2014 and December 31, 2013, the Company’s level 2 securities included asset backed securities, mortgage-backed securities comprised of residential mortgage pass-through securities, and other residential mortgage-backed securities. All other investment securities are classified as level 3.

Derivatives—The Company's derivative instruments are limited to interest rate swaps that may be accounted for as fair value hedges or non-designated hedges. The fair values of the swaps incorporate credit valuation adjustments in order to appropriately reflect nonperformance risk in the fair value measurements. The credit valuation adjustment is the dollar amount of the fair value adjustment related to credit risk and utilizes a probability weighted calculation to quantify the potential loss over the life of the trade. The credit valuation adjustments are calculated by determining the total expected exposure of the derivatives (which incorporates both the current and potential future exposure) and then applying the respective counterparties’ credit spreads to the exposure offset by marketable collateral posted, if any. Certain derrivative transactions are executed with counterparties who are large financial institutions ("dealers"). International Swaps and Derivative Association Master Agreements ("ISDA") and Credit Support Annexes ("CSA") are employed for all contracts with dealers. These contracts contain bilateral collateral arrangements. The fair value inputs of these financial instruments are determined using discounted cash flow analysis through the use of third-party models whose significant inputs are readily observable market parameters, primarily yield curves, with appropriate adjustments for liquidity and credit risk, and are classified as level 2.

Warrant liability—The Company measures the fair value of the warrant liability on a recurring basis using a Black-Scholes option pricing model. The Company's shares became publicly traded on September 20, 2012 and prior to that, had limited private trading; therefore, expected volatility was estimated using a time-based weighted migration of the Company's own stock price volatility coupled with the median historical volatility, for a period commensurate with the expected term of the warrants, of those of 9 comparable companies with publicly traded shares, and is deemed a significant unobservable input to the valuation model.

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Clawback liability—The Company periodically measures the net present value of expected future cash payments to be made by the Company to the FDIC that must be made within 45 days of the conclusion of the loss sharing. The expected cash flows are calculated in accordance with the loss sharing agreements and are based primarily on the expected losses on the covered assets, which involve significant inputs that are not market observable.

The tables below present the financial instruments measured at fair value on a recurring basis as of March 31, 2014 and December 31, 2013