CULLEN/FROST BANKERS, INC.
Form 10-K
February 06, 2014
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K
ý Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the fiscal year ended: December 31, 2013
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: 001-13221
CULLEN/FROST BANKERS, INC.
(Exact name of registrant as specified in its charter)

Texas	74-1751768
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
100 W. Houston Street, San Antonio, Texas	78205
(Address of principal executive offices)	(Zip code)

(210) 220-4011
(Registrant's telephone number, including area code)
Securities registered pursuant to Section 12(b) of the Act:

Common Stock, $.01 Par Value,	The New York Stock Exchange, Inc.
(Title of each class)	(Name of each exchange on which registered)

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 ý 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 ý
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 Website, 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ý
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	ý	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 Act.) Yes ¨ No ý
As of June 30, 2013, the last business day of the registrant's most recently completed second fiscal quarter, the aggregate market value of the shares of common stock held by non-affiliates, based upon the closing price per share of the registrant's common stock as reported on The New York Stock Exchange, Inc., was approximately $3.9 billion.
As of February 5, 2014, there were 60,757,118 shares of the registrant's common stock, $.01 par value, outstanding.
DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the 2014 Annual Meeting of Shareholders of Cullen/Frost Bankers, Inc. to be held on April 24, 2014 are incorporated by reference in this Form 10-K in response to Part III, Items 10, 11, 12, 13 and 14.

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PART I

ITEM 1. BUSINESS

The disclosures set forth in this item are qualified by Item 1A. Risk Factors and the section captioned "Forward-Looking Statements and Factors that Could Affect Future Results" in Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations of this report and other cautionary statements set forth elsewhere in this report.

The Corporation

Cullen/Frost Bankers, Inc. ("Cullen/Frost"), a Texas business corporation incorporated in 1977, is a financial holding company and a bank holding company headquartered in San Antonio, Texas that provides, through its subsidiaries (collectively referred to as the "Corporation"), a broad array of products and services throughout numerous Texas markets. The Corporation offers commercial and consumer banking services, as well as trust and investment management, mutual funds, investment banking, insurance, brokerage, leasing, asset-based lending, treasury management and item processing services. At December 31, 2013, Cullen/Frost had consolidated total assets of $24.3 billion and was one of the largest independent bank holding companies headquartered in the State of Texas.

The Corporation's philosophy is to grow and prosper, building long-term relationships based on top quality service, high ethical standards, and safe, sound assets. The Corporation operates as a locally oriented, community-based financial services organization, augmented by experienced, centralized support in select critical areas. The Corporation's local market orientation is reflected in its regional management and regional advisory boards, which are comprised of local business persons, professionals and other community representatives that assist the Corporation's regional management in responding to local banking needs. Despite this local market, community-based focus, the Corporation offers many of the products available at much larger money-center financial institutions.

The Corporation serves a wide variety of industries including, among others, energy, manufacturing, services, construction, retail, telecommunications, healthcare, military and transportation. The Corporation's customer base is similarly diverse. While the Corporation's loan portfolio has a significant concentration of energy-related loans totaling approximately 11.7% of total loans, the Corporation is not dependent upon any single industry or customer.

The Corporation's operating objectives include expansion, diversification within its markets, growth of its fee-based income, and growth internally and through acquisitions of financial institutions, branches and financial services businesses. The Corporation generally seeks merger or acquisition partners that are culturally similar and have experienced management and possess either significant market presence or have potential for improved profitability through financial management, economies of scale and expanded services. The Corporation regularly evaluates merger and acquisition opportunities and conducts due diligence activities related to possible transactions with other financial institutions and financial services companies. As a result, merger or acquisition discussions and, in some cases, negotiations may take place and future mergers or acquisitions involving cash, debt or equity securities may occur. Acquisitions typically involve the payment of a premium over book and market values, and, therefore, some dilution of the Corporation's tangible book value and net income per common share may occur in connection with any future transaction. During 2013, the Corporation announced an agreement to acquire WNB Bancshares, Inc., a bank holding company located in Odessa, Texas ("WNB"). The merger, which is subject to regulatory approval, is expected to be consummated in the second quarter of 2014. See Note 21 - Pending Acquisition in the accompanying notes to consolidated financial statements included elsewhere in this report. Also during 2013, the Corporation acquired a Houston-based insurance agency specializing in commercial lines insurance products. During 2012, the Corporation acquired a Houston-based human resources consulting firm that specializes in compensation, benefits and outsourcing services. During 2011, the Corporation acquired an insurance agency in the San Antonio market area. None of these acquisitions had a significant impact on the Corporation's financial statements during their respective reporting periods.

The Corporation's ability to engage in certain merger or acquisition transactions, whether or not any regulatory approval is required, will be dependent upon the Corporation's bank regulators' views at the time as to the capital levels, quality of management and overall condition of the Corporation and their assessment of a variety of other factors. Certain merger or acquisition transactions, including those involving the acquisition of a depository institution or the assumption of the deposits of any depository institution, require formal approval from various bank regulatory authorities, which will be subject to a variety of factors and considerations. See the section captioned “Supervision and Regulation” included elsewhere in this item for further discussion of these matters.

Although Cullen/Frost is a corporate entity, legally separate and distinct from its affiliates, bank holding companies such as Cullen/Frost are required to act as a source of financial strength for their subsidiary banks. The principal source of Cullen/Frost’s income is dividends from its subsidiaries. There are certain regulatory restrictions on the extent to which these subsidiaries can pay dividends or otherwise supply funds to Cullen/Frost. See the section captioned “Supervision and Regulation” included elsewhere in this item for further discussion of these matters.

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Cullen/Frost's executive offices are located at 100 W. Houston Street, San Antonio, Texas 78205, and its telephone number is (210) 220-4011.

Subsidiaries of Cullen/Frost

Cullen/Frost Capital Trust II

Cullen/Frost Capital Trust II ("Trust II") is a Delaware statutory business trust formed in 2004 for the purpose of issuing $120.0 million in trust preferred securities and lending the proceeds to Cullen/Frost. Cullen/Frost guarantees, on a limited basis, payments of distributions on the trust preferred securities and payments on redemption of the trust preferred securities.

Trust II is a variable interest entity for which the Corporation is not the primary beneficiary. As such, the accounts of Trust II are not included in the Corporation's consolidated financial statements. See the Corporation's accounting policy related to consolidation in Note 1 - Summary of Significant Accounting Policies in the notes to consolidated financial statements included in Item 8. Financial Statements and Supplementary Data, which is located elsewhere in this report.

Although the accounts of Trust II are not included in the Corporation's consolidated financial statements, the $120.0 million in trust preferred securities issued by Trust II are currently included in the Tier 1 capital of Cullen/Frost for regulatory capital purposes. See the section captioned "Supervision and Regulation - Capital Requirements" for a discussion of the regulatory capital treatment of the Corporation's trust preferred securities, including the recently adopted revisions to that treatment that will require the Corporation to phase-out the inclusion of trust preferred securities in Tier 1 capital.

Frost Bank

Frost Bank, the principal operating subsidiary and sole banking subsidiary of Cullen/Frost, is primarily engaged in the business of commercial and consumer banking through approximately 114 financial centers across Texas in the Austin, Corpus Christi, Dallas, Fort Worth, Houston, Rio Grande Valley and San Antonio regions. Frost Bank expects to enter the Midland/Odessa region in 2014 after the closing of the aforementioned acquisition of WNB. Frost Bank also operates over 1,100 automated-teller machines ("ATMs") throughout the State of Texas, including over 630 ATMs operated in connection with a branding arrangement to be the exclusive cash-machine provider for CST Brands, Inc. Corner Stores in Texas. Frost Bank was chartered as a national banking association in 1899, but its origin can be traced to a mercantile partnership organized in 1868. At December 31, 2013, Frost Bank had consolidated total assets of $24.4 billion and total deposits of $20.8 billion and was one of the largest commercial banks headquartered in the State of Texas.

Significant services offered by Frost Bank include:

- Commercial Banking. Frost Bank provides commercial banking services to corporations and other business clients. Loans are made for a wide variety of general corporate purposes, including financing for industrial and commercial properties and to a lesser extent, financing for interim construction related to industrial and commercial properties, financing for equipment, inventories and accounts receivable, and acquisition financing. The Corporation also originates commercial leases and offers treasury management services.
- Consumer Services. Frost Bank provides a full range of consumer banking services, including checking accounts, savings programs, ATMs, overdraft facilities, installment and real estate loans, home equity loans and lines of credit, drive-in and night deposit services, safe deposit facilities and brokerage services.
- International Banking. Frost Bank provides international banking services to customers residing in or dealing with businesses located in Mexico. These services consist of accepting deposits (generally only in U.S. dollars), making loans (in U.S. dollars only), issuing letters of credit, handling foreign collections, transmitting funds, and to a limited extent, dealing in foreign exchange.
- Correspondent Banking. Frost Bank acts as correspondent for approximately 333 financial institutions, which are primarily banks in Texas. These banks maintain deposits with Frost Bank, which offers them a full range of services including check clearing, transfer of funds, fixed income security services, and securities custody and clearance services.
- Trust Services. Frost Bank provides a wide range of trust, investment, agency and custodial services for individual and corporate clients. These services include the administration of estates and personal trusts, as well as the

management of investment accounts for individuals, employee benefit plans and charitable foundations. At December 31, 2013, the estimated fair value of trust assets was $28.4 billion, including managed assets of $11.9 billion and custody assets of $16.5 billion.

- Capital Markets - Fixed-Income Services. Frost Bank’s Capital Markets Division supports the transaction needs of fixed-income institutional investors. Services include sales and trading, new issue underwriting, money market trading, and securities safekeeping and clearance.

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- Global Trade Services. Frost Bank's Global Trade Services Division supports international business activities including foreign exchange, international letters of credit and export-import financing, among other things.

Frost Insurance Agency, Inc.

Frost Insurance Agency, Inc. is a wholly owned subsidiary of Frost Bank that provides insurance brokerage services to individuals and businesses covering corporate and personal property and casualty insurance products, as well as group health and life insurance products and consulting services.

Frost Brokerage Services, Inc.

Frost Brokerage Services, Inc. (“FBS”) is a wholly owned subsidiary of Frost Bank that provides brokerage services and performs other transactions or operations related to the sale and purchase of securities of all types. FBS is registered as a fully disclosed introducing broker-dealer under the Securities Exchange Act of 1934 and, as such, does not hold any customer accounts.

Frost Investment Advisors, LLC

Frost Investment Advisors is a registered investment advisor entity and a wholly owned subsidiary of Frost Bank that provides investors access to various Frost-managed mutual funds.

Tri–Frost Corporation

Tri-Frost Corporation is a wholly-owned subsidiary of Frost Bank that primarily holds securities for investment purposes and the receipt of cash flows related to principal and interest on the securities until such time that the securities mature.

Frost Securities, Inc.

Frost Securities, Inc. is a wholly owned subsidiary of Cullen/Frost that provides advisory and private equity services to middle market companies in Texas.

Main Plaza Corporation

Main Plaza Corporation is a wholly owned subsidiary of Cullen/Frost that occasionally makes loans to qualified borrowers. Loans are funded with current cash or borrowings against internal credit lines.

Other Subsidiaries

Cullen/Frost has various other subsidiaries that are not significant to the consolidated entity.

Operating Segments

Cullen/Frost’s operations are managed along two reportable operating segments consisting of Banking and Frost Wealth Advisors. See the sections captioned “Results of Segment Operations” in Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations and Note 18 - Operating Segments in the notes to consolidated financial statements included in Item 8. Financial Statements and Supplementary Data, which are located elsewhere in this report.

Competition

There is significant competition among commercial banks in the Corporation’s market areas. In addition, the Corporation also competes with other providers of financial services, such as savings and loan associations, credit unions, consumer finance companies, securities firms, insurance companies, insurance agencies, commercial finance and leasing companies, full service brokerage firms and discount brokerage firms. Some of the Corporation’s competitors have greater resources and, as such, may have higher lending limits and may offer other services that are not provided by the Corporation. The Corporation generally competes on the basis of customer service and responsiveness to customer needs, available loan and deposit products, the rates of interest charged on loans, the rates of interest paid for funds, and the availability and pricing of trust, brokerage and insurance services.

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Supervision and Regulation

Cullen/Frost, Frost Bank and many of its non-banking subsidiaries are subject to extensive regulation under federal and state laws. The regulatory framework is intended primarily for the protection of depositors, federal deposit insurance funds and the banking system as a whole and not for the protection of shareholders and creditors. Significant elements of the laws and regulations applicable to Cullen/Frost and its subsidiaries are described below. The description is qualified in its entirety by reference to the full text of the statutes, regulations and policies that are described. Also, such statutes, regulations and policies are continually under review by Congress and state legislatures and federal and state regulatory agencies. A change in statutes, regulations or regulatory policies applicable to Cullen/Frost and its subsidiaries could have a material effect on the business, financial condition and results of operations of the Corporation.

Regulatory Reforms

The Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act" or "Dodd-Frank"), which was enacted in July 2010, significantly restructures the financial regulatory regime in the United States. Although the Dodd-Frank Act's provisions that have received the most public attention generally have been those applying to or more likely to affect larger institutions such as bank holding companies with total consolidated assets of $50 billion or more, it contains numerous other provisions that affect all bank holding companies and banks, including the Corporation and Frost Bank, some of which are described in more detail below.

Many of the Dodd-Frank Act's provisions are subject to final rulemaking by the U.S. financial regulatory agencies, and the implications of the Dodd-Frank Act for the Corporation's businesses will depend to a large extent on how such rules are adopted and implemented by the primary U.S. financial regulatory agencies. The Corporation continues to analyze the impact of rules adopted under Dodd-Frank, on the Corporation's businesses. However, the full impact will not be known until the rules, and other regulatory initiatives that overlap with the rules, are finalized and their combined impacts can be understood.

Regulatory Agencies

Cullen/Frost is a legal entity separate and distinct from Frost Bank and its other subsidiaries. As a financial holding company and a bank holding company, Cullen/Frost is regulated under the Bank Holding Company Act of 1956, as amended ("BHC Act"), and its subsidiaries are subject to inspection, examination and supervision by the Federal Reserve Board. The BHC Act provides generally for "umbrella" regulation of financial holding companies such as Cullen/Frost by the Federal Reserve Board, and for functional regulation of banking activities by bank regulators, securities activities by securities regulators, and insurance activities by insurance regulators. Cullen/Frost is also under the jurisdiction of the Securities and Exchange Commission ("SEC") and is subject to the disclosure and regulatory requirements of the Securities Act of 1933, as amended, and the Securities Exchange Act of 1934, as amended, as administered by the SEC. Cullen/Frost's common stock is listed on the New York Stock Exchange ("NYSE") under the trading symbol "CFR," and is subject to the rules of the NYSE for listed companies.

Prior to June 22, 2012, Frost Bank was organized as a national banking association under the National Bank Act and was subject to regulation and examination by the Office of the Comptroller of the Currency ("OCC"). On June 22, 2012, Frost Bank became a Texas state chartered bank and a member of the Federal Reserve System. Accordingly, the Texas Department of Banking and the Federal Reserve are now the primary regulators of Frost Bank, and Frost Bank is no longer regulated by the OCC. Deposits at Frost Bank continue to be insured by the Federal Deposit Insurance Corporation ("FDIC") up to applicable limits.

Many of the Corporation's non-bank subsidiaries also are subject to regulation by the Federal Reserve Board and other federal and state agencies. Frost Securities, Inc. and Frost Brokerage Services, Inc. are regulated by the SEC, the Financial Industry Regulatory Authority ("FINRA") and state securities regulators. Frost Investment Advisors, LLC is subject to the disclosure and regulatory requirements of the Investment Advisors Act of 1940, as administered by the SEC. The Corporation's insurance subsidiary is subject to regulation by applicable state insurance regulatory agencies. Other non-bank subsidiaries are subject to both federal and state laws and regulations.

Bank Holding Company Activities

In general, the BHC Act limits the business of bank holding companies to banking, managing or controlling banks and other activities that the Federal Reserve Board has determined to be so closely related to banking as to be a proper incident thereto. In addition, bank holding companies that qualify and elect to be financial holding companies may engage in any activity, or acquire and retain the shares of a company engaged in any activity, that is either (i) financial in nature or incidental to such financial activity (as determined by the Federal Reserve Board in consultation with the Secretary of the Treasury) or (ii) 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 (as solely determined by the Federal Reserve Board), without prior approval of the Federal Reserve Board. Activities that are financial in nature include securities underwriting and dealing, insurance underwriting and making merchant banking investments.

To maintain financial holding company status, a financial holding company and all of its depository institution subsidiaries must be “well capitalized” and “well managed.” A depository institution subsidiary is considered to be “well capitalized” if it satisfies the requirements for this status discussed in the section captioned “Capital Adequacy and Prompt Corrective Action,” included elsewhere in this item. A depository institution subsidiary is considered “well managed” if it received a composite rating and management rating of at least “satisfactory” in its most recent examination. A financial holding company’s status will also depend upon it maintaining its status as “well capitalized” and “well managed’ under applicable Federal Reserve Board regulations. If a financial holding company ceases to meet these capital and management requirements, the Federal Reserve Board’s regulations provide that the financial holding company must enter into an agreement with the Federal Reserve Board to comply with all applicable capital and management requirements. Until the financial holding company returns to compliance, the Federal Reserve Board may impose limitations or conditions on the conduct of 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 Board. If the company does not return to compliance within 180 days, the Federal Reserve Board may require divestiture of the holding company’s depository institutions. Bank holding companies and banks must also be both well capitalized and well managed in order to acquire banks located outside their home state.

In order for a financial holding company to commence any new activity permitted by the BHC Act or to acquire a company engaged in any new activity permitted by the BHC Act, each insured depository institution subsidiary of the financial holding company must have received a rating of at least “satisfactory” in its most recent examination under the Community Reinvestment Act. See the section captioned “Community Reinvestment Act” included elsewhere in this item.

The Federal Reserve Board has the power to order any bank holding company or its subsidiaries to terminate any activity or to terminate its ownership or control of any subsidiary when the Federal Reserve Board has reasonable grounds to believe that continuation of such activity or such ownership or control constitutes a serious risk to the financial soundness, safety or stability of any bank subsidiary of the bank holding company.

The Dodd-Frank Act amends the BHC Act to require the federal financial regulatory agencies to adopt rules that prohibit banks and their affiliates from engaging in proprietary trading and investing in and sponsoring certain unregistered investment companies (defined as hedge funds and private equity funds). The statutory provision is commonly called the “Volcker Rule”. The Federal Reserve adopted final rules implementing the Volcker Rule on December 10, 2013. The Volcker Rule became effective on July 21, 2012 and the final rules are effective April 1, 2014, but the Federal Reserve issued an order extending the period during which institutions have to conform their activities and investments to the requirements of the Volcker Rule to July 21, 2015. Although the Corporation is continuing to evaluate the impact of the Volcker Rule and the final rules adopted thereunder, the Corporation does not currently anticipate that the Volcker Rule will have a material effect on the operations of Cullen/Frost and its subsidiaries, as the Corporation does not engage in the businesses prohibited by the Volcker Rule. The Corporation may incur costs to adopt additional policies and systems to ensure compliance with the Volcker Rule, but any such costs are not expected to be material.

The BHC Act, the Bank Merger Act, the Texas Banking Code and other federal and state statutes regulate acquisitions of commercial banks. The BHC Act requires the prior approval of the Federal Reserve Board for the direct or indirect acquisition by a bank holding company of more than 5.0% of the voting shares of a commercial bank or its parent holding company. Under the Bank Merger Act, the prior approval of the Federal Reserve Board or other appropriate bank regulatory authority is required for a member bank to merge with another bank or purchase the assets or assume the deposits of another bank. In reviewing applications seeking approval of merger and acquisition transactions, the bank regulatory authorities will consider, among other things, the competitive effect and public benefits of the transactions, the capital position of the combined organization, the risks to the stability of the U.S. banking or financial system, the applicant’s performance record under the Community Reinvestment Act (see the section captioned “Community Reinvestment Act” included elsewhere in this item) and its compliance with fair housing and other consumer protection laws and the effectiveness of the subject organizations in combating money laundering activities.

Dividends

The principal source of Cullen/Frost's liquidity is dividends from Frost Bank. The prior approval of the Federal Reserve is required if the total of all dividends declared by a state-chartered member bank in any calendar year would exceed the sum of the bank's net profits for that year and its retained net profits for the preceding two calendar years, less any required transfers to surplus or to fund the retirement of preferred stock. Federal law also prohibits a state-chartered, member bank from paying dividends that would be greater than the bank's undivided profits. Frost Bank is also subject to limitations under Texas state law regarding the level of dividends that may be paid. Under the foregoing dividend restrictions, and while maintaining its "well capitalized" status, Frost Bank could pay aggregate dividends of approximately $294.7 million to Cullen/Frost, without obtaining affirmative governmental approvals, at December 31, 2013. This amount is not necessarily indicative of amounts that may be paid or available to be paid in future periods.

In addition, Cullen/Frost and Frost Bank are subject to other regulatory policies and requirements relating to the payment of dividends, including requirements to maintain adequate capital above regulatory minimums. The appropriate federal regulatory authority is authorized to determine under certain circumstances relating to the financial condition of a bank holding company or a bank that the payment of dividends would be an unsafe or unsound practice and to prohibit payment thereof. The appropriate federal regulatory authorities have stated that paying dividends that deplete a bank's capital base to an inadequate level would be an unsafe and unsound banking practice and that banking organizations should generally pay dividends only out of current operating earnings. In addition, in the current financial and economic environment, the Federal Reserve Board has indicated that bank holding companies should carefully review their dividend policy and has discouraged payment ratios that are at maximum allowable levels unless both asset quality and capital are very strong.

In October 2012, as required by Dodd-Frank, the Federal Reserve Board published final rules regarding company-run stress testing. The rules require institutions, such as Cullen/Frost and Frost Bank, with average total consolidated assets greater than $10 billion to conduct an annual company-run stress test of capital, consolidated earnings and losses under one base and at least two stress scenarios provided by the agencies. Implementation of the rules for covered institutions with total consolidated assets between $10 billion and $50 billion began in 2013. The company-run stress tests are conducted using data as of September 30th and scenarios released by the agencies. Stress test results must be reported to the agencies by the following March 31st. Public disclosure of summary stress test results under the severely adverse scenario will begin in June 2015 for stress tests commencing in 2014. It is anticipated that the Corporation's capital ratios reflected in the stress test calculations will be an important factor considered by the Federal Reserve Board in evaluating the capital adequacy of Cullen/Frost and Frost Bank and whether the appropriateness of any proposed payments of dividends or stock repurchases may be an unsafe or unsound practice.

Transactions with Affiliates

Transactions between Frost Bank, on the one hand, and Cullen/Frost and its other subsidiaries, on the other hand, are regulated by the Federal Reserve Board. These regulations limit the types and amounts of covered transactions engaged in by Frost Bank and generally require those transactions to be on an arm's-length basis. "Covered transactions" are defined by statute to include a loan or extension of credit, as well as a purchase of securities issued by an affiliate, a purchase of assets (unless otherwise exempted by the Federal Reserve Board) from the affiliate, certain derivative transactions that create a credit exposure to an affiliate, the acceptance of securities issued by the affiliate as collateral for a loan, and the issuance of a guarantee, acceptance or letter of credit on behalf of an affiliate. In general, these regulations require that any such transaction by Frost Bank (or its subsidiaries) with an affiliate must be secured by designated amounts of specified collateral and must be limited to certain thresholds on an individual and aggregate basis.

Source of Strength Doctrine

Federal Reserve Board policy and federal law require bank holding companies to act as a source of financial and managerial strength to their subsidiary banks. Under this requirement, Cullen/Frost is expected to commit resources to support Frost Bank, including at times when Cullen/Frost may not be in a financial position to provide such resources. Any capital loans by a bank holding company to any of its subsidiary banks are subordinate in right of payment to depositors and to certain other indebtedness of such subsidiary banks. In the event of a bank holding company's bankruptcy, any commitment by the bank holding company to a federal bank regulatory agency to maintain the capital of a subsidiary bank will be assumed by the bankruptcy trustee and entitled to priority of payment.

Capital Requirements

Cullen/Frost and Frost Bank are subject to the regulatory capital requirements administered by the Federal Reserve Board, and, for Frost Bank, the FDIC. The federal regulatory authorities' current risk-based capital guidelines are based upon the 1988 capital accord ("Basel I") of the Basel Committee on Banking Supervision (the "Basel Committee"). The Basel Committee is a committee of central banks and bank supervisors/regulators from the major industrialized countries that develops broad policy guidelines for use by each country's supervisors in determining the supervisory policies they apply. The requirements are intended to ensure that banking organizations have adequate capital given the risk levels of assets and off-balance sheet financial instruments. Under the requirements, banking organizations are required to maintain minimum ratios for Tier 1 capital and total capital to risk-weighted assets (including certain off-balance sheet items, such as letters of credit). For purposes of calculating the ratios, a banking organization's assets and some of its specified off-balance sheet commitments and obligations are assigned to various risk categories. A depository institution’s or holding company’s capital, in turn, is classified in one of two tiers, depending on type:

- Core Capital (Tier 1). Tier 1 capital includes common equity, retained earnings, qualifying non-cumulative perpetual preferred stock, minority interests in equity accounts of consolidated subsidiaries (and, under existing standards, a limited amount of qualifying trust preferred securities and qualifying cumulative perpetual preferred stock at the holding company level), less goodwill, most intangible assets and certain other assets.
- Supplementary Capital (Tier 2). Tier 2 capital includes, among other things, perpetual preferred stock and trust preferred securities not meeting the Tier 1 definition, qualifying mandatory convertible debt securities, qualifying subordinated debt, and allowances for loan and lease losses, subject to limitations.

Cullen/Frost, like other bank holding companies, currently is required to maintain Tier 1 capital and “total capital” (the sum of Tier 1 and Tier 2 capital) equal to at least 4.0% and 8.0%, respectively, of its total risk-weighted assets (including various off-balance-sheet items, such as letters of credit). Frost Bank, like other depository institutions, is required to maintain similar capital levels under capital adequacy guidelines. In addition, for a depository institution to be considered “well capitalized” under the regulatory framework for prompt corrective action, its Tier 1 and total capital ratios must be at least 6.0% and 10.0% on a risk-adjusted basis, respectively.

Bank holding companies and banks are also currently required to comply with minimum leverage ratio requirements. The leverage ratio is the ratio of a banking organization’s Tier 1 capital to its total adjusted quarterly average assets (as defined for regulatory purposes). The requirements necessitate a minimum leverage ratio of 3.0% for bank holding companies and member banks that either have the highest supervisory rating or have implemented the appropriate federal regulatory authority’s risk-adjusted measure for market risk. All other bank holding companies and member banks are required to maintain a minimum leverage ratio of 4.0%, unless a different minimum is specified by an appropriate regulatory authority. In addition, for a depository institution to be considered “well capitalized” under the regulatory framework for prompt corrective action, its leverage ratio must be at least 5.0%. The Federal Reserve Board has not advised Cullen/Frost or Frost Bank, of any specific minimum leverage ratio applicable to either entity.

Basel III Capital Rules. In July 2013, Cullen/Frost’s and Frost Bank’s primary federal regulator, the Federal Reserve, published the Basel III Capital Rules establishing a new comprehensive capital framework for U.S. banking organizations. The rules implement the Basel Committee’s December 2010 framework known as “Basel III” for strengthening international capital standards as well as certain provisions of the Dodd-Frank Act. The Basel III Capital Rules substantially revise the risk-based capital requirements applicable to bank holding companies and depository institutions, including Cullen/Frost and Frost Bank, compared to the current U.S. risk-based capital rules. The Basel III Capital Rules define the components of capital and address other issues affecting the numerator in banking institutions’ regulatory capital ratios. The Basel III Capital Rules also address risk weights and other issues affecting the denominator in banking institutions’ regulatory capital ratios and replace the existing risk-weighting approach, which was derived from the Basel I capital accords of the Basel Committee, with a more risk-sensitive approach based, in part, on the standardized approach in the Basel Committee’s 2004 “Basel II” capital accords. The Basel III Capital Rules also implement the requirements of Section 939A of the Dodd-Frank Act to remove references to credit ratings from the federal banking agencies’ rules. The Basel III Capital Rules are effective for Cullen/Frost and Frost Bank on January 1, 2015 (subject to a phase-in period).

The Basel III Capital Rules, among other things, (i) introduce a new capital measure called “Common Equity Tier 1” (“CET1”), (ii) specify that Tier 1 capital consists of CET1 and “Additional Tier 1 capital” instruments meeting specified requirements, (iii) define CET1 narrowly by requiring that most deductions/adjustments to regulatory capital measures be made to CET1 and not to the other components of capital and (iv) expand the scope of the deductions/adjustments as compared to existing regulations.

When fully phased in on January 1, 2019, the Basel III Capital Rules will require Cullen/Frost and Frost Bank to maintain (i) a minimum ratio of CET1 to risk-weighted assets of at least 4.5%, plus a 2.5% “capital conservation buffer” (which is added to the 4.5% CET1 ratio as that buffer is phased in, effectively resulting in a minimum ratio of CET1 to risk-weighted assets of at least 7% upon full implementation), (ii) a minimum ratio of Tier 1 capital to risk-weighted assets of at least 6.0%, plus the capital conservation buffer (which is added to the 6.0% Tier 1 capital ratio as that buffer is phased in, effectively resulting in a minimum Tier 1 capital ratio of 8.5% upon full implementation), (iii) a minimum ratio of Total capital (that is, Tier 1 plus Tier 2) to risk-weighted assets of at least 8.0%, plus the capital conservation buffer (which is added to the 8.0% total capital ratio as that buffer is phased in, effectively resulting in a minimum total capital ratio of 10.5% upon full implementation) and (iv) a minimum leverage ratio of 4%, calculated as the ratio of Tier 1 capital to average assets (as compared to a current minimum leverage ratio of 3% for banking organizations that either have the highest supervisory rating or have implemented the appropriate federal regulatory authority’s risk-adjusted measure for market risk).

The Basel III Capital Rules also provides for a “countercyclical capital buffer” that is applicable to only certain covered institutions and is not expected to have any current applicability to Cullen/Frost or Frost Bank.

The aforementioned capital conservation buffer is designed to absorb losses during periods of economic stress. Banking institutions with a ratio of CET1 to risk-weighted assets above the minimum but below the conservation buffer (or below the combined capital conservation buffer and countercyclical capital buffer, when the latter is applied) will face constraints on dividends, equity repurchases and compensation based on the amount of the shortfall.

Under the Basel III Capital Rules, the initial minimum capital ratios as of January 1, 2015 will be as follows:

- 4.5% CET1 to risk-weighted assets.
- 6.0% Tier 1 capital to risk-weighted assets.
- 8.0% Total capital to risk-weighted assets.

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The Basel III Capital Rules provide for a number of deductions from and adjustments to CET1. These include, for example, the requirement that mortgage servicing rights, deferred tax assets arising from temporary differences that could not be realized through net operating loss carrybacks and significant investments in non-consolidated financial entities be deducted from CET1 to the extent that any one such category exceeds 10% of CET1 or all such categories in the aggregate exceed 15% of CET1. Under current capital standards, the effects of accumulated other comprehensive income items included in capital are excluded for the purposes of determining regulatory capital ratios. Under the Basel III Capital Rules, the effects of certain accumulated other comprehensive items are not excluded; however, non-advanced approaches banking organizations, including Cullen/Frost and Frost Bank, may make a one-time permanent election to continue to exclude these items. Cullen/Frost and Frost Bank expect to make this election in order to avoid significant variations in the level of capital depending upon the impact of interest rate fluctuations on the fair value of the Corporation's available-for-sale securities portfolio. The Basel III Capital Rules also preclude certain hybrid securities, such as trust preferred securities, as Tier 1 capital of bank holding companies, subject to phase-out. As a result, beginning in 2015, only 25% of the Corporation's trust preferred securities will be included in Tier 1 capital and in 2016, none of the Corporation's trust preferred securities will be included in Tier 1 capital. Trust preferred securities no longer included in the Corporation's Tier 1 capital may nonetheless be included as a component of Tier 2 capital on a permanent basis without phase-out.

Implementation of the deductions and other adjustments to CET1 will begin on January 1, 2015 and will be phased-in over a four-year period (beginning at 40% on January 1, 2015 and an additional 20% per year thereafter). The implementation of the capital conservation buffer will begin on January 1, 2016 at the 0.625% level and be phased in over a four-year period (increasing by that amount on each subsequent January 1, until it reaches 2.5% on January 1, 2019).

With respect to Frost Bank, the Basel III Capital Rules also revise the "prompt corrective action" regulations pursuant to Section 38 of the Federal Deposit Insurance Act, as discussed below under "Prompt Corrective Action."

The Basel III Capital Rules prescribe a standardized approach for risk weightings that expand the risk-weighting categories from the current four Basel I-derived categories (0%, 20%, 50% and 100%) to a much larger and more risk-sensitive number of categories, depending on the nature of the assets, generally ranging from 0% for U.S. government and agency securities, to 600% for certain equity exposures, and resulting in higher risk weights for a variety of asset categories. Specifics changes to current rules impacting the Corporation's determination of risk-weighted assets include, among other things:

- Applying a 150% risk weight instead of a 100% risk weight for certain high volatility commercial real estate acquisition, development and construction loans.
- Assigning a 150% risk weight to exposures (other than residential mortgage exposures) that are 90 days past due.
- Providing for a 20% credit conversion factor for the unused portion of a commitment with an original maturity of one year or less that is not unconditionally cancellable (currently set at 0%).
- Providing for a risk weight, generally not less than 20% with certain exceptions, for securities lending transactions based on the risk weight category of the underlying collateral securing the transaction.
- Providing for a 100% risk weight for claims on securities firms.
- Eliminating the current 50% cap on the risk weight for OTC derivatives.

In addition, the Basel III Capital Rules provide more advantageous risk weights for derivatives and repurchase-style transactions cleared through a qualifying central counterparty and increase the scope of eligible guarantors and eligible collateral for purposes of credit risk mitigation.

Management believes that, as of December 31, 2013, Cullen/Frost and Frost Bank would meet all capital adequacy requirements under the Basel III Capital Rules on a fully phased-in basis as if such requirements were currently in effect.

Liquidity Requirements

Historically, the regulation and monitoring of bank and bank holding company liquidity has been addressed as a supervisory matter, without required formulaic measures. The Basel III liquidity framework requires banks and bank holding companies to measure their liquidity against specific liquidity tests that, although similar in some respects to liquidity measures historically applied by banks and regulators for management and supervisory purposes, going forward would be required by regulation. One test, referred to as the liquidity coverage ratio (“LCR”), is designed to ensure that the banking entity maintains an adequate level of unencumbered high-quality liquid assets equal to the entity’s expected net cash outflow for a 30-day time horizon (or, if greater, 25% of its expected total cash outflow) under an acute liquidity stress scenario. The other test, referred to as the net stable funding ratio (“NSFR”), is designed to promote more medium- and long-term funding of the assets and activities of banking entities over a one-year time horizon. These requirements will incent banking entities to increase their holdings of U.S. Treasury securities and other sovereign debt as a component of assets and increase the use of long-term debt as a funding source. In October 2013, the federal banking agencies proposed rules implementing the LCR for advanced approaches banking organizations and a modified version of the LCR for bank holding companies with at least $50 billion in total consolidated assets that are not advanced approach banking organizations, neither of which would apply to Cullen/Frost or Frost Bank. The federal banking agencies have not yet proposed rules to implement the NSFR.

Prompt Corrective Action

The Federal Deposit Insurance Act, as amended (“FDIA”), requires among other things, the federal banking agencies to take “prompt corrective action” in respect of depository institutions that do not meet minimum capital requirements. The FDIA includes the following five capital tiers: “well capitalized,” “adequately capitalized,” “undercapitalized,” “significantly undercapitalized” and “critically undercapitalized.” A depository institution’s capital tier will depend upon how its capital levels compare with various relevant capital measures and certain other factors, as established by regulation. The relevant capital measures are the total capital ratio, the Tier 1 capital ratio and the leverage ratio.

A bank will be (i) “well capitalized” if the institution has a total risk-based capital ratio of 10.0% or greater, a Tier 1 risk-based capital ratio of 6.0% or greater, and a leverage ratio of 5.0% or greater, and is not subject to any order or written directive by any such regulatory authority to meet and maintain a specific capital level for any capital measure; (ii) “adequately capitalized” if the institution has a total risk-based capital ratio of 8.0% or greater, a Tier 1 risk-based capital ratio of 4.0% or greater, and a leverage ratio of 4.0% or greater and is not “well capitalized”; (iii) “undercapitalized” if the institution has a total risk-based capital ratio that is less than 8.0%, a Tier 1 risk-based capital ratio of less than 4.0% or a leverage ratio of less than 4.0%; (iv) “significantly undercapitalized” if the institution has a total risk-based capital ratio of less than 6.0%, a Tier 1 risk-based capital ratio of less than 3.0% or a leverage ratio of less than 3.0%; and (v) “critically undercapitalized” if the institution’s tangible equity is equal to or less than 2.0% of average quarterly tangible assets. An institution may be downgraded to, or deemed to be in, a capital category that is lower than indicated by its capital ratios if it is determined to be in an unsafe or unsound condition or if it receives an unsatisfactory examination rating with respect to certain matters. A bank’s capital category is determined solely for the purpose of applying prompt corrective action regulations, and the capital category may not constitute an accurate representation of the bank’s overall financial condition or prospects for other purposes.

The FDIA generally prohibits a depository institution from making any capital distributions (including payment of a dividend) or paying any management fee to its parent holding company if the depository institution would thereafter be “undercapitalized.” “Undercapitalized” institutions are subject to growth limitations and are required to submit a capital restoration plan. The agencies 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 depository institution’s capital. In addition, for a capital restoration plan to be acceptable, the depository institution’s parent holding company must guarantee that the institution will comply with such capital restoration plan. The bank holding company must also provide appropriate assurances of performance. The aggregate liability of the parent holding company is limited to the lesser of (i) an amount equal to 5.0% of the depository institution’s total assets at the time it became undercapitalized and (ii) the amount which is necessary (or would have been necessary) to bring the institution into compliance with all capital standards applicable with respect to such institution as of the time it fails to comply with the plan. If a depository institution fails to submit an acceptable plan, it is treated as if it is “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. “Critically undercapitalized” institutions are subject to the appointment of a receiver or conservator.

The appropriate federal banking agency may, under certain circumstances, reclassify a well capitalized insured depository institution as adequately capitalized. The FDIA provides that an institution may be reclassified if the appropriate federal banking agency determines (after notice and opportunity for hearing) that the institution is in an unsafe or unsound condition or deems the institution to be engaging in an unsafe or unsound practice.

The appropriate agency is also permitted to require an adequately capitalized or undercapitalized institution to comply with the supervisory provisions as if the institution were in the next lower category (but not treat a significantly undercapitalized institution as critically undercapitalized) based on supervisory information other than the capital levels of the institution.

Cullen/Frost believes that, as of December 31, 2013, its bank subsidiary, Frost Bank, was “well capitalized” based on the aforementioned ratios. For further information regarding the capital ratios and leverage ratio of Cullen/Frost and Frost Bank see the discussion under the section captioned “Capital and Liquidity” included in Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations and Note 9 - Capital and Regulatory Matters in the notes to consolidated financial statements included in Item 8. Financial Statements and Supplementary Data, elsewhere in this report.

The Basel III Capital Rules revise the current prompt corrective action requirements effective January 1, 2015 by (i) introducing a CET1 ratio requirement at each level (other than critically undercapitalized), with the required CET1 ratio being 6.5% for well-capitalized status; (ii) increasing the minimum Tier 1 capital ratio requirement for each category (other than critically undercapitalized), with the minimum Tier 1 capital ratio for well-capitalized status being 8% (as compared to the current 6%); and (iii) eliminating the current provision that provides that a bank with a composite supervisory rating of 1 may have a 3% leverage ratio and still be adequately capitalized. The Basel III Capital Rules do not change the total risk-based capital requirement for any prompt corrective action category.

Deposit Insurance

Substantially all of the deposits of Frost Bank are insured up to applicable limits by the Deposit Insurance Fund ("DIF") of the FDIC and are subject to deposit insurance assessments to maintain the DIF. Deposit insurance assessments are based on average total assets minus average tangible equity. For larger institutions, such as Frost Bank, the FDIC uses a performance score and a loss-severity score that are used to calculate an initial assessment rate. In calculating these scores, the FDIC uses a bank's capital level and supervisory ratings (its "CAMELS ratings") and certain financial measures to assess an institution's ability to withstand asset-related stress and funding-related stress. The FDIC has the ability to make discretionary adjustments to the total score based upon significant risk factors that are not adequately captured in the calculations.

The initial base assessment rate ranges from 5 to 35 basis points on an annualized basis. After the effect of potential base-rate adjustments, the total base assessment rate could range from 2.5 to 45 basis points on an annualized basis. As the DIF reserve ratio grows, the rate schedule will be adjusted downward. Additionally, an institution must pay an additional premium equal to 50 basis points on every dollar (above 3% of an institution's Tier 1 capital) of long-term, unsecured debt held that was issued by another insured depository institution (excluding debt guaranteed under the Temporary Liquidity Guarantee Program).

In October 2010, the FDIC adopted a new DIF restoration plan to ensure that the fund reserve ratio reaches 1.35% by September 30, 2020, as required by the Dodd-Frank Act. At least semi-annually, the FDIC will update its loss and income projections for the fund and, if needed, will increase or decrease assessment rates, following notice-and-comment rulemaking if required.

FDIC deposit insurance expense totaled \$11.7 million, \$11.1 million and \$12.7 million in 2013, 2012 and 2011, respectively. FDIC deposit insurance expense includes deposit insurance assessments and Financing Corporation ("FICO") assessments related to outstanding FICO bonds. The FICO is a mixed-ownership government corporation established by the Competitive Equality Banking Act of 1987 whose sole purpose was to function as a financing vehicle for the now defunct Federal Savings & Loan Insurance Corporation.

Under 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.

Safety and Soundness Standards

The FDIA requires the federal bank regulatory agencies to prescribe standards, by regulations or guidelines, relating to internal controls, information systems and internal audit systems, loan documentation, credit underwriting, interest rate risk exposure, asset growth, asset quality, earnings, stock valuation and compensation, fees and benefits, and such other operational and managerial standards as the agencies deem appropriate. Guidelines adopted by the federal bank regulatory agencies establish general standards relating to internal controls and information systems, internal audit systems, loan documentation, credit underwriting, interest rate exposure, asset growth and compensation, fees and benefits. In general, the guidelines require, among other things, appropriate systems and practices to identify and manage the risk and exposures specified in the guidelines. The guidelines prohibit excessive compensation as an unsafe and unsound practice and describe compensation as excessive when the amounts paid are unreasonable or disproportionate to the services performed by an executive officer, employee, director or principal stockholder. In addition, the agencies adopted regulations that authorize, but do not require, an agency to order an institution that has been given notice by an agency that it is not satisfying any of such safety and soundness standards to submit a compliance plan. If, after being so notified, an institution fails to submit an acceptable compliance plan or fails in any material respect to implement an acceptable compliance plan, the agency must issue an order directing action to correct the deficiency and may issue an order directing other actions of the types to which an undercapitalized institution is subject under the "prompt corrective action" provisions of the FDIA. See "Prompt Corrective Action" above. If an institution fails to comply with such an order, the agency may seek to enforce such order in judicial proceedings and to impose civil money penalties.

Consumer Financial Protection Bureau Supervision

Dodd-Frank centralized responsibility for consumer financial protection by creating a new agency, the Consumer Financial Protection Bureau ("CFPB"), and giving it responsibility for implementing, examining and enforcing compliance with federal consumer protection laws. In July 2011, Frost Bank was notified that it will be supervised by the CFPB for certain consumer protection purposes. The CFPB will focus on:

- Risks to consumers and compliance with the federal consumer financial laws, when it evaluates the policies and practices of a financial institution.

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- The markets in which firms operate and risks to consumers posed by activities in those markets.
- Depository institutions that offer a wide variety of consumer financial products and services; depository institutions with a more specialized focus.
- Non-depository companies that offer one or more consumer financial products or services.

Banking regulators take into account compliance with consumer protection laws when considering approval of a proposed transaction.

Depositor Preference

The FDIA provides that, in the event of the "liquidation or other resolution" of an insured depository institution, the claims of depositors of the institution, including the claims of the FDIC as subrogee of insured depositors, and certain claims for administrative expenses of the FDIC as a receiver, will have priority over other general unsecured claims against the institution. If an insured depository institution fails, insured and uninsured depositors, along with the FDIC, will have priority in payment ahead of unsecured, non-deposit creditors, including depositors whose deposits are payable only outside of the United States and the parent bank holding company, with respect to any extensions of credit they have made to such insured depository institution.

Community Reinvestment Act

The Community Reinvestment Act of 1977 ("CRA") requires depository institutions to assist in meeting the credit needs of their market areas consistent with safe and sound banking practice. Under the CRA, each depository institution is required to help meet the credit needs of its market areas by, among other things, providing credit to low- and moderate-income individuals and communities. Depository institutions are periodically examined for compliance with the CRA and are assigned ratings. In order for a financial holding company to commence any new activity permitted by the BHC Act, or to acquire any company engaged in any new activity permitted by the BHC Act, each insured depository institution subsidiary of the financial holding company must have received a rating of at least "satisfactory" in its most recent examination under the CRA. Furthermore, banking regulators take into account CRA ratings when considering approval of a proposed transaction. Frost Bank received a rating of "satisfactory" in its most recent CRA examination in 2008.

Financial Privacy

The federal banking regulators adopted rules that limit the ability of banks and other financial institutions to disclose non-public information about consumers to nonaffiliated third parties. These limitations require disclosure of privacy policies to consumers and, in some circumstances, allow consumers to prevent disclosure of certain personal information to a nonaffiliated third party. These regulations affect how consumer information is transmitted through diversified financial companies and conveyed to outside vendors.

Anti-Money Laundering and the USA Patriot Act

A major focus of governmental policy on financial institutions in recent years has been aimed at combating money laundering and terrorist financing. The USA PATRIOT Act of 2001 (the "USA Patriot Act") substantially broadened the scope of United States anti-money laundering laws and regulations by imposing significant new compliance and due diligence obligations, creating new crimes and penalties and expanding the extra-territorial jurisdiction of the United States. Failure of a financial institution to maintain and implement adequate programs to combat money laundering and terrorist financing, or to comply with all of the relevant laws or regulations, could have serious legal and reputational consequences for the institution, including causing applicable bank regulatory authorities not to approve merger or acquisition transactions when regulatory approval is required or to prohibit such transactions even if approval is not required.

Office of Foreign Assets Control Regulation

The United States has imposed economic sanctions that affect transactions with designated foreign countries, nationals and others which are administered by the U.S. Treasury Department Office of Foreign Assets Control. Failure to comply with these sanctions could have serious legal and reputational consequences, including causing applicable bank regulatory authorities not to approve merger or acquisition transactions when regulatory approval is required or to prohibit such transactions even if approval is not required.

Incentive Compensation

The Dodd-Frank Act requires the federal bank regulatory agencies and the SEC to establish joint regulations or guidelines prohibiting incentive-based payment arrangements at specified regulated entities, such as the Corporation and Frost Bank, having at least $1 billion in total assets that encourage inappropriate risks by providing an executive officer, employee, director or principal shareholder with excessive compensation, fees, or benefits or that could lead to material financial loss to the entity. In addition,

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these regulators must establish regulations or guidelines requiring enhanced disclosure to regulators of incentive-based compensation arrangements. The agencies proposed such regulations in April 2011, but the regulations have not been finalized. If the regulations are adopted in the form initially proposed, they will impose limitations on the manner in which the Corporation may structure compensation for its executives.

In June 2010, the Federal Reserve Board, OCC and FDIC issued a comprehensive final guidance on incentive compensation policies intended to ensure that the incentive compensation policies of banking organizations do not undermine the safety and soundness of such organizations by encouraging excessive risk-taking. The 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 the key principles that a banking organization’s incentive compensation arrangements should (i) provide incentives that do not encourage risk-taking beyond the organization’s ability to effectively identify and manage risks, (ii) be compatible with effective internal controls and risk management, and (iii) be supported by strong corporate governance, including active and effective oversight by the organization’s board of directors. These three principles are incorporated into the proposed joint compensation regulations under the Dodd-Frank Act, discussed above.

The Federal Reserve Board will review, as part of the regular, risk-focused examination process, the incentive compensation arrangements of banking organizations, such as the Corporation, that are not “large, complex banking organizations.” These reviews will be tailored to each organization based on the scope and complexity of the organization’s activities and the prevalence of incentive compensation arrangements. The findings of the supervisory initiatives will be included in reports of examination. Deficiencies will be incorporated into the organization’s supervisory ratings, which can affect the organization’s ability to make acquisitions and take other actions. Enforcement actions may be taken against a banking organization if its incentive compensation arrangements, or related risk-management control or governance processes, pose a risk to the organization’s safety and soundness and the organization is not taking prompt and effective measures to correct the deficiencies.

Legislative and Regulatory Initiatives

From time to time, various legislative and regulatory initiatives are introduced in Congress and state legislatures, as well as by regulatory agencies. Such initiatives may 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 Corporation 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 Corporation 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 Corporation. A change in statutes, regulations or regulatory policies applicable to Cullen/Frost or any of its subsidiaries could have a material effect on the Corporation’s business, financial condition and results of operations.

Employees

At December 31, 2013, the Corporation employed 3,979 full-time equivalent employees. None of the Corporation’s employees are represented by collective bargaining agreements. The Corporation believes its employee relations to be good.

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Executive Officers of the Registrant

The names, ages as of December 31, 2013, recent business experience and positions or offices held by each of the executive officers of Cullen/Frost are as follows:

Name and Position Held	Age	Recent Business Experience
Richard W. Evans, Jr. Chairman of the Board, Chief Executive Officer and Director	67	Officer of Frost Bank since 1973. Chairman of the Board and Chief Executive Officer of Cullen/Frost from October 1997 to present.
Patrick B. Frost President of Frost Bank and Director	53	Officer of Frost Bank since 1985. President of Frost Bank from August 1993 to present. Director of Cullen/Frost from May 1997 to present.
Phillip D. Green Group Executive Vice President, Chief Financial Officer	59	Officer of Frost Bank since July 1980. Group Executive Vice President, Chief Financial Officer of Cullen/Frost from October 1995 to present.
David W. Beck President, Chief Business Banking Officer of Frost Bank	63	Officer of Frost Bank since July 1973. President, Chief Business Banking Officer of Frost Bank from February 2001 to present.
Robert A. Berman Group Executive Vice President, E-Commerce Operations Research and Strategy of Frost Bank	51	Officer of Frost Bank since January 1989. Group Executive Vice President, E-Commerce Operations Research and Strategy of Frost Bank from May 2001 to present.
Paul H. Bracher President, State Regions of Frost Bank	57	Officer of Frost Bank since January 1982. President, State Regions of Frost Bank from February 2001 to present.
Richard Kardys Group Executive Vice President, Frost Wealth Advisors of Frost Bank	67	Officer of Frost Bank since January 1977. Group Executive Vice President, Frost Wealth Advisors of Frost Bank from May 2001 to present.
Paul J. Olivier Group Executive Vice President, Chief Consumer Banking Officer of Frost Bank	61	Officer of Frost Bank since August 1976. Group Executive Vice President, Chief Consumer Banking Officer of Frost Bank from May 2001 to present.
William L. Perotti Group Executive Vice President, Chief Credit Officer and Chief Risk Officer of Frost Bank	56	Officer of Frost Bank since December 1982. Group Executive Vice President, Chief Credit Officer of Frost Bank from May 2001 to present. Chief Risk Officer of Frost Bank from April 2005 to present.
Emily A. Skillman Group Executive Vice President, Human Resources of Frost Bank	69	Officer of Frost Bank since January 1998. Group Executive Vice President, Human Resources of Frost Bank from October 2003 to present.

There are no arrangements or understandings between any executive officer of Cullen/Frost and any other person pursuant to which such executive officer was or is to be selected as an officer.

Available Information

Under the Securities Exchange Act of 1934, Cullen/Frost is required to file annual, quarterly and current reports, proxy statements and other information with the Securities and Exchange Commission (“SEC”). You may read and copy any document Cullen/Frost files with the SEC at the SEC’s Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information about the public reference room. The SEC maintains a website at http://www.sec.gov that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC. Cullen/Frost files electronically with the SEC.

Cullen/Frost makes available, free of charge through its website, its reports on Forms 10-K, 10-Q and 8-K, and amendments to those reports, as soon as reasonably practicable after such reports are filed with or furnished to the SEC. Additionally, the Corporation has adopted and posted on its website a code of ethics that applies to its principal executive officer, principal financial officer and principal accounting officer. The Corporation’s website also includes its corporate governance guidelines and the charters for its audit committee, its compensation and benefits committee, and its corporate governance and nominating committee. The address for the Corporation’s website is http://www.frostbank.com. The Corporation will provide a printed copy of any of the aforementioned documents to any requesting shareholder.

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ITEM 1A. RISK FACTORS

An investment in the Corporation's common stock is subject to risks inherent to the Corporation's business. The material risks and uncertainties that management believes affect the Corporation are described below. Before making an investment decision, you should carefully consider the risks and uncertainties described below together with all of the other information included or incorporated by reference in this report. The risks and uncertainties described below are not the only ones facing the Corporation. Additional risks and uncertainties that management is not aware of or focused on or that management currently deems immaterial may also impair the Corporation's business operations. This report is qualified in its entirety by these risk factors.

If any of the following risks actually occur, the Corporation's business, financial condition and results of operations could be materially and adversely affected. If this were to happen, the market price of the Corporation's common stock could decline significantly, and you could lose all or part of your investment.

Risks Related To The Corporation's Business

The Corporation's Business May Be Adversely Affected By Conditions In The Financial Markets and Economic Conditions Generally

In recent years, the U.S. economy has faced a severe economic crisis including a major recession from which it is slowly recovering. Business activity across a wide range of industries and regions in the U.S. remains reduced and local governments and many businesses continue to experience financial difficulty. While reflecting some improvement, unemployment levels remain elevated. There can be no assurance that these conditions will continue to improve and these conditions could worsen. In addition, on-going federal budget negotiations, the implementation of the Patient Protection and Affordable Care Act and the level of U.S. debt may have a destabilizing effect on financial markets.

The Corporation's financial performance generally, and in particular the ability of borrowers to pay interest on and repay principal of outstanding loans and the value of collateral securing those loans, as well as demand for loans and other products and services the Corporation offers, is highly dependent upon the business environment in the markets where the Corporation operates, in the State of Texas and in the United States as a whole. A favorable business environment is generally characterized by, among other factors, economic growth, efficient capital markets, low inflation, low unemployment, high business and investor confidence, and strong business earnings. Unfavorable or uncertain economic and market conditions can be caused by declines in economic growth, business activity or investor or business confidence; limitations on the availability or increases in the cost of credit and capital; increases in inflation or interest rates; high unemployment, natural disasters; or a combination of these or other factors.

Overall, during recent years, the business environment has been adverse for many households and businesses in the United States and worldwide. While economic conditions in the State of Texas, the United States and worldwide have improved since the recession, there can be no assurance that this improvement will continue. Economic pressure on consumers and uncertainty regarding continuing economic improvement may result in changes in consumer and business spending, borrowing and savings habits. Such conditions could adversely affect the credit quality of the Corporation's loans and the Corporation' business, financial condition and results of operations.

The Corporation Is Subject To Lending Risk

There are inherent risks associated with the Corporation's lending activities. These risks include, among other things, the impact of changes in interest rates and changes in the economic conditions in the markets where the Corporation operates as well as those across the State of Texas and the United States. Increases in interest rates and/or weakening economic conditions could adversely impact the ability of borrowers to repay outstanding loans or the value of the collateral securing these loans. The Corporation is also subject to various laws and regulations that affect its lending activities. Failure to comply with applicable laws and regulations could subject the Corporation to regulatory enforcement action that could result in the assessment of significant civil money penalties against the Corporation.

As of December 31, 2013, approximately 88.0% of the Corporation's loan portfolio consisted of commercial and industrial, construction and commercial real estate mortgage loans. These types of loans are generally viewed as having more risk of default than residential real estate loans or consumer loans. These types of loans are also typically larger than residential real estate loans and consumer loans. Because the Corporation's loan portfolio contains a significant number of commercial and industrial, construction and commercial real estate loans with relatively large balances, the deterioration of one or a few of these loans could cause a significant increase in non-performing loans. An increase in non-performing loans could result in a net loss of earnings from these loans, an increase in the provision for loan losses and an increase in loan charge-offs, all of which could have a material adverse effect on the Corporation's business, financial condition and results of operations.

See the section captioned “Loans” in Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations located elsewhere in this report for further discussion related to commercial and industrial, construction and commercial real estate loans.

The Corporation Is Subject To Interest Rate Risk

The Corporation’s earnings and cash flows are largely dependent upon its net interest income. Net interest income is the difference between interest income earned on interest-earning assets such as loans and securities and interest expense paid on interest-bearing liabilities such as deposits and borrowed funds. Interest rates are highly sensitive to many factors that are beyond the Corporation’s control, including general economic conditions and policies of various governmental and regulatory agencies and, in particular, the Federal Open Market Committee. Changes in monetary policy, including changes in interest rates, could influence not only the interest the Corporation receives on loans and securities and the amount of interest it pays on deposits and borrowings, but such changes could also affect (i) the Corporation’s ability to originate loans and obtain deposits, (ii) the fair value of the Corporation’s financial assets and liabilities, and (iii) the average duration of the Corporation’s mortgage-backed securities portfolio. If the interest rates paid on deposits and other borrowings increase at a faster rate than the interest rates received on loans and other investments, the Corporation’s net interest income, and therefore earnings, could be adversely affected. Earnings could also be adversely affected if the interest rates received on loans and other investments fall more quickly than the interest rates paid on deposits and other borrowings. Any substantial, unexpected, prolonged change in market interest rates could have a material adverse effect on the Corporation’s business, financial condition and results of operations.

See the section captioned “Net Interest Income” in Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations located elsewhere in this report for further discussion related to the Corporation’s management of interest rate risk.

The Corporation’s Allowance For Loan Losses May Be Insufficient

The Corporation maintains an allowance for loan losses, which is a reserve established through a provision for loan losses charged to expense, which represents management’s best estimate of probable losses that have been incurred within the existing portfolio of loans. The allowance, in the judgment of management, is necessary to reserve for estimated loan losses and risks inherent in the loan portfolio. The level of the allowance reflects management’s continuing evaluation of industry concentrations; specific credit risks; loan loss experience; current loan portfolio quality; present economic, political and regulatory conditions and unidentified losses inherent in the current loan portfolio. The determination of the appropriate level of the allowance for loan losses inherently involves a high degree of subjectivity and requires the Corporation to make significant estimates of current credit risks and future trends, all of which may undergo material changes. Continuing deterioration in economic conditions affecting borrowers, new information regarding existing loans, identification of additional problem loans and other factors, both within and outside of the Corporation’s control, may require an increase in the allowance for loan losses. In addition, bank regulatory agencies periodically review the Corporation’s allowance for loan losses and may require an increase in the provision for loan losses or the recognition of further loan charge-offs, based on judgments different than those of management. Furthermore, if charge-offs in future periods exceed the allowance for loan losses, the Corporation will need additional provisions to increase the allowance for loan losses. Any increases in the allowance for loan losses will result in a decrease in net income and, possibly, capital, and may have a material adverse effect on the Corporation’s business, financial condition and results of operations.

See the section captioned “Allowance for Loan Losses” in Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations located elsewhere in this report for further discussion related to the Corporation’s process for determining the appropriate level of the allowance for loan losses.

The Corporation’s Profitability Depends Significantly On Economic Conditions In The State Of Texas

The Corporation’s success depends primarily on the general economic conditions of the State of Texas and the specific local markets in which the Corporation operates. Unlike larger national or other regional banks that are more geographically diversified, the Corporation provides banking and financial services to customers across Texas through financial centers in the Austin, Corpus Christi, Dallas, Fort Worth, Houston, Rio Grande Valley and San Antonio regions. The local economic conditions in these areas have a significant impact on the demand for the Corporation’s products and services as well as the ability of the Corporation’s customers to repay loans, the value of the collateral securing loans and the stability of the Corporation’s deposit funding sources. Moreover, approximately 96.3% of the securities in the Corporation’s municipal bond portfolio were issued by political subdivisions or agencies within the State of Texas. A significant decline in general economic conditions in Texas, whether caused by recession, inflation, unemployment, changes in securities markets, acts of terrorism, outbreak of hostilities or other international or domestic occurrences or other factors could impact these local economic conditions and, in turn, have a material adverse effect on the Corporation’s business, financial condition and results of operations.

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The Corporation May Be Adversely Affected By The Soundness Of Other Financial Institutions

Financial services institutions are interrelated as a result of trading, clearing, counterparty, or other relationships. The Corporation has exposure to many different industries and counterparties, and routinely executes transactions with counterparties in the financial services industry, including commercial banks, brokers and dealers, investment banks, and other institutional clients. Many of these transactions expose the Corporation to credit risk in the event of a default by a counterparty or client. In addition, the Corporation's credit risk may be exacerbated when the collateral held by the Corporation cannot be realized upon or is liquidated at prices not sufficient to recover the full amount of the credit or derivative exposure due to the Corporation. Any such losses could have a material adverse effect on the Corporation's business, financial condition and results of operations.

The Corporation Operates In A Highly Competitive Industry and Market Area

The Corporation faces substantial competition in all areas of its operations from a variety of different competitors, many of which are larger and may have more financial resources. Such competitors primarily include national, regional, and community banks within the various markets where the Corporation operates. The Corporation also faces competition from many other types of financial institutions, including, without limitation, savings and loans, credit unions, finance companies, brokerage firms, insurance companies, factoring companies and other financial intermediaries. The financial services industry could become even more competitive as a result of legislative, regulatory and technological changes and continued consolidation. Also, technology and other changes have lowered barriers to entry and made it possible for non-banks to offer products and services traditionally provided by banks. For example, consumers can maintain funds that would have historically been held as bank deposits in brokerage accounts or mutual funds. Consumers can also complete transactions such as paying bills and/or transferring funds directly without the assistance of banks. The process of eliminating banks as intermediaries, known as "disintermediation," could result in the loss of fee income, as well as the loss of customer deposits and the related income generated from those deposits. Further, many of the Corporation's competitors have fewer regulatory constraints and may have lower cost structures. Additionally, due to their size, many competitors may be able to achieve economies of scale and, as a result, may offer a broader range of products and services as well as better pricing for those products and services than the Corporation can.

The Corporation's ability to compete successfully depends on a number of factors, including, among other things:

- The ability to develop, maintain and build long-term customer relationships based on top quality service, high ethical standards and safe, sound assets.
- The ability to expand the Corporation's market position.
- The scope, relevance and pricing of products and services offered to meet customer needs and demands.
- The rate at which the Corporation introduces new products and services relative to its competitors.
- Customer satisfaction with the Corporation's level of service.
- Industry and general economic trends.

Failure to perform in any of these areas could significantly weaken the Corporation's competitive position, which could adversely affect the Corporation's growth and profitability, which, in turn, could have a material adverse effect on the Corporation's business, financial condition and results of operations.

The Corporation Is Subject To Extensive Government Regulation and Supervision and Possible Enforcement and Other Legal Actions

The Corporation, primarily through Cullen/Frost, Frost Bank and certain non-bank subsidiaries, is subject to extensive federal and state regulation and supervision, which vests a significant amount of discretion in the various regulatory authorities. Banking regulations are primarily intended to protect depositors' funds, federal deposit insurance funds and the banking system as a whole, not security holders. These regulations and supervisory guidance affect the Corporation's lending practices, capital structure, investment practices, dividend policy and growth, among other things. Congress and federal regulatory agencies continually review banking laws, regulations and policies for possible changes. The Dodd-Frank Act, enacted in July 2010, instituted major changes to the banking and financial institutions regulatory regimes. Other changes to statutes, regulations or regulatory policies or supervisory guidance, including changes in interpretation or implementation of statutes, regulations, policies or supervisory guidance, could affect the Corporation in substantial and unpredictable ways. Such changes could subject the Corporation to additional costs, limit the types of financial services and products the Corporation may offer and/or increase the ability of non-banks to offer competing financial services and products, among other things. Failure to comply with laws, regulations, policies or supervisory guidance could result in enforcement and other legal actions by Federal or state authorities, including criminal and civil penalties, the loss of FDIC insurance, the revocation of a banking charter, other sanctions by regulatory agencies, civil money penalties and/or reputation damage. In this regard, government authorities, including the bank regulatory agencies, are pursuing aggressive enforcement actions with respect to compliance and other legal matters involving financial activities, which heightens the risks associated with actual and perceived compliance failures. Any of the foregoing could have a material adverse effect on the Corporation's business, financial condition and results of operations.

See the sections captioned "Supervision and Regulation" included in Item 1. Business and Note 9 - Capital and Regulatory Matters in the notes to consolidated financial statements included in Item 8. Financial Statements and Supplementary Data, which are located elsewhere in this report.

The Corporation's Accounting Estimates and Risk Management Processes Rely On Analytical and Forecasting Models

The processes the Corporation uses to estimate its probable loan 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 Corporation'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 Corporation uses for interest rate risk and asset-liability management are inadequate, the Corporation may incur increased or unexpected losses upon changes in market interest rates or other market measures. If the models the Corporation uses for determining its probable loan losses are inadequate, the allowance for loan losses may not be sufficient to support future charge-offs. If the models the Corporation uses to measure the fair value financial instruments are inadequate, the fair value of such financial instruments may fluctuate unexpectedly or may not accurately reflect what the Corporation could realize upon sale or settlement of such financial instruments. Any such failure in the Corporation's analytical or forecasting models could have a material adverse effect on the Corporation's business, financial condition and results of operations.

The Repeal Of Federal Prohibitions On Payment Of Interest On Demand Deposits Could Increase The Corporation's Interest Expense

All federal prohibitions on the ability of financial institutions to pay interest on demand deposit accounts were repealed as part of the Dodd-Frank Act beginning on July 21, 2011. As a result, some financial institutions have commenced offering interest on demand deposits to compete for customers. The Corporation does not yet know what interest rates other institutions may offer as market interest rates begin to increase. The Corporation's interest expense will increase and its net interest margin will decrease if it begins offering interest on demand deposits to attract additional customers or maintain current customers, which could have a material adverse effect on the Corporation's business, financial condition and results of operations.

The Corporation May Need To Raise Additional Capital In The Future, and Such Capital May Not Be Available When Needed Or At All

The Corporation may need to raise additional capital in the future to provide it with sufficient capital resources and liquidity to meet its commitments and business needs, particularly if its asset quality or earnings were to deteriorate significantly. The Corporation's ability to raise additional capital, if needed, will depend on, among other things, conditions in the capital markets at that time, which are outside of its control, and its financial condition. Economic conditions and the loss of confidence in financial institutions may increase the Corporation's cost of funding and limit access to certain customary sources of capital, including inter-bank borrowings, repurchase agreements and borrowings from the discount window of the Federal Reserve Board.

The Corporation cannot assure that such capital will be available on acceptable terms or at all. Any occurrence that may limit the Corporation's access to the capital markets, such as a decline in the confidence of debt purchasers, depositors of Frost Bank or counterparties participating in the capital markets, or a downgrade of Cullen/Frost's or Frost Bank's debt ratings, may adversely affect the Corporation's capital costs and its ability to raise capital and, in turn, its liquidity. Moreover, if the Corporation needs to raise capital in the future, it may have to do so when many other financial institutions are also seeking to raise capital and would have to compete with those institutions for investors. An inability to raise additional capital on acceptable terms when needed could have a materially adverse effect on the Corporation's business, financial condition and results of operations.

The Value Of The Corporation's Goodwill and Other Intangible Assets May Decline In The Future

As of December 31, 2013, the Corporation had $543.0 million of goodwill and other intangible assets. A significant decline in the Corporation's expected future cash flows, a significant adverse change in the business climate, slower growth rates or a significant and sustained decline in the price of Cullen/Frost's common stock may necessitate taking charges in the future related to the impairment of the Corporation's goodwill and other intangible assets. If the Corporation were to conclude that a future write-down of goodwill and other intangible assets is necessary, the Corporation would record the appropriate charge, which could have a material adverse effect on the Corporation's business, financial condition and results of operations.

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The Corporation's Controls and Procedures May Fail or Be Circumvented

The Corporation's internal controls, disclosure controls and procedures, and corporate governance policies and procedures are based in part on certain assumptions and can provide only reasonable, not absolute, assurances that the objectives of the system are met. Any failure or circumvention of the Corporation's controls and procedures or failure to comply with regulations related to controls and procedures could have a material adverse effect on the Corporation's business, financial condition and results of operations.

New Lines Of Business Or New Products and Services May Subject The Corporation To Additional Risks

From time to time, the Corporation 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 developing and marketing new lines of business and/or new products and services the Corporation 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 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 the Corporation's system of internal controls. Failure to successfully manage these risks in the development and implementation of new lines of business or new products or services could have a material adverse effect on the Corporation's business, financial condition and results of operations.

Cullen/Frost Relies On Dividends From Its Subsidiaries For Most Of Its Revenue

Cullen/Frost is a separate and distinct legal entity from its subsidiaries. It receives substantially all of its revenue from dividends from its subsidiaries. These dividends are the principal source of funds to pay dividends on Cullen/Frost's common stock and interest and principal on Cullen/Frost's debt. Various federal and state laws and regulations limit the amount of dividends that Frost Bank and certain non-bank subsidiaries may pay to Cullen/Frost. Also, Cullen/Frost's right to participate in a distribution of assets upon a subsidiary's liquidation or reorganization is subject to the prior claims of the subsidiary's creditors. In the event Frost Bank is unable to pay dividends to Cullen/Frost, Cullen/Frost may not be able to service debt, pay obligations or pay dividends on the Corporation's common stock. The inability to receive dividends from Frost Bank could have a material adverse effect on the Corporation's business, financial condition and results of operations.

See the section captioned "Supervision and Regulation" in Item 1. Business and Note 9 - Capital and Regulatory Matters in the notes to consolidated financial statements included in Item 8. Financial Statements and Supplementary Data, which are located elsewhere in this report.

Potential Acquisitions May Disrupt The Corporation's Business and Dilute Stockholder Value

The Corporation generally seeks merger or acquisition partners that are culturally similar and have experienced management and possess either significant market presence or have potential for improved profitability through financial management, economies of scale or expanded services. Acquiring other banks, businesses, or branches involves various risks commonly associated with acquisitions, including, among other things:

- Potential exposure to unknown or contingent liabilities of the target company.
- Exposure to potential asset quality issues of the target company.
- Potential disruption to the Corporation's business.
- Potential diversion of the Corporation's management's time and attention.
- The possible loss of key employees and customers of the target company.
- Difficulty in estimating the value of the target company.
- Potential changes in banking or tax laws or regulations that may affect the target company.

Acquisitions typically involve the payment of a premium over book and market values, and, therefore, some dilution of the Corporation's tangible book value and net income per common share may occur in connection with any future transaction. Furthermore, failure to realize the expected revenue increases, cost savings, increases in geographic or product presence, and/or other projected benefits from an acquisition could have a material adverse effect on the Corporation's business, financial condition and results of operations.

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The Corporation Is Subject To Liquidity Risk

The Corporation requires liquidity to meet its deposit and debt obligations as they come due. The Corporation's access to funding sources in amounts adequate to finance its activities or on terms that are acceptable to it could be impaired by factors that affect it specifically or the financial services industry or economy generally. Factors that could reduce its access to liquidity sources include a downturn in the Texas market, difficult credit markets or adverse regulatory actions against the Corporation. The Corporation's access to deposits may also be affected by the liquidity needs of its depositors. In particular, a substantial majority of the Corporation's liabilities are demand, savings, interest checking and money market deposits, which are payable on demand or upon several days' notice, while by comparison, a substantial portion of its assets are loans, which cannot be called or sold in the same time frame. The Corporation may not be able to replace maturing deposits and advances as necessary in the future, especially if a large number of its depositors sought to withdraw their accounts, regardless of the reason. A failure to maintain adequate liquidity could have a material adverse effect on the Corporation's business, financial condition and results of operations.

The Corporation May Not Be Able To Attract and Retain Skilled People

The Corporation's success depends, in large part, on its ability to attract and retain key people. Competition for the best people in most activities engaged in by the Corporation can be intense and the Corporation may not be able to hire people or to retain them. The Corporation does not currently have employment agreements or non-competition agreements with any of its senior officers. The unexpected loss of services of key personnel of the Corporation could have a material adverse impact on the Corporation's business, financial condition and results of operations because of their skills, knowledge of the Corporation's market, years of industry experience and the difficulty of promptly finding qualified replacement personnel.

The Corporation's Information Systems May Experience An Interruption Or Breach In Security

The Corporation relies heavily on communications and information systems to conduct its business. Any failure, interruption or breach in security of these systems could result in failures or disruptions in the Corporation's customer relationship management, general ledger, deposit, loan and other systems. Moreover, if any such failures, interruptions or security breaches do occur, they may not be adequately addressed. The occurrence of any failures, interruptions or security breaches of the Corporation's information systems could damage the Corporation's reputation, result in a loss of customer business, subject the Corporation to additional regulatory scrutiny, or expose the Corporation to civil litigation and possible financial liability, any of which could have a material adverse effect on the Corporation's business, financial condition and results of operations.

The Corporation Continually Encounters Technological Change

The financial services industry is continually undergoing rapid technological change with frequent introductions of new technology-driven products and services. The effective use of technology increases efficiency and enables financial institutions to better serve customers and to reduce costs. The Corporation's future success depends, in part, upon its ability to address the needs of its customers by using technology to provide products and services that will satisfy customer demands, as well as to create additional efficiencies in the Corporation's operations. Many of the Corporation's competitors have substantially greater resources to invest in technological improvements. The Corporation may not be able to effectively implement new technology-driven products and services or be successful in marketing these products and services to its customers. Failure to successfully keep pace with technological change affecting the financial services industry could have a material adverse impact on the Corporation's business, financial condition and results of operations.

The Corporation Is Subject To Claims and Litigation Pertaining To Fiduciary Responsibility

From time to time, customers make claims and take legal action pertaining to the Corporation's performance of its fiduciary responsibilities. Whether customer claims and legal action related to the Corporation's performance of its fiduciary responsibilities are founded or unfounded, if such claims and legal actions are not resolved in a manner favorable to the Corporation they may result in significant financial liability and/or adversely affect the market perception of the Corporation and its products and services as well as impact customer demand for those products and services. Any financial liability or reputation damage could have a material adverse effect on the Corporation's business, financial condition and results of operations.

The Corporation's Operations Rely On Certain External Vendors

The Corporation relies on certain external vendors to provide products and services necessary to maintain day-to-day operations of the Corporation. Accordingly, the Corporation’s operations are exposed to risk that these vendors will not perform in accordance with the contracted arrangements under service level agreements. The failure of an external vendor to perform in accordance with the contracted arrangements under service level agreements, because of changes in the vendor’s organizational structure, financial condition, support for existing products and services or strategic focus or for any other reason, could be disruptive to the Corporation’s operations, which could have a material adverse impact on the Corporation’s business and, in turn, the Corporation’s financial condition and results of operations.

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The Corporation Is Subject to Claims and Litigation Pertaining to Intellectual Property

Banking and other financial services companies, such as the Corporation, rely on technology companies to provide information technology products and services necessary to support the Corporations' day-to-day operations. Technology companies frequently enter into litigation based on allegations of patent infringement or other violations of intellectual property rights. In addition, patent holding companies seek to monetize patents they have purchased or otherwise obtained. Competitors of the Corporation's vendors, or other individuals or companies, have from time to time claimed to hold intellectual property sold to the Corporation by its vendors. Such claims may increase in the future as the financial services sector becomes more reliant on information technology vendors. The plaintiffs in these actions frequently seek injunctions and substantial damages.

Regardless of the scope or validity of such patents or other intellectual property rights, or the merits of any claims by potential or actual litigants, the Corporation may have to engage in protracted litigation. Such litigation is often expensive, time-consuming, disruptive to the Corporation's operations, and distracting to management. If the Corporation is found to infringe upon one or more patents or other intellectual property rights, it may be required to pay substantial damages or royalties to a third-party. In certain cases, the Corporation may consider entering into licensing agreements for disputed intellectual property, although no assurance can be given that such licenses can be obtained on acceptable terms or that litigation will not occur. These licenses may also significantly increase the Corporation's operating expenses. If legal matters related to intellectual property claims were resolved against the Corporation or settled, the Corporation could be required to make payments in amounts that could have a material adverse effect on its business, financial condition and results of operations.

The Corporation Is Subject To Environmental Liability Risk Associated With Lending Activities

A significant portion of the Corporation's loan portfolio is secured by real property. During the ordinary course of business, the Corporation may foreclose on and take title to properties securing certain loans. In doing so, there is a risk that hazardous or toxic substances could be found on these properties. If hazardous or toxic substances are found, the Corporation may be liable for remediation costs, as well as for personal injury and property damage. Environmental laws may require the Corporation to incur substantial expenses and may materially reduce the affected property's value or limit the Corporation's ability to use or sell the affected property. In addition, future laws or more stringent interpretations or enforcement policies with respect to existing laws may increase the Corporation's exposure to environmental liability. Environmental reviews of real property before initiating foreclosure actions may not be sufficient to detect all potential environmental hazards. The remediation costs and any other financial liabilities associated with an environmental hazard could have a material adverse effect on the Corporation's business, financial condition and results of operations.

Severe Weather, Natural Disasters, Acts Of War Or Terrorism and Other External Events Could Significantly Impact The Corporation's Business

Severe weather, natural disasters, acts of war or terrorism and other adverse external events could have a significant impact on the Corporation's ability to conduct business. In addition, such events could affect the stability of the Corporation's deposit base, impair the ability of borrowers to repay outstanding loans, impair the value of collateral securing loans, cause significant property damage, result in loss of revenue and/or cause the Corporation to incur additional expenses. The occurrence of any such event in the future could have a material adverse effect on the Corporation's business, which, in turn, could have a material adverse effect on the Corporation's business, financial condition and results of operations.

Financial Services Companies Depend On The Accuracy and Completeness Of Information About Customers and Counterparties

In deciding whether to extend credit or enter into other transactions, the Corporation may rely on information furnished by or on behalf of customers and counterparties, including financial statements, credit reports and other financial information. The Corporation may also rely on representations of those customers, counterparties or other third parties, such as independent auditors, as to the accuracy and completeness of that information. Reliance on inaccurate or misleading financial statements, credit reports or other financial information could have a material adverse impact on the Corporation's business, financial condition and results of operations.

Risks Associated With The Corporation's Common Stock

The Corporation’s Stock Price Can Be Volatile

Stock price volatility may make it more difficult for you to resell your common stock when you want and at prices you find attractive. The Corporation’s stock price can fluctuate significantly in response to a variety of factors including, among other things:

- Actual or anticipated variations in quarterly results of operations.
- Recommendations by securities analysts.

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- Operating and stock price performance of other companies that investors deem comparable to the Corporation.
- News reports relating to trends, concerns and other issues in the financial services industry.
- Perceptions in the marketplace regarding the Corporation and/or its competitors.
- New technology used, or services offered, by competitors.
- Significant acquisitions or business combinations, strategic partnerships, joint ventures or capital commitments by or involving the Corporation or its competitors.
- Failure to integrate acquisitions or realize anticipated benefits from acquisitions.
- Changes in government regulations.
- Geopolitical conditions such as acts or threats of terrorism or military conflicts.

General market fluctuations, industry factors and general economic and political conditions and events, such as economic slowdowns or recessions, interest rate changes or credit loss trends, could also cause the Corporation's stock price to decrease regardless of operating results.

The Trading Volume In The Corporation's Common Stock Is Less Than That Of Other Larger Financial Services Companies

Although the Corporation's common stock is listed for trading on the New York Stock Exchange (NYSE), the trading volume in its common stock is less than that of other, larger financial services companies. A public trading market having the desired characteristics of depth, liquidity and orderliness depends on the presence in the marketplace of willing buyers and sellers of the Corporation's common stock at any given time. This presence depends on the individual decisions of investors and general economic and market conditions over which the Corporation has no control. Given the lower trading volume of the Corporation's common stock, significant sales of the Corporation's common stock, or the expectation of these sales, could cause the Corporation's stock price to fall.

Cullen/Frost May Not Continue To Pay Dividends On Its Common Stock In The Future

Holders of Cullen/Frost common stock are only entitled to receive such dividends as its board of directors may declare out of funds legally available for such payments. Although Cullen/Frost has historically declared cash dividends on its common stock, it is not required to do so and may reduce or eliminate its common stock dividend in the future. This could adversely affect the market price of Cullen/Frost's common stock. Also, Cullen/Frost is a bank holding company, and its ability to declare and pay dividends is dependent on certain federal regulatory considerations, including the guidelines of the Federal Reserve Board regarding capital adequacy and dividends.

As more fully discussed in Note 9 - Capital and Regulatory Matters in the notes to consolidated financial statements included in Item 8. Financial Statements and Supplementary Data, which are located elsewhere in this report, the ability of the Corporation to declare or pay dividends on its common stock may also be subject to certain restrictions in the event that the Corporation elects to defer the payment of interest on its junior subordinated deferrable interest debentures or does not declare and pay dividends on its Series A Preferred Stock.

An Investment In The Corporation's Common Stock Is Not An Insured Deposit

The Corporation's common stock is not a bank deposit and, therefore, is not insured against loss by the Federal Deposit Insurance Corporation (FDIC), any other deposit insurance fund or by any other public or private entity. Investment in the Corporation's common stock is inherently risky for the reasons described in this "Risk Factors" section and elsewhere in this report and is subject to the same market forces that affect the price of common stock in any company. As a result, if you acquire the Corporation's common stock, you could lose some or all of your investment.

Certain Banking Laws May Have An Anti-Takeover Effect

Provisions of federal banking laws, including regulatory approval requirements, could make it more difficult for a third party to acquire the Corporation, even if doing so would be perceived to be beneficial to the Corporation's shareholders. These provisions effectively inhibit a non-negotiated merger or other business combination, which, in turn, could adversely affect the market price of the Corporation's common stock.

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ITEM 1B. UNRESOLVED STAFF COMMENTS

None

ITEM 2. PROPERTIES

The Corporation’s headquarters are located in downtown San Antonio, Texas. These facilities, which are owned by the Corporation, house the Corporation’s executive and primary administrative offices, as well as the principal banking headquarters of Frost Bank. The Corporation also owns or leases other facilities within its primary market areas in the regions of Austin, Corpus Christi, Dallas, Fort Worth, Houston, Rio Grande Valley and San Antonio. The Corporation considers its properties to be suitable and adequate for its present needs.

ITEM 3. LEGAL PROCEEDINGS

The Corporation is subject to various claims and legal actions that have arisen in the course of conducting business. Management does not expect the ultimate disposition of these matters to have a material adverse impact on the Corporation’s business, financial condition and results of operations.

ITEM 4. MINE SAFETY DISCLOSURES

None

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PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Common Stock Market Prices and Dividends

The Corporation's common stock is traded on the New York Stock Exchange, Inc. ("NYSE") under the symbol "CFR". The tables below set forth for each quarter of 2013 and 2012 the high and low intra-day sales prices per share of Cullen/Frost's common stock and the cash dividends declared per share.

	2013		2012	
Sales Price Per Share	High	Low	High	Low
First quarter	$62.62	$54.91	$61.11	$53.54
Second quarter	67.20	59.11	59.65	54.22
Third quarter	76.36	66.96	60.21	53.88
Fourth quarter	74.67	69.12	58.42	53.37

Cash Dividends Per Share	2013	2012
First quarter	$0.48	$0.46
Second quarter	0.50	0.48
Third quarter	0.50	0.48
Fourth quarter	0.50	0.48
Total	$1.98	$1.90

As of December 31, 2013, there were 60,566,443 shares of the Corporation's common stock outstanding held by 1,375 holders of record. The closing price per share of common stock on December 31, 2013, the last trading day of the Corporation's fiscal year, was $74.43.

The Corporation's management is currently committed to continuing to pay regular cash dividends; however, there can be no assurance as to future dividends because they are dependent on the Corporation's future earnings, capital requirements and financial condition. See the section captioned "Supervision and Regulation" included in Item 1. Business, the section captioned "Capital and Liquidity" included in Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations and Note 9 - Capital and Regulatory Matters in the notes to consolidated financial statements included in Item 8. Financial Statements and Supplementary Data, all of which are included elsewhere in this report.

Stock-Based Compensation Plans

Information regarding stock-based compensation awards outstanding and available for future grants as of December 31, 2013, segregated between stock-based compensation plans approved by shareholders and stock-based compensation plans not approved by shareholders, is presented in the table below. Additional information regarding stock-based compensation plans is presented in Note 11 - Employee Benefit Plans in the notes to consolidated financial statements included in Item 8. Financial Statements and Supplementary Data located elsewhere in this report.

Plan Category	Number of Shares to be Issued Upon Exercise of Outstanding Awards	Weighted-Average Exercise Price of Outstanding Awards	Number of Shares Available for Future Grants
Plans approved by shareholders	4,738,690	$54.35	2,862,603
Plans not approved by shareholders	—	—	—
Total	4,738,690	$54.35	2,862,603

Stock Repurchase Plans

From time to time, the Corporation has maintained several stock repurchase plans authorized by the Corporation's board of directors. In general, stock repurchase plans allow the Corporation to proactively manage its capital position and return excess capital to shareholders. Shares purchased under such plans also provide the Corporation with shares of common stock necessary to satisfy obligations related to stock compensation awards. During 2013, the Corporation implemented an accelerated share repurchase as a part of stock repurchase program authorized by the Corporation's board of directors in December 2012 to buy up to $150.0 million of the Corporation's common stock. The Corporation repurchased 2,236,748 shares at a total cost of $144.0 million under the accelerated share repurchase. No shares were repurchased under stock repurchase plans during 2012 or 2011.

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The following table provides information with respect to purchases made by or on behalf of the Corporation or any "affiliated purchaser" (as defined in Rule 10b-18(a)(3) under the Securities Exchange Act of 1934), of the Corporation's common stock during the fourth quarter of 2013.

Period	Total Number of Shares Purchased		Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans	Maximum Number (or Approximate Dollar Value) of Shares That May Yet Be Purchased Under the Plans at the End of the Period
October 1, 2013 to October 31, 2013	8,824	(1)	$ 71.47	—	$ 6,000
November 1, 2013 to November 30, 2013	—		—	—	6,000
December 1, 2013 to December 31, 2013	—		—	—	6,000
Total	8,824		$ 71.47	—	

(1) Represents repurchases made in connection with the vesting of certain share awards.

Performance Graph

The performance graph below compares the cumulative total shareholder return on Cullen/Frost Common Stock with the cumulative total return on the equity securities of companies included in the Standard & Poor's 500 Stock Index and the Standard and Poor's 500 Bank Index, measured at the last trading day of each year shown. The graph assumes an investment of $100 on December 31, 2008 and reinvestment of dividends on the date of payment without commissions. The performance graph represents past performance and should not be considered to be an indication of future performance.

	2008	2009	2010	2011	2012	2013
Cullen/Frost	$ 100.00	$ 102.34	$ 129.31	$ 115.85	$ 122.91	$ 173.63
S&P 500	100.00	126.46	145.51	148.59	172.37	228.19
S&P 500 Banks	100.00	93.41	111.94	99.95	124.17	168.52

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ITEM 6. SELECTED FINANCIAL DATA

The following consolidated selected financial data is derived from the Corporation's audited financial statements as of and for the five years ended December 31, 2013. The following consolidated financial data should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and the Consolidated Financial Statements and related notes included elsewhere in this report. All of the Corporation's acquisitions during the five years ended December 31, 2013 were accounted for using the purchase method. Accordingly, the operating results of the acquired companies are included with the Corporation's results of operations since their respective dates of acquisition. Dollar amounts, except per share data, and common shares outstanding are in thousands.

	Year Ended December 31,				
	2013	2012	2011	2010	2009
Consolidated Statements of Income					
Interest income:					
Loans, including fees	$415,230	$401,364	$397,855	$409,651	$432,222
Securities	219,904	225,844	218,744	202,713	188,446
Interest-bearing deposits	7,284	4,300	6,357	4,901	2,161
Federal funds sold and resell agreements	82	104	61	74	207
Total interest income	642,500	631,612	623,017	617,339	623,036
Interest expense:					
Deposits	14,459	18,099	22,179	29,973	56,015
Federal funds purchased and repurchase agreements	121	140	312	437	1,052
Junior subordinated deferrable interest debentures	6,426	6,806	6,783	6,982	7,231
Subordinated notes payable and other borrowings	939	1,706	11,967	16,488	22,059
Total interest expense	21,945	26,751	41,241	53,880	86,357
Net interest income	620,555	604,861	581,776	563,459	536,679
Provision for loan losses	20,582	10,080	27,445	43,611	65,392
Net interest income after provision for loan losses	599,973	594,781	554,331	519,848	471,287
Non-interest income:					
Trust and investment management fees	91,375	83,317	78,297	72,321	69,933
Service charges on deposit accounts	81,432	83,392	86,125	91,025	96,525
Insurance commissions and fees	43,140	39,948	35,421	34,015	33,096
Interchange and debit card transaction fees	16,979	16,933	29,625	30,542	26,248
Other charges, commissions and fees	34,185	30,180	27,750	25,380	23,826
Net gain (loss) on securities transactions	1,176	4,314	6,414	6	(1,260)
Other	34,531	30,703	26,370	28,744	45,338
Total non-interest income	302,818	288,787	290,002	282,033	293,706
Non-interest expense:					
Salaries and wages	273,692	258,752	252,028	239,589	230,643
Employee benefits	62,407	57,635	52,939	52,352	55,224
Net occupancy	50,468	48,975	46,968	46,166	44,188
Furniture and equipment	58,443	55,279	51,469	47,651	44,223
Deposit insurance	11,682	11,087	12,714	20,451	25,812
Intangible amortization	3,141	3,896	4,387	5,125	6,537
Other	152,077	139,469	137,593	124,207	125,611

Total non-interest expense	611,910	575,093	558,098	535,541	532,238
Income before income taxes	290,881	308,475	286,235	266,340	232,755
Income taxes	53,015	70,523	68,700	57,576	53,721
Net income	237,866	237,952	217,535	208,764	179,034
Preferred stock dividends	6,719	—	—	—	—
Net income available to common shareholders	$231,147	$237,952	$217,535	$208,764	$179,034

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	As of or for the Year Ended December 31,				
	2013	2012	2011	2010	2009
Per Common Share Data					
Net income - basic	$3.82	$3.87	$3.55	$3.44	$3.00
Net income - diluted	3.80	3.86	3.54	3.44	3.00
Cash dividends declared and paid	1.98	1.90	1.83	1.78	1.71
Book value	39.13	39.32	37.27	33.74	31.55
Common Shares Outstanding					
Period-end	60,566	61,479	61,264	61,108	60,038
Weighted-average shares - basic	60,350	61,298	61,101	60,411	59,456
Dilutive effect of stock compensation	766	345	177	175	58
Weighted - average shares - diluted	61,116	61,643	61,278	60,586	59,514
Performance Ratios					
Return on average assets	1.02 %	1.14 %	1.17 %	1.21 %	1.14 %
Return on average common equity	9.93	10.03	10.01	10.30	9.78
Net interest income to average earning assets	3.41	3.59	3.88	4.08	4.23
Dividend pay-out ratio	51.75	49.11	51.58	51.75	57.05
Balance Sheet Data					
Period-end:					
Loans	$9,515,700	$9,223,848	$7,995,129	$8,117,020	$8,367,780
Earning assets	22,238,286	21,148,475	18,497,987	15,806,350	14,437,267
Total assets	24,312,939	23,124,069	20,317,245	17,617,092	16,288,038
Non-interest-bearing demand deposits	8,311,149	8,096,937	6,672,555	5,360,436	4,645,802
Interest-bearing deposits	12,377,637	11,400,429	10,084,193	9,118,906	8,667,508
Total deposits	20,688,786	19,497,366	16,756,748	14,479,342	13,313,310
Long-term debt and other borrowings	223,712	223,719	223,738	373,757	392,646
Shareholders’ equity	2,514,161	2,417,482	2,283,537	2,061,680	1,894,424
Average:					
Loans	$9,229,574	$8,456,818	$8,042,968	$8,125,150	$8,652,563
Earning assets	20,991,221	19,015,707	16,769,028	15,333,348	13,803,919
Total assets	22,752,037	20,826,885	18,568,967	17,186,572	15,701,960
Non-interest-bearing demand deposits	7,657,774	7,021,927	5,738,982	5,023,780	4,258,484
Interest-bearing deposits	11,610,320	10,270,173	9,483,633	9,023,839	8,161,143
Total deposits	19,268,094	17,292,100	15,222,615	14,047,619	12,419,627
Long-term debt and other borrowings	223,713	223,728	310,870	382,651	576,161
Shareholders’ equity	2,455,041	2,372,745	2,172,096	2,027,699	1,831,133
Asset Quality					
Allowance for loan losses	$92,438	$104,453	$110,147	$126,316	$125,309
Allowance for losses to period-end loans	0.97 %	1.13 %	1.38 %	1.56 %	1.50 %
Net loan charge-offs	$32,597	$15,774	$43,614	$42,604	$50,327
Net loan charge-offs to average loans	0.35 %	0.19 %	0.54 %	0.52 %	0.58 %
Non-performing assets	$69,773	$105,246	$120,946	$164,950	$180,179
Non-performing assets to:					
Total loans plus foreclosed assets	0.73 %	1.14 %	1.51 %	2.03 %	2.14 %
Total assets	0.29	0.46	0.60	0.94	1.11

Consolidated Capital Ratios					
Tier 1 risk-based capital ratio	14.65 %	13.68 %	14.38 %	13.82 %	11.91 %
Total risk-based capital ratio	15.79	15.11	16.24	15.91	14.19
Leverage ratio	8.49	8.28	8.66	8.68	8.50
Average shareholders' equity to average total assets	10.79	11.39	11.70	11.80	11.66

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The following tables set forth unaudited consolidated selected quarterly statement of operations data for the years ended December 31, 2013 and 2012. Dollar amounts are in thousands, except per share data.

	Year Ended December 31, 2013			
	4th Quarter	3rd Quarter	2nd Quarter	1st Quarter
Interest income	$163,869	$160,851	$159,018	$158,762
Interest expense	4,661	5,498	5,837	5,949
Net interest income	159,208	155,353	153,181	152,813
Provision for loan losses	5,899	5,108	3,575	6,000
Non-interest income(1)	78,538	73,991	72,509	77,780
Non-interest expense	154,515	151,823	149,758	155,814
Income before income taxes	77,332	72,413	72,357	68,779
Income taxes	14,761	11,969	12,694	13,591
Net income	62,571	60,444	59,663	55,188
Preferred stock dividends	2,016	2,015	2,688	—
Net income available to common shareholders	$60,555	$58,429	$56,975	$55,188
Net income per common share:				
Basic	$1.00	$0.96	$0.95	$0.91
Diluted	0.99	0.96	0.94	0.91

	Year Ended December 31, 2012			
	4th Quarter	3rd Quarter	2nd Quarter	1st Quarter
Interest income	$160,792	$158,159	$155,796	$156,865
Interest expense	6,387	6,627	6,579	7,158
Net interest income	154,405	151,532	149,217	149,707
Provision for loan losses	4,125	2,500	2,355	1,100
Non-interest income(2)	75,887	71,158	69,763	71,979
Non-interest expense	146,067	144,450	142,536	142,040
Income before income taxes	80,100	75,740	74,089	78,546
Income taxes	19,912	17,071	16,027	17,513
Net income	$60,188	$58,669	$58,062	$61,033
Net income per common share:				
Basic	$0.98	$0.95	$0.94	$0.99
Diluted	0.97	0.95	0.94	0.99

(1) Includes net gains on securities transactions of $1.2 million, $6 thousand and $5 thousand during the fourth, second and first quarters of 2013, respectively, and net losses on securities transactions of $14 thousand during the third quarter of 2013.

(2) Includes net gains on securities transactions of $4.4 million during the fourth quarter of 2012 and $370 thousand during the second quarter of 2012 and net losses on securities transactions of $491 thousand during the first quarter of 2012.

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ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward-Looking Statements and Factors that Could Affect Future Results

Certain statements contained in this Annual Report on Form 10-K that are not statements of historical fact constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 (the "Act"), notwithstanding that such statements are not specifically identified as such. In addition, certain statements may be contained in the Corporation's future filings with the SEC, in press releases, and in oral and written statements made by or with the approval of the Corporation that are not statements of historical fact and constitute forward-looking statements within the meaning of the Act. Examples of forward-looking statements include, but are not limited to: (i) projections of revenues, expenses, income or loss, earnings or loss per share, the payment or nonpayment of dividends, capital structure and other financial items; (ii) statements of plans, objectives and expectations of Cullen/Frost or its management or Board of Directors, including those relating to products or services; (iii) statements of future economic performance; and (iv) statements of assumptions underlying such statements. Words such as "believes", "anticipates", "expects", "intends", "targeted", "continue", "remain", "will", "should", "may" and other similar exp intended to identify forward-looking statements but are not the exclusive means of identifying such statements.

Forward-looking statements involve risks and uncertainties that may cause actual results to differ materially from those in such statements. Factors that could cause actual results to differ from those discussed in the forward-looking statements include, but are not limited to:

- Local, regional, national and international economic conditions and the impact they may have on the Corporation and its customers and the Corporation's assessment of that impact.
- Volatility and disruption in national and international financial markets.
- Government intervention in the U.S. financial system.
- Changes in the mix of loan geographies, sectors and types or the level of non-performing assets and charge-offs.
- Changes in estimates of future reserve requirements based upon the periodic review thereof under relevant regulatory and accounting requirements.
- The effects of and changes in trade and monetary and fiscal policies and laws, including the interest rate policies of the Federal Reserve Board.
- Inflation, interest rate, securities market and monetary fluctuations.
- The effect of changes in laws and regulations (including laws and regulations concerning taxes, banking, securities and insurance) with which the Corporation and its subsidiaries must comply.
- The soundness of other financial institutions.
- Political instability.
- Impairment of the Corporation's goodwill or other intangible assets.
- Acts of God or of war or terrorism.
- The timely development and acceptance of new products and services and perceived overall value of these products and services by users.
- Changes in consumer spending, borrowings and savings habits.
- Changes in the financial performance and/or condition of the Corporation's borrowers.
- Technological changes.
- Acquisitions and integration of acquired businesses.
- The ability to increase market share and control expenses.
- The Corporation's ability to attract and retain qualified employees.
- Changes in the competitive environment in the Corporation's markets and among banking organizations and other financial service providers.
- 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.
- Changes in the reliability of the Corporation's vendors, internal control systems or information systems.

- Changes in the Corporation’s liquidity position.
- Changes in the Corporation’s organization, compensation and benefit plans.
- The costs and effects of legal and regulatory developments, the resolution of legal proceedings or regulatory or other governmental inquiries, the results of regulatory examinations or reviews and the ability to obtain required regulatory approvals.
- Greater than expected costs or difficulties related to the integration of new products and lines of business.
- The Corporation’s success at managing the risks involved in the foregoing items.

Forward-looking statements speak only as of the date on which such statements are made. The Corporation undertakes no obligation to update any forward-looking statement to reflect events or circumstances after the date on which such statement is made, or to reflect the occurrence of unanticipated events.

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Application of Critical Accounting Policies and Accounting Estimates

The accounting and reporting policies followed by the Corporation conform, in all material respects, to accounting principles generally accepted in the United States and to general practices within the financial services industry. The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. While the Corporation bases estimates on historical experience, current information and other factors deemed to be relevant, actual results could differ from those estimates.

The Corporation considers 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 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 Corporation's financial statements.

Accounting policies related to the allowance for loan losses are considered to be critical, as these policies involve considerable subjective judgment and estimation by management. The allowance for loan losses is a reserve established through a provision for loan losses charged to expense, which represents management's best estimate of probable losses that have been incurred within the existing portfolio of loans. The allowance, in the judgment of management, is necessary to reserve for estimated loan losses and risks inherent in the loan portfolio. The Corporation's allowance for loan loss methodology includes allowance allocations calculated in accordance with Accounting Standards Codification (ASC) Topic 310, "Receivables" and allowance allocations calculated in accordance with ASC Topic 450, "Contingencies." The level of the allowance reflects management's continuing evaluation of industry concentrations, specific credit risks, loan loss experience, current loan portfolio quality, present economic, political and regulatory conditions and unidentified losses inherent in the current loan portfolio, as well as trends in the foregoing. Portions of the allowance may be allocated for specific credits; however, the entire allowance is available for any credit that, in management's judgment, should be charged off. While management utilizes its best judgment and information available, the ultimate adequacy of the allowance is dependent upon a variety of factors beyond the Corporation's control, including the performance of the Corporation's loan portfolio, the economy, changes in interest rates and the view of the regulatory authorities toward loan classifications. See the section captioned "Allowance for Loan Losses" elsewhere in this discussion and Note 3 - Loans in the notes to consolidated financial statements included in Item 8. Financial Statements and Supplementary Data elsewhere in this report for further details of the risk factors considered by management in estimating the necessary level of the allowance for loan losses.

Overview

The following discussion and analysis presents the more significant factors affecting the Corporation's financial condition as of December 31, 2013 and 2012 and results of operations for each of the years in the three-year period ended December 31, 2013. This discussion and analysis should be read in conjunction with the Corporation's consolidated financial statements, notes thereto and other financial information appearing elsewhere in this report. The Corporation acquired a Houston-based insurance agency specializing in commercial lines insurance products during 2013, a human resources consulting firm in the Houston market area, with offices in Dallas and Austin, in 2012 and an insurance agency in the San Antonio market area in 2011. All of the Corporation's acquisitions during the reported periods were accounted for as purchase transactions, and as such, their related results of operations are included from the date of acquisition, though none of these acquisitions had a significant impact on the Corporation's financial statements during their respective reporting periods.

Taxable-equivalent adjustments are the result of increasing income from tax-free loans and investments by an amount equal to the taxes that would be paid if the income were fully taxable based on a 35% federal tax rate, thus making tax-exempt yields comparable to taxable asset yields.

Dollar amounts in tables are stated in thousands, except for per share amounts.

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Results of Operations

Net income available to common shareholders totaled $231.1 million, or $3.80 diluted per common share, in 2013 compared to $238.0 million, or $3.86 diluted per common share, in 2012 and $217.5 million, or $3.54 diluted per common share, in 2011.

Selected income statement data, returns on average assets and average equity and dividends per share for the comparable periods were as follows:

	2013	2012	2011
Taxable-equivalent net interest income	$710,850	$668,176	$642,066
Taxable-equivalent adjustment	90,295	63,315	60,290
Net interest income	620,555	604,861	581,776
Provision for loan losses	20,582	10,080	27,445
Non-interest income	302,818	288,787	290,002
Non-interest expense	611,910	575,093	558,098
Income before income taxes	290,881	308,475	286,235
Income taxes	53,015	70,523	68,700
Net income	237,866	237,952	217,535
Preferred stock dividends	6,719	—	—
Net income available to common shareholders	$231,147	$237,952	$217,535
Earnings per common share - basic	$3.82	$3.87	$3.55
Earnings per common share - diluted	3.80	3.86	3.54
Dividends per common share	1.98	1.90	1.83
Return on average assets	1.02 %	1.14 %	1.17 %
Return on average common equity	9.93	10.03	10.01
Average shareholders' equity to average assets	10.79	11.39	11.70

Net income available to common shareholders decreased $6.8 million for 2013 compared to 2012. The decrease was primarily the result of a $36.8 million increase in non-interest expense, a $10.5 million increase in the provision for loan losses and $6.7 million related to preferred stock dividends partly offset by a $17.5 million decrease in income tax expense, a $15.7 million increase in net interest income and a $14.0 million increase in non-interest income. Net income available to common shareholders for 2012 increased $20.4 million, or 9.4%, compared to 2011. The increase was primarily the result of a $23.1 million increase in net interest income and a $17.4 million decrease in the provision for loan losses partly offset by $17.0 million increase in non-interest expense, a $1.8 million increase in income tax expense and a $1.2 million decrease in non-interest income.

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

Net Interest Income

Net interest income is the difference between interest income on earning assets, such as loans and securities, and interest expense on liabilities, such as deposits and borrowings, which are used to fund those assets. Net interest income is the Corporation’s largest source of revenue, representing 67.2% of total revenue during 2013. Net interest margin is the ratio of taxable-equivalent net interest income to average earning assets for the period. The level of interest rates and the volume and mix of earning assets and interest-bearing liabilities impact net interest income and net interest margin.

The Federal Reserve influences the general market rates of interest, including the deposit and loan rates offered by many financial institutions. The Corporation’s loan portfolio is significantly affected by changes in the prime interest rate. The prime interest rate, which is the rate offered on loans to borrowers with strong credit, remained at 3.25% during 2013, 2012 and 2011. The Corporation’s loan portfolio is also impacted, to a lesser extent, by changes in the London Interbank Offered Rate (LIBOR). At December 31, 2013, the one-month and three-month U.S. dollar LIBOR rates were 0.17% and 0.25%, respectively, while at December 31, 2012, the one-month and three-month U.S. dollar LIBOR rates were 0.21% and 0.31%, respectively. The intended federal funds rate, which is the cost of immediately available overnight funds, remained at zero to 0.25% during 2013, 2012 and 2011.

The Corporation's balance sheet has historically been asset sensitive, meaning that earning assets generally reprice more quickly than interest-bearing liabilities. Therefore, the Corporation's net interest margin was likely to increase in sustained periods of rising interest rates and decrease in sustained periods of declining interest rates. During the fourth quarter of 2007, in an effort to make the Corporation's balance sheet less sensitive to changes in interest rates, the Corporation entered into various interest rate swaps which effectively converted certain variable-rate loans into fixed-rate instruments for a period of time. During the fourth quarter of 2008, the Corporation also entered into an interest rate swap which effectively converted variable-rate debt into fixed-rate debt for a period of

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time. As a result of these actions, the Corporation’s balance sheet was more interest-rate neutral and changes in interest rates had a less significant impact on the Corporation’s net interest margin than would have otherwise been the case. During the fourth quarter of 2009, a portion of the interest rate swaps on variable-rate loans were terminated, while the remaining interest rate swaps on variable-rate loans were terminated during the fourth quarter of 2010. These actions increased the asset sensitivity of the Corporation’s balance sheet. The deferred accumulated gain applicable to the settled interest rate contracts included in accumulated other comprehensive income totaled $30.6 million ($19.9 million on an after-tax basis) at December 31, 2013. The remaining deferred gain of $30.6 million ($19.9 million on an after-tax basis) will be recognized ratably in interest income through October 2014. See Note 15 - Derivative Financial Instruments in the accompanying notes to consolidated financial statements included elsewhere in this report for additional information related to these interest rate swaps.

The Corporation is primarily funded by core deposits, with non-interest-bearing demand deposits historically being a significant source of funds. This lower-cost funding base is expected to have a positive impact on the Corporation’s net interest income and net interest margin in a rising interest rate environment. The Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") repealed the federal prohibition on the payment of interest on demand deposits, thereby permitting depository institutions to pay interest on business transaction and other accounts beginning July 21, 2011. Although the ultimate impact of this legislation on the Corporation has not yet been determined, the Corporation may begin to incur interest costs associated with demand deposits in the future as market conditions warrant. See Item 7A. Quantitative and Qualitative Disclosures About Market Risk elsewhere in this report for information about the expected impact of this legislation on the Corporation’s sensitivity to interest rates. Further analysis of the components of the Corporation’s net interest margin is presented below.

The following table presents the changes in taxable-equivalent net interest income and identifies the changes due to differences in the average volume of 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. The Corporation’s consolidated average balance sheets along with an analysis of taxable-equivalent net interest income are presented in Item 8. Financial Statements and Supplementary Data of this report.

	2013 vs. 2012 Increase (Decrease) Due to Change in			2012 vs. 2011 Increase (Decrease) Due to Change in		
	Rate	Volume	Total	Rate	Volume	Total
Interest-bearing deposits	$(171)	$3,155	$2,984	$449	$(2,506)	$(2,057)
Federal funds sold and resell agreements	16	(38)	(22)	(1)	44	43
Securities:						
Taxable	(11,862)	(22,697)	(34,559)	(55,750)	61,110	5,360
Tax-exempt	(23,392)	79,027	55,635	(6,268)	10,737	4,469
Loans, net of unearned discounts	(22,518)	36,348	13,830	(16,472)	20,277	3,805
Total earning assets	(57,927)	95,795	37,868	(78,042)	89,662	11,620
Savings and interest checking	(449)	152	(297)	(840)	343	(497)
Money market deposit accounts	(3,565)	1,571	(1,994)	(3,360)	1,114	(2,246)
Time accounts	(1,131)	(184)	(1,315)	(783)	(449)	(1,232)
Public funds	(107)	73	(34)	(79)	(26)	(105)
Federal funds purchased and repurchase agreements	—	(19)	(19)	(176)	4	(172)
Junior subordinated deferrable interest debentures	(380)	—	(380)	23	—	23
Subordinated notes payable and other notes	(766)	—	(766)	(6,272)	(3,988)	(10,260)

Federal Home Loan Bank advances	—	(1)	(1)	—	(1)	(1)
Total interest-bearing liabilities	(6,398)	1,592	(4,806)	(11,487)	(3,003)	(14,490)
Net change	$(51,529)	$94,203	$42,674	$(66,555)	$92,665	$26,110

Taxable-equivalent net interest income for 2013 increased $42.7 million, or 6.4%, compared to 2012. The increase primarily related to an increase in the average volume of interest-earning assets partly offset by a decrease in the net interest margin. The average volume of interest-earning assets for 2013 increased $2.0 billion or 10.4% compared to 2012. The net interest margin decreased 18 basis points from 3.59% during 2012 to 3.41% during 2013. The decrease in the net interest margin was partly due to an increase in the relative proportion of average interest-earning assets invested in lower-yielding, interest bearing deposits during 2013 compared to 2012 while the relative proportion of average interest-earning assets invested in higher-yielding securities and loans decreased. The net interest margin was also negatively impacted by a decrease in the average yield on loans. The net interest margin was positively impacted by

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an increase in the average yield on securities which resulted from an increase in the relative proportion of higher-yielding tax-exempt municipal securities relative to lower-yielding taxable securities. These items are more fully discussed below. The average yield on interest-earning assets decreased 21 basis points to 3.52% during 2013 from 3.73% during 2012 while the average cost of funds decreased 6 basis points from 0.24% during 2012 to 0.18% during 2013. The average yield on interest-earning assets is primarily impacted by changes in market interest rates as well as changes in the volume and relative mix of interest-earning assets. As stated above, market interest rates have remained at historically low levels during the reported periods. The effect of lower average market interest rates during the reported periods on the average yield on average interest-earning assets was partly limited by the aforementioned interest rate swaps on variable-rate loans.

Taxable-equivalent net interest income for 2012 increased $26.1 million, or 4.1%, compared to 2011. The increase primarily resulted from an increase in the average volume of interest-earning assets partly offset by a decrease in the net interest margin. The average volume of interest-earning assets for 2012 increased $2.2 billion, or 13.4%, compared to 2011. The net interest margin decreased 29 basis points from 3.88% during 2011 to 3.59% during 2012. The decrease in the net interest margin was partly due to an increase in the relative proportion of average interest-earning assets invested in lower-yielding, taxable securities during 2012 compared to 2011 while the relative proportion of average interest-earning assets invested in higher-yielding loans decreased. The impact of this shift was partly mitigated by a decrease in the relative proportion of average interest-earning assets invested in lower-yielding interest bearing deposits. The net interest margin was also negatively impacted by a decrease in the average yield on securities. The average yield on interest-earning assets decreased 40 basis points from 4.13% during 2011 to 3.73% during 2012 while the average cost of funds decreased 16 basis points from 0.40% during 2011 to 0.24% during 2012.

The average volume of loans increased $772.8 million, or 9.1%, in 2013 compared to 2012 and increased $413.9 million, or 5.1%, in 2012 compared to 2011. Loans made up approximately 44.0% of average interest-earning assets during 2013 compared to 44.5% during 2012 and 48.0% in 2011. The average yield on loans was 4.56% during 2013 compared to 4.82% during 2012 and 5.02% during 2011. Loans generally have significantly higher yields compared to securities, interest-bearing deposits and federal funds sold and resell agreements and, as such, have a more positive effect on the net interest margin.

The average volume of securities did not significantly fluctuate during 2013 compared to 2012 and increased $2.7 billion, or 44.0%, in 2012 compared to 2011. Securities made up approximately 42.4% of average interest-earning assets in 2013 compared to 47.0% in 2012 and 37.0% in 2011. The average yield on securities was 3.48% in 2013 compared to 3.31% in 2012 and 4.57% in 2011. Despite a significant decrease in market rates for investment securities during 2013, the average yield on securities increased 17 basis points during 2013 compared to 2012 as the Corporation increased the relative proportion of investments held in higher-yielding, tax-exempt municipal securities. The relative proportion of higher-yielding, tax-exempt municipal securities to total average securities totaled 40.7% in 2013 compared to 27.4% in 2012 and 35.2% in 2011. The average yield on taxable securities was 1.90% in 2013 compared to 2.10% in 2012 and 3.27% in 2011, while the average taxable-equivalent yield on tax-exempt securities was 5.75% in 2013 compared to 6.68% in 2012 and 6.97% in 2011.

Average federal funds sold, resell agreements and interest-bearing deposits during 2013 increased $1.3 billion, or 77.6%, compared to 2012 and decreased $899.1 million, or 35.8%, in 2012 compared to 2011. Federal funds sold, resell agreements and interest-bearing deposits made up approximately 13.7% of average interest-earning assets in 2013 compared to approximately 8.5% in 2012 and 15.0% in 2011. The combined average yield on federal funds sold, resell agreements and interest-bearing deposits was 0.26% in 2013 compared to 0.27% in 2012 and 0.26% in 2011. The increase in average federal funds sold, resell agreements and interest bearing deposits compared to 2012 was primarily related to excess liquidity from deposit growth. The decrease in federal funds sold, resell agreements and interest-bearing deposits during 2012 compared to 2011 was due to the reinvestment of funds into higher-yielding securities and loans.

Average deposits increased $2.0 billion, or 11.4%, in 2013 compared to 2012 and $2.1 billion, or 13.6%, in 2012 compared to 2011. Average interest-bearing deposits increased $1.3 billion in 2013 compared to 2012 and $786.5 million in 2012 compared to 2011, while average non-interest-bearing deposits increased $635.8 million in 2013 compared to 2012 and $1.3 billion in 2012 compared to 2011. The ratio of average interest-bearing deposits to total average deposits was 60.3% in 2013 compared to 59.4% in 2012 and 62.3% in 2011. The average cost of interest-bearing deposits and total deposits was 0.12% and 0.08% in 2013 compared to 0.18% and 0.10% in 2012 and 0.23% and 0.15% in 2011. The decrease in the average cost of interest-bearing deposits during the comparable periods was primarily the result of decreases in interest rates offered on certain deposit products due to decreases in average market interest rates and decreases in renewal interest rates on maturing certificates of deposit given the current low interest rate environment. Additionally, the relative proportion of higher-cost certificates of deposit to total average interest-bearing deposits decreased to 8.4% in 2013 from 10.0% in 2012 and 11.9% in 2011.

The Corporation’s net interest spread, which represents the difference between the average rate earned on earning assets and the average rate paid on interest-bearing liabilities, was 3.34% in 2013 compared to 3.49% in 2012 and 3.73% in 2011. The net interest spread, as well as the net interest margin, will be impacted by future changes in short-term and long-term interest rate levels, as well as the impact from the competitive environment. A discussion of the effects of changing interest rates on net interest income is set forth in Item 7A. Quantitative and Qualitative Disclosures About Market Risk included elsewhere in this report.

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The Corporation's hedging policies permit the use of various derivative financial instruments, including interest rate swaps, swaptions, caps and floors, to manage exposure to changes in interest rates. Details of the Corporation's derivatives and hedging activities are set forth in Note 15 - Derivative Financial Instruments in the accompanying notes to consolidated financial statements included elsewhere in this report. Information regarding the impact of fluctuations in interest rates on the Corporation's derivative financial instruments is set forth in Item 7A. Quantitative and Qualitative Disclosures About Market Risk included elsewhere in this report.

Provision for Loan Losses

The provision for loan losses is determined by management as the amount to be added to the allowance for loan losses after net charge-offs have been deducted to bring the allowance to a level which, in management's best estimate, is necessary to absorb probable losses within the existing loan portfolio. The provision for loan losses totaled $20.6 million in 2013 compared to $10.1 million in 2012 and $27.4 million in 2011. See the section captioned "Allowance for Loan Losses" elsewhere in this discussion for further analysis of the provision for loan losses.

Non-Interest Income

The components of non-interest income were as follows:

	2013	2012	2011
Trust and investment management fees	$91,375	$83,317	$78,297
Service charges on deposit accounts	81,432	83,392	86,125
Insurance commissions and fees	43,140	39,948	35,421
Interchange and debit card transaction fees	16,979	16,933	29,625
Other charges, commissions and fees	34,185	30,180	27,750
Net gain (loss) on securities transactions	1,176	4,314	6,414
Other	34,531	30,703	26,370
Total	$302,818	$288,787	$290,002

Total non-interest income for 2013 increased $14.0 million, or 4.9%, compared to 2012 while total non-interest income for 2012 decreased $1.2 million, or 0.4%, compared to 2011. Changes in the various components of non-interest income are discussed in more detail below.

Trust and Investment Management Fees. Trust and investment management fee income for 2013 increased $8.1 million, or 9.7%, compared to 2012 while trust and investment management fee income for 2012 increased $5.0 million, or 6.4%, compared to 2011. Trust investment fees are the most significant component of trust and investment management fees, making up approximately 68%, 66% and 68% of total trust and investment management fees in 2013, 2012 and 2011, respectively. Investment and other custodial account fees are generally based on the market value of assets within a trust account. Volatility in the equity and bond markets impacts the market value of trust assets and the related investment fees.

The increase in trust and investment management fee income during 2013 compared to 2012 was primarily the result of an increase in trust investment fees (up $7.1 million), oil and gas fees (up $757 thousand) and securities lending income (up $620 thousand) partly offset by a decrease in estate fees (down $532 thousand). The increase in trust and investment management fee income during 2012 compared to 2011 was primarily the result of an increase in trust investment fees (up $1.8 million), oil and gas trust management fees (up $846 thousand), custody fees (up $777 thousand), securities lending income (up $623 thousand), estate fees (up $524 thousand) and mutual fund and investment management fees (up $294 thousand). The increases in trust investment fees and custody fees were partly due to higher average equity valuations during 2013 compared to 2012 and 2012 compared to 2011, a change in the fee schedule beginning in the fourth quarter of 2013 and increases in the number of accounts during the comparable periods. The increases in securities lending income were partly related to new business and increased loan spreads. The increases in oil and gas trust management fees were partly related to increased production and new lease bonus fees. Estate fees are transactional in nature and can vary from period to period.

At December 31, 2013, trust assets, including both managed assets and custody assets, were primarily composed of equity securities (46.0% of trust assets), fixed income securities (39.3% of trust assets) and cash equivalents (9.3% of trust assets). The estimated fair value of trust assets was $28.4 billion (including managed assets of $11.9 billion and custody assets of $16.5 billion) at December 31, 2013 compared to $26.2 billion (including managed assets of

$10.9 billion and custody assets of $15.3 billion) at December 31, 2012 and $25.2 billion (including managed assets of $10.3 billion and custody assets of $14.9 billion) at December 31, 2011.
Service Charges on Deposit Accounts. Service charges on deposit accounts for 2013 decreased $2.0 million, or 2.4%, compared to 2012. The decrease was primarily due to decreases in overdraft/insufficient funds charges on consumer accounts (down $1.2 million) and a decrease in service charges on commercial accounts (down $943 thousand). Service charges on deposit accounts for 2012 decreased

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$2.7 million, or 3.2%, compared to 2011. The decrease was primarily due to a decrease in service charges on commercial accounts (down $2.1 million) and decreases in overdraft/insufficient funds charges on both consumer and commercial accounts (down $787 thousand). The decreases in service charges on commercial accounts during the comparable periods were partly related to fluctuations in service volumes for billable services. Overdraft/insufficient funds charges totaled $33.0 million during 2013 compared to $34.1 million during 2012 and $34.9 million in 2011. Overdraft/insufficient funds charges included $25.8 million, $27.0 million and $27.7 million related to consumer accounts during 2013, 2012 and 2011, respectively, and $7.2 million, $7.1 million and $7.2 million related to commercial accounts during 2013, 2012 and 2011, respectively.

Insurance Commissions and Fees. Insurance commissions and fees for 2013 increased $3.2 million, or 8.0%, compared to 2012 and increased $4.5 million, or 12.8%, in 2012 compared to 2011. The increases were primarily related to increases in commission income (up $3.2 million in 2013 compared to 2012 and $4.6 million in 2012 compared to 2011), in large part due to an increase in employee benefit commissions and fees. The increase in employee benefit commissions and fees in 2013 compared to 2012 was partly related to customers electing to early renew policies as a result of the Affordable Care Act. The increase in employee benefit commissions and fees in 2012 compared to 2011 was partly related to the acquisitions of Clark Benefit Group during the second quarter of 2011 and Stone Partners, Inc. during the first quarter of 2012. The increases in commission income were also partly related to increases in commercial lines and personal lines property and casualty commissions resulting from normal variation in the market demand for insurance products and rate increases.

Insurance commissions and fees include contingent commissions which totaled $3.8 million in each year for 2013, 2012 and 2011. Contingent commissions primarily consist of amounts received from various property and casualty insurance carriers related to the loss performance of insurance policies previously placed. Such commissions are seasonal in nature and are mostly received during the first quarter of each year. These commissions totaled $2.2 million in 2013, $2.1 million in 2012 and $2.2 million in 2011. Contingent commissions also include amounts received from various benefit plan insurance companies related to the volume of business generated and/or the subsequent retention of such business. These commissions totaled $1.6 million in 2013, $1.7 million in 2012 and $1.6 million in 2011.

Interchange and Debit Card Transaction Fees. Interchange and debit card transaction fees consist of income from check card usage, point of sale income from PIN-based debit card transactions and ATM service fees. Interchange and debit card transaction fees for the year ended December 31, 2013 did not significantly fluctuate compared to 2012 and decreased $12.7 million in 2012 compared to 2011. Income from debit card transactions totaled approximately $14.7 million in 2013 compared to $14.1 million in 2012 and $26.6 million in 2011. Income from ATM service fees totaled approximately $2.3 million in 2013 compared to $2.8 million in 2012 and $3.0 million in 2011. The decrease in income from debit card transactions when compared to 2011 was primarily related to new rules, effective as of October 1, 2011, that significantly reduced the interchange fees that may be charged, as further discussed below.

Federal Reserve rules applicable to financial institutions that have assets of $10 billion or more provide that the maximum permissible interchange fee for an electronic debit transaction is the sum of 21 cents per transaction and 5 basis points multiplied by the value of the transaction. An upward adjustment of no more than 1 cent to an issuer's debit card interchange fee is allowed if the card issuer develops and implements policies and procedures reasonably designed to achieve certain fraud-prevention standards. In July 2013, a federal judge vacated the Federal Reserve's rule setting debit transaction interchange fees under the Dodd-Frank Act, on the basis that the rule violated the intent of the law. The ruling states that the only incremental costs, such as those related to authorization, clearing and settlement, incurred by the issuer for a particular debit transaction should be allowed and the Federal Reserve should not have considered fixed costs, fraud prevention costs, fraud losses and network fees when determining the fee cap. The judge's ruling was stayed in September 2013 pending appeal by the Federal Reserve. The current rate cap is to remain in effect until the Federal Reserve revises its rule, if it is ultimately required to do so. In October 2013, the Federal Reserve filed an appeal against the court's ruling with oral arguments beginning in January 2014. Because of the uncertainty as to the outcome of the pending appeal and any future rulemaking by the Federal Reserve, the Corporation cannot provide any assurance as to the ultimate impact of any rule change on the amount of interchange and debit card transaction fees reported in future periods.

Other Charges, Commissions and Fees. Other charges, commissions and fees for 2013 increased $4.0 million, or 13.3%, compared to 2012. The increase in other charges, commissions and fees during 2013 included increases in income related to the sale of annuities (up $1.8 million), income from the sale of mutual funds (up $1.5 million), unused balance fees on loan commitments (up $541 thousand), loan processing fees (up $518 thousand) and referral fees from the Corporation's merchant services payment processor (up $343 thousand). These increases were partly offset by decreases in other service charges (down $349 thousand), investment banking fees related to corporate advisory services (down $219 thousand) and letter of credit fees (down $166 thousand).

Other charges, commissions and fees for 2012 increased $2.4 million, or 8.8%, compared to 2011. The increase in other charges, commissions and fees during 2012 included increases in human resources consulting revenues, primarily related to the acquisition of Stone Partners, Inc. (up $1.7 million), referral fees from the Corporation’s merchant services payment processor (up $791 thousand), an increase in unused balance fees on loan commitments (up $561 thousand), service charges on funds transfers (up $560 thousand) and income from the sale of mutual funds (up $518 thousand), among other things. These increases were partly offset by decreases in income related to investment banking fees related to corporate advisory services (down $1.4 million) and the sale of annuities (down $605 thousand). Investment banking fees related to corporate advisory services are transactional in nature and can vary significantly from year to year.

Net Gain/Loss on Securities Transactions. During 2013, the Corporation realized a net gain of $1.2 million on the sale of available-for-sale securities. During 2013, the Corporation sold certain municipal securities with an amortized cost totaling $29.1 million and realized a net gain of $1.2 million on those sales. The sales were made for the purpose of divesting of certain securities issued by municipalities outside of Texas. The Corporation also sold U.S. Treasury securities with an amortized cost totaling $10.0 billion and realized a net loss of $2 thousand on those sales. These securities were primarily purchased during 2013 and subsequently sold in connection with the Corporation's tax planning strategies related to the Texas franchise tax. The gross proceeds from the sales of these securities outside of Texas are included in total revenues/receipts from all sources reported for Texas franchise tax purposes, which results in a reduction in the overall percentage of revenues/receipts apportioned to Texas and subjected to taxation under the Texas franchise tax.

During 2012, the Corporation realized a net gain of $4.3 million on the sale of available-for-sale securities. During January 2012, the Corporation purchased $996.4 million of U.S. Treasury securities utilizing excess liquidity as a defensive strategy to lock in the yield on those funds in case the Federal Reserve lowered the rate paid on funds deposited in the Federal Reserve account. Shortly thereafter, U.S. Treasury prices rallied and the Corporation sold the securities, realizing a $2.1 million gain, and concurrently purchased $998.4 million of U.S. Treasury securities having a shorter term to maturity. In March 2012, U.S. Treasury yields increased and the Corporation sold the aforementioned position in U.S. Treasury securities and recognized a $2.6 million loss. The proceeds were concurrently reinvested in U.S. Treasury securities that had a similar yield to the original, longer-term position purchased in January 2012, but with a shorter term to maturity. During the second quarter of 2012, the Corporation sold a municipal security with an amortized cost totaling $5.6 million and realized a $367 thousand gain on the sale. During the fourth quarter of 2012, the Corporation sold U.S. Treasury securities with an amortized cost totaling $595.6 million and realized a $4.4 million gain on the sale. The Corporation purchased the securities during the fourth quarter of 2012. Shortly thereafter, U.S. Treasury prices rallied and the Corporation sold the securities to capitalize on the gain as management believed the increase in U.S. Treasury prices would be temporary. During 2012, the Corporation also sold available-for-sale securities with an amortized cost totaling $14.0 billion and realized a net gain of $2 thousand on those sales. These securities were primarily purchased during 2012 and subsequently sold in connection with the Corporation’s aforementioned tax planning strategies related to the Texas franchise tax.

During 2011, the Corporation sold available-for-sale securities with an amortized cost totaling $5.6 billion and realized a net gain of $6.4 million on those sales. With the exception of the sales during the third quarter of 2011 discussed below, these securities were primarily purchased during 2011 and subsequently sold in connection with the Corporation’s aforementioned tax planning strategy related to the Texas franchise tax. During the third quarter of 2011, the Corporation sold available-for-sale securities with an amortized cost totaling $32.6 million and realized a net gain of $6.4 million on those sales. Many of these were longer-duration municipal securities.

Other Non-Interest Income. Other non-interest income for 2013 increased $3.8 million, or 12.5%, compared to 2012. The increase during 2013 was primarily related to increases in gains on the sale of assets/foreclosed assets (up $5.2 million), mineral interest income (up $950 thousand), income from municipal bond underwriting discounts/fees (up $935 thousand), sundry income from various miscellaneous items (up $790 thousand) and income from customer foreign currency transactions (up approximately $630 thousand). The increase from the aforementioned items was partly offset by a decrease in income from securities trading and customer derivative transactions (down $3.3 million) and earnings on the cash surrender value of life insurance policies (down $935 thousand). During the first quarter of 2013, the Corporation realized a $5.6 million gain related to the sale of a building and parking garage. The Corporation leased back portions of the building through the third quarter of 2013 and the first quarter of 2015. As a result, a portion of the gain was deferred and only $4.8 million of the total $5.6 million gain has been recognized during 2013. The remaining deferred portion of the gain, which totaled $768 thousand, at December 31, 2013 will be recognized ratably over the remaining lease period. Mineral interest income is related to bonus, rental and shut-in payments and oil and gas royalties received from severed mineral interests on property owned by Main Plaza Corporation, a wholly owned non-banking subsidiary of the Corporation. During 2013, sundry income from various miscellaneous items included a $1.8 million reversal of an accrual related to an acquisition contingency, $1.8 million related to the recovery of interest previously charged-off in a prior year, $553 thousand related to a refund of prior deposit insurance premiums and $312 thousand related to a distribution from a limited partnership investment. The decrease in income from securities trading and customer derivative transactions during 2013 was primarily related to a decrease in customer interest rate swap transaction fees.

Other non-interest income for 2012 increased $4.3 million, or 16.4% compared to 2011. The increase was primarily related to an increase in sundry income from various miscellaneous items (up $2.0 million), mineral interest income (up $1.6 million) and income from securities trading and customer derivative activities (up $1.1 million) partly offset by a decrease in gains on the sale of assets/foreclosed assets (down $982 thousand). The increase in sundry income from various miscellaneous items was partly related to proceeds realized in a settlement totaling $1.4 million and the reversal of a prior contingency accrual totaling $765 thousand. Mineral interest income was related to bonus, rental and shut-in payments and oil and gas royalties received from severed mineral interests on property owned by Main Plaza Corporation. The increase in income from securities trading and customer derivative activities was primarily related to an increase in customer interest rate swap transaction fees.

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Non-Interest Expense

The components of non-interest expense were as follows:

	2013	2012	2011
Salaries and wages	$273,692	$258,752	$252,028
Employee benefits	62,407	57,635	52,939
Net occupancy	50,468	48,975	46,968
Furniture and equipment	58,443	55,279	51,469
Deposit insurance	11,682	11,087	12,714
Intangible amortization	3,141	3,896	4,387
Other	152,077	139,469	137,593
Total	$611,910	$575,093	$558,098

Total non-interest expense for 2013 increased $36.8 million, or 6.4%, compared to 2012 while total non-interest expense for 2012 increased $17.0 million, or 3.0%, compared to 2011. Changes in the various components of non-interest expense are discussed below.

Salaries and Wages. Salaries and wages increased $14.9 million, or 5.8%, in 2013 compared to 2012 and increased $6.7 million, or 2.7%, in 2012 compared to 2011. The increases during the comparable periods were related to increases in the number of employees, normal annual merit and market increases, increased commissions related to higher insurance revenues and increased incentive compensation expense partly offset by decreases in stock-based compensation expense and increases in cost deferrals related to lending activity.

Employee Benefits. Employee benefits expense for 2013 increased $4.8 million, or 8.3%, compared to 2012. The increase during 2013 was primarily related to increases in expenses related to the Corporation’s 401(k) and profit sharing plans (up $690 thousand and $2.1 million, respectively), payroll taxes (up $1.4 million) and medical insurance expense (up $738 thousand) partly offset by a decrease in expenses related to the Corporation’s defined benefit retirement plans (down $286 thousand).

Employee benefits expense for 2012 increased $4.7 million, or 8.9%, compared to 2011. The increase was primarily related to increases in expenses related to the Corporation’s defined benefit retirement plans (up $3.5 million), medical insurance expense (up $2.1 million) and expenses related to the Corporation’s 401(k) plan (up $652 thousand) partly offset by a decrease in expenses related to the Corporation’s profit sharing plans (down $2.6 million). The decrease in expenses related to the Corporation’s profit sharing plans was related to the termination of the transition contributions that were only applicable to plan years before 2012.

The Corporation’s defined benefit retirement and restoration plans were frozen effective as of December 31, 2001 and were replaced by the profit sharing plan. Management believes these actions help reduce the volatility in retirement plan expense. However, the Corporation still has funding obligations related to the defined benefit and restoration plans and could recognize retirement expense related to these plans in future years, which would be dependent on the return earned on plan assets, the level of interest rates and employee turnover. The Corporation recognized net expense related to the defined benefit retirement and restoration plans totaling $2.8 million in 2013 compared to net expense of $3.1 million in 2012 and a net benefit of $412 thousand in 2011. Future expense/benefits related to these plans is dependent upon a variety of factors, including the actual return on plan assets. The increase in expense related to the Corporation’s defined benefit retirement plan during 2012 compared to 2011 was partly related to a decrease in the return on plan assets.

For additional information related to the Corporation’s employee benefit plans, see Note 11 - Employee Benefit Plans in the accompanying notes to consolidated financial statements included elsewhere in this report.

Net Occupancy. Net occupancy expense for 2013 increased $1.5 million, or 3.0%, compared to 2012. The increase was primarily related to increases in lease expense (up $1.5 million), a decrease in rental income (down $410 thousand), an increase in depreciation on leasehold improvements (up $383 thousand) and a decrease in parking garage income (down $288 thousand). These items were partly offset by a decrease in legal and other professional services expense (down $207 thousand), building depreciation (down $199 thousand) and utilities expense (down $195 thousand), among other things.

Net occupancy expense for 2012 increased $2.0 million, or 4.3%, compared to 2011. The increase was primarily related to increases in lease expense (up $1.1 million), building maintenance and repair expense (up $460 thousand) and depreciation expense related to leasehold improvements (up $371 thousand), among other things. These increases were partly offset by a decrease in utilities expense (down $303 thousand).

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Furniture and Equipment. Furniture and equipment expense for 2013 increased $3.2 million, or 5.7%, compared to 2012. The increase was primarily related to increases in software maintenance (up $1.1 million), software amortization (up $771 thousand), repairs expense (up $455 thousand), furniture and fixtures depreciation (up $420 thousand) and equipment rental expense (up $312 thousand).

Furniture and equipment expense for 2012 increased $3.8 million, or 7.4%, compared to 2011. The increase was primarily related to increases in software maintenance (up $2.1 million), service contracts expense (up $1.2 million) and software amortization (up $589 thousand).

Deposit Insurance. Deposit insurance expense totaled $11.7 million in 2013 compared to $11.1 million in 2012 and $12.7 million in 2011. The increase in deposit insurance expense during 2013 compared to 2012 was primarily related to an increase in assets, partly offset by the impact of a decrease in the assessment rate. The decrease in deposit insurance expense during 2012 compared to 2011 was primarily related to a change in the deposit insurance assessment base and a change in the method by which the assessment rate is determined for large financial institutions, which became effective on April 1, 2011.

Intangible Amortization. Intangible amortization is primarily related to core deposit intangibles and, to a lesser extent, intangibles related to customer relationships and non-compete agreements. Intangible amortization totaled $3.1 million in 2013 compared to $3.9 million in 2012 and $4.4 million in 2011. The decrease in amortization expense during the comparable years was primarily the result of the completion of amortization of certain intangible assets, as well as a reduction in the annual amortization rate of certain intangible assets as the Corporation uses an accelerated amortization approach which results in higher amortization rates during the earlier years of the useful lives of intangible assets. The decreases in amortization were partly offset by the additional amortization related to intangible assets recorded in connection with the acquisitions of Kolkhorst Insurance Agency, Inc. on November 1, 2013, Stone Partners Inc. on January 1, 2012 and Clark Benefit Group on May 1, 2011. See Note 5 - Goodwill and Other Intangible Assets in the accompanying notes to consolidated financial statements included elsewhere in this report.

Other Non-Interest Expense. Other non-interest expense for 2013 increased $12.6 million, or 9.0%, compared to 2012. The increase during 2013 was primarily related to the write-down of certain land and other assets totaling $7.2 million during the first quarter of 2013. Approximately $6.2 million of this amount was related to the write-down of certain long-term bank-owned property in downtown San Antonio that was made available for sale. Additionally, other components of other non-interest expense with significant increases during 2013 included professional services expense (up $3.8 million), ATM expense (up $3.4 million), check card expense (up $1.6 million) and travel, meals and entertainment expense (up $522 thousand). The increases in the aforementioned items were partly offset by decreases in sundry losses from various miscellaneous items (down $1.0 million), advertising/promotions/public relations expense (down $962 thousand), amortization of net deferred costs related to loan commitments (down $665 thousand) and regulatory examination fees (down $373 thousand). In 2013, professional services expense included $1.3 million and travel, meals and entertainment expense included $130 thousand in costs incurred associated with the pending acquisition of WNB Bancshares. See Note 21 - Pending Acquisition in the accompanying notes to consolidated financial statements included elsewhere in this report. The increase in ATM expense was related to a branding arrangement entered into in 2012 that more than doubled the number of ATM machines, as further discussed below. Advertising/promotions expenses were higher in 2012 in part due to an expanded marketing campaign that began in 2011.

Other non-interest expense for 2012 increased $1.9 million, or 1.4%, compared to 2011. Components of other non-interest expense with significant increases during 2012 included professional services expense (up $2.5 million); travel, meals and entertainment (up $1.6 million); advertising/promotions/public relations expense (up $1.8 million); amortization of net deferred costs related to loan commitments (up $925 thousand); and check card expense (up $901 thousand). The increase in advertising/promotions/public relations expense was partly related to the Corporation’s branding arrangement to be the exclusive cash-machine provider for CST Brands, Inc. Corner Stores in Texas. The increase in the amortization of net deferred costs related to loan commitments was primarily related to an increase in commitments outstanding. The increases in the aforementioned items were partly offset by decreases in donation expense (down $2.5 million), sundry losses from various miscellaneous items (down $2.0 million), losses on the sale/write-down of assets/foreclosed assets (down $994 thousand) examination fees (down $642 thousand), property taxes on foreclosed assets (down $623 thousand) and sub-advisor investment management fees related to Frost Investment Advisors, LLC, (down $459 thousand).

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Results of Segment Operations

The Corporation's operations are managed along two operating segments: Banking and Frost Wealth Advisors. A description of each business and the methodologies used to measure financial performance is described in Note 18 - Operating Segments in the accompanying notes to consolidated financial statements included elsewhere in this report. Net income (loss) by operating segment is presented below:

	2013	2012	2011
Banking	$226,783	$229,312	$216,419
Frost Wealth Advisors	15,653	14,198	9,050
Non-Banks	(4,570)	(5,558)	(7,934)
Consolidated net income	$237,866	$237,952	$217,535

Banking

Net income for 2013 decreased $2.5 million, or 1.1%, compared to 2012. The decrease was primarily the result of a $28.6 million increase in non-interest expense and a $10.5 million increase in the provision for loan losses partly offset by a $18.3 million decrease in income tax expense, a $16.0 million increase in net interest income and a $2.3 million increase in non-interest income. Net income for 2012 increased $12.9 million, or 6.0%, compared to 2011. The increase was primarily the result of a $17.4 million decrease in the provision for loan losses, a $17.2 million increase in net interest income and a $2.2 million decrease in income tax expense partly offset by a $16.2 million increase in non-interest expense and a $7.8 million decrease in non-interest income.

Net interest income for 2013 increased $16.0 million, or 2.6%, compared to 2012 while net interest income for 2012 increased $17.2 million, or 2.9%, compared to 2011. The increases primarily resulted from increases in the average volume of interest-earning assets partly offset by decreases in the net interest margin. See the analysis of net interest income included in the section captioned "Net Interest Income" included elsewhere in this discussion.

The provision for loan losses for 2013 totaled $20.6 million compared to $10.1 million in 2012 and $27.5 million in 2011. See the analysis of the provision for loan losses included in the section captioned "Allowance for Loan Losses" included elsewhere in this discussion.

Non-interest income for 2013 increased $2.3 million, or 1.2%, compared to 2012. The increase was primarily due to increases in other non-interest income, insurance commissions and fees and other charges, commissions and fees partly offset by a decrease in the net gain on securities transactions and a decrease in service charges on deposits. The increase in other non-interest income was primarily related to a gain realized on the sale of a building and parking garage. The increase in insurance commissions and fees was primarily due to increased commission income in large part due to an increase in employee benefit commissions and fees and, to a lesser extent, increases in commercial lines and personal lines property and casualty commissions resulting from normal variation in the market demand for insurance products and rate increases. The decrease in service charges on deposit accounts was mostly due to a decrease in overdraft/insufficient funds charges on consumer accounts and a decrease in service charges on commercial accounts. See the analysis of these categories of non-interest income included in the section captioned "Non-Interest Income" included elsewhere in this discussion.

Non-interest income for 2012 decreased $7.8 million, or 4.0%, compared to 2011. The decreases were primarily due to decreases in interchange and debit card transaction fees, service charges on deposit accounts and the net gain on securities transactions partly offset by increases in insurance commissions and fees, other charges, commissions and fees and other non-interest income. The decrease in interchange and debit card transaction fees was primarily related to new rules, effective on October 1, 2011, that significantly reduced the interchange fees that may be charged. The decrease in service charges on deposit accounts was related to decreases in service charges on commercial accounts and in overdraft/insufficient funds charges on both consumer and commercial accounts. The increase in insurance commissions was partly due to an increase in employee benefit commissions and fees and an increase in property and casualty commissions. The increase in other charges, commissions and fees was related to increases in human resources consulting revenues, referral fees from the Corporation's merchant services payment processor, unused balance fees on loan commitments and service charges on funds transfers, among other things. The increase in other non-interest income was primarily related to increases in sundry income from various miscellaneous items and income from securities trading and customer derivative activities. See the analysis of these categories of non-interest income included in the section captioned “Non-Interest Income” included elsewhere in this discussion.

Non-interest expense for 2013 increased $28.6 million, or 5.9%, compared to 2012. The increase during 2013 was primarily due to increases in salaries and wages and employee benefits, other non-interest expense, furniture and equipment expense and net occupancy expense. The increase in salaries and wages was primarily related to normal annual merit and market increases, increased commissions related to higher insurance revenues and increased incentive compensation partly offset by a decrease in stock-based compensation expense and an increase in cost deferrals related to lending activity. The increase in employee benefits expense was primarily related to increases in expenses related to the Corporation's 401(k) and profit sharing plans, payroll taxes and medical insurance expense. The

increase in other non-interest expense during 2013 was primarily related to the write-down of certain land and other assets during the first quarter of 2013, the majority of which was related to the write-down of certain long-term bank-owned property in downtown San Antonio that was made available for sale. Other non-interest expense during 2013 was also impacted by increases in professional services expense, ATM expense and overhead cost allocations, among other things. The increase in furniture and equipment expense was primarily due to increases in software maintenance, software amortization, repairs expense, furniture and fixtures depreciation and equipment rental expense. The increase in net occupancy was primarily related to increases in lease expense, a decrease in rental income, an increase in depreciation on leasehold improvements and a decrease in parking garage income. See the analysis of these items included in the section captioned “Non-Interest Expense” included elsewhere in this discussion.
Non-interest expense for 2012 increased $16.2 million, or 3.4%, compared to the 2011. The increase during 2012 was primarily related to increases in salaries and wages, employee benefits, furniture and equipment expense, net occupancy expense and other non-interest expense partly offset by a decrease in deposit insurance expense and intangible amortization. The increase in salaries and wages was primarily related to normal annual merit and market increases, increased commissions related to higher insurance revenues and increased incentive compensation partly offset by a decrease in stock-based compensation expense and an increase in cost deferrals related to lending activity. The increase in employee benefits expense was primarily related to increases in expenses related to the Corporation’s defined benefit retirement and 401(k) plans and medical insurance expense partly offset by a decrease in expense related to the Corporation’s profit sharing plans. The increase in furniture and equipment expense was due to increases in software maintenance, service contract expenses and software amortization. The increase in net occupancy expense was due to increases in lease expense, building maintenance and repair expense and depreciation expense related to leasehold improvements. The increase in other non-interest expense was related to increases in professional services expense, travel/meals and entertainment, advertising/promotions expense and amortization of net deferred costs related to loan commitments, among other things, as well as increases in overhead cost allocations. The decrease in deposit insurance expense was primarily related to a change in the deposit insurance assessment base and a change in the method by which the assessment rate is determined for large financial institutions which became effective on April 1, 2011. See the analysis of these items included in the section captioned “Non-Interest Expense” included elsewhere in this discussion.
Income tax expense for 2013 decreased $18.3 million, or 26.4%, compared to 2012. The decrease was related a decrease in pre-tax net income combined with a decrease in the effective tax rate. Income tax expense for 2012 decreased $2.2 million, or 3.1%, compared to 2011. The decrease was primarily due to the correction, during the third quarter of 2011, of an under-accrual of taxes that resulted from incorrectly deducting premium amortization on municipal securities for federal income tax purposes since 2008. See the section captioned “Income Taxes” included elsewhere in this discussion.
Frost Insurance Agency, which is included in the Banking operating segment, had gross commission revenues of $43.8 million during 2013 compared to $40.6 million in 2012 and $36.0 million in 2011. Insurance commission revenues increased $3.2 million, or 7.9%, during 2013 compared to 2012 and increased $4.6 million, or 12.7%, during 2012 compared to 2011. See the analysis of insurance commissions and fees included in the section captioned “Non-Interest Income” included elsewhere in this discussion. Frost Insurance Agency also had consulting revenues totaling $1.5 million during 2013 and $1.7 million during 2012. Consulting revenues are reported as a component of other charges, commissions and fees and were primarily related to an acquisition during the first quarter of 2012.
Frost Wealth Advisors
Net income for 2013 increased $1.5 million, or 10.2%, compared to 2012. The increase was primarily due to a $11.2 million increase in non-interest income partly offset by a $7.4 million increase in non-interest expense, a $1.4 million decrease in net interest income and a $917 thousand increase in income tax expense. Net income for 2012 increased $5.1 million, or 56.9%, compared to 2011. The increase was primarily due to a $4.9 million increase in non-interest income, a $1.7 million increase in net interest income and a $1.4 million decrease in non-interest expense partly offset by a $2.8 million increase in income tax expense.
Net interest income for 2013 decreased $1.4 million, or 17.8%, compared to 2012. The decrease in net interest income was partly due to a decrease in the funds transfer price received for providing funds. Net interest income for 2012

increased $1.7 million, or 26.7%, compared to 2011. The increase in net interest income was due to an increase in the average volume of funds provided due to an increase in the average volume of Frost Wealth Advisor's repurchase agreements combined with an increase in the funds transfer price received for providing those funds.

Non-interest income for 2013 increased $11.2 million, or 11.6%, compared to 2012. The increase was primarily due to increases in trust and investment management fees (up $8.2 million) and increases in other charges, commissions and fees (up $3.1 million). Non-interest income for 2012 increased $4.9 million, or 5.3%, compared to 2011. The increase was primarily due to increases in trust and investment management fees (up $5.2 million) partly offset by decreases in other charges, commissions and fees (down $228 thousand).

Trust and investment management fee income is the most significant income component for Frost Wealth Advisors. Investment fees are the most significant component of trust and investment management fees, making up approximately 68%, 66% and 68% of total trust and investment management fees in 2013, 2012 and 2011, respectively. Investment and other custodial account fees are generally based on the market value of assets within a trust account. Volatility in the equity and bond markets impacts the market value of trust assets and the related investment fees. The increase in trust and investment management fee income during 2013 compared to 2012

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was primarily the result of an increase in trust investment fees, oil and gas trust management fees and securities lending income. The increase in trust and investment management fee income during 2012 compared to 2011 was primarily the result of an increase in trust investment fees, oil and gas trust management fees, custody fees, securities lending income, estate fees and mutual fund and investment management fees. See the analysis of trust and investment management fees included in the section captioned "Non-Interest Income" included elsewhere in this discussion.

The increase in other charges, commissions and fees during 2013 compared to 2012 was primarily due to an increase in income related to the sale of annuities and mutual funds. The decrease in other charges, commissions and fees during 2012 compared to 2011 was primarily due to a decrease in income related to the sale of annuities partly offset by an increase in income from the sale of mutual funds.

Non-interest expense for 2013 increased $7.4 million, or 8.9%, compared to 2012. The increase was primarily due to an increase in salaries and wages (up $4.3 million), other non-interest expense (up $2.2 million) and employee benefits (up $752 thousand). The increases in salaries and wages were primarily related to normal annual merit and market increases. The increase in other non-interest expense was related to an increase in professional services expense as well as increases in various miscellaneous categories of expense and overhead cost allocation. The increase in employee benefits was related to increased payroll taxes, 401(k) and profit sharing plan expenses and medical insurance expense.

Non-interest expense for 2012 decreased $1.4 million, or 1.6%, compared to 2011. The decrease was primarily due to a decrease in other non-interest expense (down $2.4 million) partly offset by increases in salaries and wages and employee benefits (up $909 thousand on a combined basis). The decrease in other non-interest expense was related to decreases in various overhead cost allocations as well as decreases in sundry losses from various miscellaneous items and sub-advisor investment management fees related to Frost Investment Advisors, LLC, among other things. The increases in salaries and wages and employee benefits were primarily related to normal annual merit and market increases as well as increases in medical insurance and retirement plan expense.

Non-Banks

The Non-Banks segment had a net loss of $4.6 million in 2013, decreasing $988 thousand, or 17.8%, compared to $5.6 million in 2012. The decrease in the net loss during 2013 was primarily due to a decrease in net interest expense (down $1.1 million), an increase in non-interest income (up $522 thousand) thousand and an increase in the net income tax benefit (up $170 thousand), partly offset by an $822 thousand increase in non-interest expense. The decrease in net interest expense was related to a decrease in the interest rate paid on the Corporation's $100 million fixed-to-floating rate subordinated notes, which changed to a floating interest rate during the first quarter of 2012. The increase in non-interest income was primarily related to increased mineral interest income related to bonus, rental and shut-in payments and oil and gas royalties received from severed mineral interests on property owned by Main Plaza Corporation, a wholly-owned non-banking subsidiary of the Corporation. The increase non-interest expense was primarily related to an increase in professional services expense which included $1.3 million in costs incurred during the third and fourth quarters of 2013 associated with the pending acquisition of WNB Bancshares (See Note 21 - Pending Acquisition).

The Non-Banks operating segment had a net loss of $5.6 million in 2012, decreasing $2.4 million, or 29.9%, compared to $7.9 million in 2011. The decrease in the net loss was primarily due to a $4.2 million decrease in net interest expense and a $1.7 million increase in non-interest income partly offset by a $2.2 million increase in non-interest expense and a $1.3 million decrease in the net income tax benefit. The decrease in net interest expense was related to a decrease in the interest rate paid on the Corporation's $100 million fixed-to-floating rate subordinated notes, which changed to a floating interest rate during the first quarter of 2012. The increase in non-interest income was primarily related to increased mineral interest income. The increase in non-interest expense was partly related to non-recurring write-downs of certain equipment assets totaling $903 thousand in 2012 as well as increases in professional services expense, travel expense and directors fees.

Income Taxes

The Corporation recognized income tax expense of $53.0 million, for an effective tax rate of 18.2%, in 2013 compared to $70.5 million, for an effective tax rate of 22.9%, in 2012 and $68.7 million, for an effective rate of 24.0%, in 2011. The effective income tax rates differed from the U.S. statutory rate of 35% during the comparable periods primarily due to the effect of tax-exempt income from loans, securities and life insurance policies. The lower effective tax rate during 2013 was partly related to an increase in the relative proportion of tax-exempt income as the Corporation purchased additional tax-exempt municipal securities. The higher effective tax rate for 2011 was impacted by the correction, during the third quarter of 2011, of an under-accrual of taxes that resulted from incorrectly deducting premium amortization on municipal securities for federal income tax purposes since 2008. As a result, the Corporation recognized additional income tax expense totaling $4.1 million, which included interest, related to the 2010, 2009 and 2008 tax years. Excluding the effect of the correction related to prior year amounts, the Corporation's effective tax rate would have been 22.6% for 2011.

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Sources and Uses of Funds

The following table illustrates, during the years presented, the mix of the Corporation's funding sources and the assets in which those funds are invested as a percentage of the Corporation's average total assets for the period indicated. Average assets totaled $22.8 billion in 2013 compared to $20.8 billion in 2012 and $18.6 billion in 2011.

	2013		2012		2011	
Sources of Funds:						
Deposits:						
Non-interest-bearing	33.6	%	33.7	%	30.9	%
Interest-bearing	51.0		49.3		51.1	
Federal funds purchased and repurchase agreements	2.4		2.9		3.2	
Long-term debt and other borrowings	1.0		1.1		1.7	
Other non-interest-bearing liabilities	1.2		1.6		1.4	
Equity capital	10.8		11.4		11.7	
Total	100.0	%	100.0	%	100.0	%
Uses of Funds:						
Loans	40.6	%	40.6	%	43.3	%
Securities	39.1		42.9		33.5	
Federal funds sold, resell agreements and interest-bearing deposits	12.6		7.8		13.5	
Other non-interest-earning assets	7.7		8.7		9.7	
Total	100.0	%	100.0	%	100.0	%

Deposits continue to be the Corporation's primary source of funding. Average deposits increased $2.0 billion, or 11.4%, in 2013 compared to 2012 and $2.1 billion, or 13.6% in 2012 compared to 2011. Non-interest-bearing deposits remain a significant source of funding, which has been a key factor in maintaining the Corporation's relatively low cost of funds. Average non-interest-bearing deposits totaled 39.7% of total average deposits in 2013 compared to 40.6% in 2012, and 37.7% in 2011. The Dodd-Frank Act repealed the federal prohibitions on the payment of interest on demand deposits, thereby permitting depository institutions to pay interest on business transaction and other accounts beginning July 21, 2011. Although the ultimate impact of this legislation on the Corporation has not yet been determined, the Corporation may begin to incur interest costs associated with demand deposits in the future as market conditions warrant, in which case, the relative proportion of non-interest-bearing deposits to total deposits would be expected to decrease.

The Corporation primarily invests funds in loans and securities. Loans continue to be a large component of the Corporation's mix of invested assets. Average loans increased $772.8 million, or 9.1%, in 2013 compared to 2012 and increased $413.9 million, or 5.1% in 2012 compared to 2011. Average securities decreased $49.5 million, or 0.6%, in 2013 compared to 2012 and increased $2.7 billion, or 44.0%, in 2012 compared to 2011. Average federal funds sold, resell agreements and interest-bearing deposits increased $1.3 billion, or 77.6%, in 2013 compared to 2012 and decreased $899.1 million, or 35.8%, in 2012 compared to 2011. The increase in average federal funds sold, resell agreements and interest bearing deposits, in 2013 compared to 2012, was primarily related to excess liquidity from deposit growth in 2013.

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Loans

Year-end loans were as follows:

	2013	Percentage of Total	2012	2011	2010	2009
Commercial and industrial:						
Commercial	$4,460,543	46.9 %	$4,357,100	$3,553,989	$3,479,349	$3,577,758
Leases	319,577	3.4	278,535	193,412	186,443	197,605
Asset-based	126,956	1.3	192,977	169,466	122,866	117,213
Total commercial and industrial	4,907,076	51.6	4,828,612	3,916,867	3,788,658	3,892,576
Commercial real estate:						
Commercial mortgages	2,800,760	29.4	2,495,481	2,383,479	2,374,542	2,327,471
Construction	426,639	4.5	608,306	434,870	593,273	659,459
Land	239,937	2.5	216,008	202,478	234,952	259,200
Total commercial real estate	3,467,336	36.4	3,319,795	3,020,827	3,202,767	3,246,130
Consumer real estate:						
Home equity loans	329,853	3.5	310,675	282,244	275,806	289,535
Home equity lines of credit	195,132	2.1	186,522	191,960	186,465	166,441
1-4 family residential mortgages	32,447	0.3	38,323	45,943	57,877	66,351
Construction	13,123	0.1	17,621	17,544	23,565	30,325
Other	237,649	2.5	224,206	225,118	254,551	275,780
Total consumer real estate	808,204	8.5	777,347	762,809	798,264	828,432
Total real estate	4,275,540	44.9	4,097,142	3,783,636	4,001,031	4,074,562
Consumer and other:						
Consumer installment	350,827	3.7	311,310	301,518	319,384	346,255
Student loans held for sale	—	—	—	—	—	24,201
Other	7,289	0.1	8,435	11,018	28,234	52,406
Total consumer and other	358,116	3.8	319,745	312,536	347,618	422,862
Unearned discounts	(25,032)	(0.3)	(21,651)	(17,910)	(20,287)	(22,220)
Total	$9,515,700	100.0 %	$9,223,848	$7,995,129	$8,117,020	$8,367,780

Overview. Year-end total loans increased $291.9 million, or 3.2%, during 2013 compared to 2012. The Corporation does not generally originate 1-4 family residential mortgage loans and sold its student loan portfolio during 2010. As such, these loans are excluded when analyzing the growth of the loan portfolio. Excluding 1-4 family residential mortgages and student loans, year-end loans increased $297.7 million, or 3.2% during 2013 compared to 2012 increased $1.2 billion, or 15.6% during 2012 compared to 2011, decreased $110.0 million, or 1.4% during 2011 compared to 2010, and decreased $218.1 million, or 2.6%, during 2010 compared to 2009.

The majority of the Corporation's loan portfolio is comprised of commercial and industrial loans and real estate loans. Commercial and industrial loans made up 51.6% and 52.3% of total loans at December 31, 2013 and 2012 while real estate loans made up 44.9% and 44.4% of total loans at December 31, 2013 and 2012. Real estate loans include both commercial and consumer balances.

Loan Origination/Risk Management. The Corporation has certain lending policies and procedures in place that are designed to maximize loan income within an acceptable level of risk. Management reviews and approves these policies and procedures on a regular basis. A reporting system supplements the review process by providing management with frequent reports related to loan production, loan quality, concentrations of credit, loan delinquencies and non-performing and potential problem loans. Diversification in the loan portfolio is a means of managing risk associated with fluctuations in economic conditions. See Note 3 - Loans in the accompanying notes to consolidated financial statements included elsewhere in this report for further details of the Corporation's policies and procedures related to loan origination and risk management.

Commercial and Industrial Loans. Commercial and industrial loans increased $78.5 million, or 1.6%, during 2013 compared to 2012 and $911.7 million, or 23.3% from in 2012 compared to 2011. At December 31, 2012, commercial and industrial loans included $95.3 million related to an overdraft by a correspondent bank customer. The overdraft cleared subsequent to year-end. Excluding the effect of this overdraft, commercial and industrial loans increased $173.8 million, or 3.6% in 2013 compared to 2012 and $816.5 million, or 20.8%, in 2012 compared to 2011. The Corporation's commercial and industrial loans are a diverse group of loans to small, medium and large businesses. The purpose of these loans varies from supporting seasonal working capital needs to term financing of equipment. While some short-term loans may be made on an unsecured basis, most are secured by the assets being financed with collateral margins that are consistent with the Corporation's loan policy guidelines. The commercial and industrial loan portfolio also includes the

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commercial lease and asset-based lending portfolios as well as purchased shared national credits ("SNCs"), which are discussed in more detail below.

Industry Concentrations. As of December 31, 2013 and 2012, other than energy loans, there were no concentrations of loans within any single industry in excess of 10% of total loans, as segregated by Standard Industrial Classification code ("SIC code"). The SIC code is a federally designed standard industrial numbering system used by the Corporation to categorize loans by the borrower's type of business. The following table summarizes the industry concentrations of the Corporation's loan portfolio, as segregated by SIC code. Industry concentrations are stated as a percentage of year-end total loans as of December 31, 2013 and 2012:

	2013		2012	
Industry concentrations:				
Energy	11.7	%	11.7	%
Medical services	5.7		5.7	
Public finance	5.6		6.3	
Manufacturing, other	3.2		3.1	
Religion	2.9		2.8	
Services	2.8		2.9	
General and specific trade contractors	2.7		3.0	
Legal services	2.6		1.8	
Transportation	2.6		2.1	
Automobile dealers	2.3		2.0	
Insurance	2.1		2.1	
All other (36 categories in 2013 and 35 categories in 2012)	55.8		56.5	
Total loans	100.0	%	100.0	%

The Corporation's largest concentration in any single industry is in energy. Year-end energy loans were as follows:

	2013	2012
Energy loans:		
Production	$809,090	$765,424
Service	260,047	242,448
Manufacturing	31,507	50,721
Traders	9,462	20,126
Refining	5,303	4,467
Total energy loans	$1,115,409	$1,083,186

Large Credit Relationships. The market areas served by the Corporation include three of the top ten most populated cities in the United States. These market areas are also home to a significant number of Fortune 500 companies. As a result, the Corporation originates and maintains large credit relationships with numerous commercial customers in the ordinary course of business. The Corporation considers large credit relationships to be those with commitments equal to or in excess of $10.0 million, excluding treasury management lines exposure, prior to any portion being sold. Large relationships also include loan participations purchased if the credit relationship with the agent is equal to or in excess of $10.0 million. In addition to the Corporation's normal policies and procedures related to the origination of large credits, the Corporation's Central Credit Committee (CCC) must approve all new and renewed credit facilities which are part of large credit relationships. The CCC meets regularly and reviews large credit relationship activity and discusses the current pipeline, among other things. The following table provides additional information on the Corporation's large credit relationships outstanding at year-end.

	2013			2012		
	Number of	Period-End Balances		Number of	Period-End Balances	
	Relationships	Committed	Outstanding	Relationships	Committed	Outstanding
Committed amount:						
$20.0 million and greater	178	$6,859,052	$3,283,355	149	$5,539,527	$2,986,522
$10.0 million to $19.9 million	165	2,267,864	1,307,519	170	2,343,440	1,295,147

The average commitment per large credit relationship in excess of $20.0 million totaled $38.5 million at December 31, 2013 and $37.2 million at December 31, 2012. The average outstanding balance per large credit relationship with a commitment in excess of $20.0 million totaled $18.4 million at December 31, 2013 and $20.0 million at December 31, 2012. The average commitment per large credit relationship between $10.0 million and $19.9 million totaled $13.7 million at December 31, 2013 and $13.8 million at

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December 31, 2012. The average outstanding balance per large credit relationship with a commitment between $10 million and $19.9 million totaled $7.9 million at December 31, 2013 and $7.6 million at December 31, 2012.

Purchased Shared National Credits. Purchased SNCs are participations purchased from upstream financial organizations and tend to be larger in size than the Corporation's originated portfolio. The Corporation's purchased SNC portfolio totaled $586.2 million at December 31, 2013 decreasing $41.8 million, or 6.7%, from $628.0 million at December 31, 2012. At December 31, 2013, 56.2% of outstanding purchased SNCs was related to the energy industry. The remaining purchased SNCs were diversified throughout various other industries, with no other single industry exceeding 10% of the total purchased SNC portfolio. Additionally, almost all of the outstanding balance of purchased SNCs was included in the commercial and industrial portfolio, with the remainder included in the real estate categories. SNC participations are originated in the normal course of business to meet the needs of the Corporation's customers. As a matter of policy, the Corporation generally only participates in SNCs for companies headquartered in or which have significant operations within the Corporation's market areas. In addition, the Corporation must have direct access to the company's management, an existing banking relationship or the expectation of broadening the relationship with other banking products and services within the following 12 to 24 months. SNCs are reviewed at least quarterly for credit quality and business development successes. The following table provides additional information about certain credits within the Corporation's purchased SNCs portfolio as of year-end.

	2013			2012		
	Number of	Period-End Balances		Number of	Period-End Balances	
	Relationships	Committed	Outstanding	Relationships	Committed	Outstanding
Purchased shared national credits:						
$20.0 million and greater	40	$1,329,601	$451,306	37	$1,194,902	$465,975
$10.0 million to $19.9 million	15	224,354	114,297	17	233,262	145,081

Real Estate Loans. Real estate loans totaled $4.3 billion at December 31, 2013 increasing $178.4 million, or 4.4%, compared to $4.1 billion at December 31, 2012. Commercial real estate loans totaled $3.5 billion, or 81.1%, of total real estate loans, at December 31, 2013 and $3.3 billion, or 81.0% of total real estate loans, at December 31, 2012. The majority of this portfolio consists of commercial real estate mortgages, which includes both permanent and intermediate term loans. The Corporation's primary focus for the commercial real estate portfolio has been growth in loans secured by owner-occupied properties. These loans are viewed primarily as cash flow loans and secondarily as loans secured by real estate. Consequently, these loans must undergo the analysis and underwriting process of a commercial and industrial loan, as well as that of a real estate loan.

The following tables summarize the Corporation's commercial real estate loan portfolio, as segregated by (i) the type of property securing the credit and (ii) the geographic region in which the loans were originated. Property type concentrations are stated as a percentage of year-end total commercial real estate loans as of December 31, 2013 and 2012:

	2013		2012	
Property type:				
Office building	17.1	%	16.7	%
Office/warehouse	15.2		15.5	
Medical offices and services	9.2		9.8	
Religious	7.6		7.5	
Non-farm/non-residential	7.4		7.1	
Multifamily	6.8		4.2	
1-4 Family	4.9		4.3	
Retail	4.6		7.1	
All other	27.2		27.8	
Total commercial real estate loans	100.0	%	100.0	%
Geographic region:				
San Antonio	24.7	%	24.9	%

Fort Worth	23.9		24.7	
Houston	19.3		19.6	
Dallas	12.5		10.2	
Austin	10.0		9.9	
Rio Grande Valley	5.6		6.1	
Corpus Christi	4.0		4.6	
Total commercial real estate loans	100.0	%	100.0	%

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Consumer Loans. The consumer loan portfolio, including all consumer real estate, increased $70.4 million, or 6.5%, from December 31, 2012. As the following table illustrates, the consumer loan portfolio has two distinct segments, including consumer real estate and consumer installment.

	2013	2012
Consumer real estate:		
Home equity loans	$329,853	$310,675
Home equity lines of credit	195,132	186,522
1-4 family residential mortgages	32,447	38,323
Construction	13,123	17,621
Other	237,649	224,206
Total consumer real estate	808,204	777,347
Consumer installment	350,827	311,310
Total consumer loans	$1,159,031	$1,088,657

Consumer real estate loans, increased $30.9 million, or 4.0%, from December 31, 2012. Combined, home equity loans and lines of credit made up 65.0% and 64.0% of the consumer real estate loan total at December 31, 2013 and 2012, respectively. The Corporation offers home equity loans up to 80% of the estimated value of the personal residence of the borrower, less the value of existing mortgages and home improvement loans. In general, the Corporation no longer originates 1-4 family mortgage loans, however, from time to time, the Corporation may invest in such loans to meet the needs of its customers.

The consumer installment loan portfolio primarily consists of automobile loans, unsecured revolving credit products, personal loans secured by cash and cash equivalents, and other similar types of credit facilities.

Foreign Loans. The Corporation makes U.S. dollar-denominated loans and commitments to borrowers in Mexico. The outstanding balance of these loans and the unfunded amounts available under these commitments were not significant at December 31, 2013 or 2012.

Maturities and Sensitivities of Loans to Changes in Interest Rates. The following table presents the maturity distribution of the Corporation's loans, excluding 1-4 family residential real estate loans and unearned discounts, at December 31, 2013. The table also presents the portion of loans that have fixed interest rates or variable interest rates that fluctuate over the life of the loans in accordance with changes in an interest rate index such as the prime rate or LIBOR.

	Due in One Year or Less	After One, but Within Five Years	After Five Years	Total
Commercial and industrial	$2,213,790	$2,231,689	$461,597	$4,907,076
Real estate construction	124,171	248,421	54,047	426,639
Commercial real estate and land	323,938	1,560,251	1,156,508	3,040,697
Consumer and other	206,770	195,925	731,178	1,133,873
Total	$2,868,669	$4,236,286	$2,403,330	$9,508,285
Loans with fixed interest rates	$773,311	$1,308,885	$1,392,182	$3,474,378
Loans with floating interest rates	2,095,358	2,927,401	1,011,148	6,033,907
Total	$2,868,669	$4,236,286	$2,403,330	$9,508,285

The Corporation generally structures commercial loans with shorter-term maturities in order to match the Corporation's funding sources and to enable the Corporation to effectively manage the loan portfolio by providing the flexibility to respond to liquidity needs, changes in interest rates and changes in underwriting standards and loan structures, among other things. Due to the shorter-term nature of such loans, from time to time and in the ordinary course of business, the Corporation will renew/extend maturing lines of credit or refinance existing loans at their maturity dates. Some loans may renew multiple times in a given year as a result of general customer practice and need. These renewals, extensions and refinancings are made in the ordinary course of business for customers that meet the Corporation's normal level of credit standards. Such borrowers typically request renewals to support their on-going working capital needs to finance their operations. Such borrowers are not experiencing financial difficulties and generally could obtain similar financing from another financial institution. In connection with each renewal, extension or refinancing, the Corporation may require a principal reduction, adjust the rate of interest and/or modify the structure and other terms to reflect the current market pricing/structuring for such loans or to maintain competitiveness with other financial institutions. In such cases, the Corporation does not generally grant concessions, and, except for those reported in Note 3 - Loans, any such renewals, extensions or refinancings that occurred during the reported periods were not deemed to be troubled debt restructurings pursuant to applicable accounting guidance. Loans exceeding $1.0 million undergo a complete underwriting process at each renewal.

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Non-Performing Assets and Potential Problem Loans

Non-Performing Assets. Year-end non-performing assets and accruing past due loans were as follows:

	2013	2012	2011	2010	2009
Non-accrual loans:					
Commercial and industrial	$26,733	$46,308	$43,874	$60,408	$82,219
Real estate	29,242	42,504	49,736	76,270	63,926
Consumer and other	745	932	728	462	722
Total non-accrual loans	56,720	89,744	94,338	137,140	146,867
Restructured loans	1,137	—	—	—	—
Foreclosed assets:					
Real estate	11,916	15,152	26,608	27,339	33,305
Other	—	350	—	471	7
Total foreclosed assets	11,916	15,502	26,608	27,810	33,312
Total non-performing assets	$69,773	$105,246	$120,946	$164,950	$180,179
Ratio of non-performing assets to:					
Total loans and foreclosed assets	0.73 %	1.14 %	1.51 %	2.03 %	2.14 %
Total assets	0.29	0.46	0.60	0.94	1.11
Accruing past due loans:					
30 to 89 days past due	$31,297	$35,969	$42,463	$55,045	$90,173
90 or more days past due	7,635	6,994	17,417	26,922	23,911
Total accruing past due loans	$38,932	$42,963	$59,880	$81,967	$114,084
Ratio of accruing past due loans to total loans:					
30 to 89 days past due	0.33 %	0.39 %	0.53 %	0.68 %	1.08 %
90 or more days past due	0.08	0.08	0.22	0.33	0.28
Total accruing past due loans	0.41 %	0.47 %	0.75 %	1.01 %	1.36 %

Non-performing assets include non-accrual loans, trouble debt restructurings and foreclosed assets. Non-performing assets at December 31, 2013 decreased $35.5 million from December 31, 2012. While down significantly in 2013, in general, the level of non-performing assets in recent years has been reflective of the weaker economic conditions which began in the latter part of 2008. Non-accrual commercial and industrial loans included one credit relationship in excess of $5 million totaling $6.3 million at December 31, 2013 and three credit relationships in excess of $5 million totaling $27.8 million at December 31, 2012. Non-accrual real estate loans primarily consist of land development, 1-4 family residential construction credit relationships and loans secured by office buildings and religious facilities. Non-accrual commercial real estate loans included one credit relationships in excess of $5 million totaling $7.3 million at December 31, 2013 and two credit relationships in excess of $5 million totaling $18.2 million at December 31, 2012. At December 31, 2013, one credit relationship totaling $7.9 million was included in both non-accrual commercial and industrial loans ($4.7 million) and non-accrual commercial real estate loans ($3.2 million). Approximately $15.0 million of the non-accrual commercial and industrial loans and $12.6 million of the non-accrual commercial real estate loans at December 31, 2012 pertained to the same customer.

Non-accrual commercial and industrial loans included two credit relationships in excess of $5 million totaling $17.3 million at December 31, 2011, three credit relationships in excess of $5 million totaling $25.8 million at December 31, 2010 and three credit relationships in excess of $5 million totaling $37.6 million at December 31, 2009. Non-accrual commercial real estate loans included one credit relationship in excess of $5 million totaling $5.8 million at December 31, 2011. Non-accrual commercial and industrial and real estate loans also included $6.5 million and $16.3 million in loans to certain Mexican borrowers at December 31, 2010 and December 31, 2009, respectively, primarily related to deterioration in the U.S. dollar exchange rate of the Mexican peso.

Generally, loans are placed on non-accrual status if principal or interest payments become 90 days past due and/or management deems the collectibility of the principal and/or interest to be in question, as well as when required by regulatory requirements. Once interest accruals are discontinued, accrued but uncollected interest is charged to current year operations. Subsequent receipts on non-accrual loans are recorded as a reduction of principal, and interest income is recorded only after principal recovery is reasonably assured. Classification of a loan as non-accrual does not preclude the ultimate collection of loan principal or interest.

Foreclosed assets represent property acquired as a 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 loan losses. Regulatory guidelines require the Corporation to reevaluate the fair value of foreclosed assets on at least an annual basis. The Corporation's policy is to comply with the regulatory guidelines. Write-downs are provided for subsequent declines in value

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and are included in other non-interest expense along with other expenses related to maintaining the properties. During 2013 and 2012, foreclosed assets, particularly among certain classes of property (primarily land), experienced significant deterioration in fair values as a result of the prevailing weaker economic conditions. Write-downs of foreclosed assets totaled $895 thousand and $2.1 million, during 2013 and 2012, respectively. During 2013, the Corporation recognized write-downs on 13 different properties/relationships with the average write-down totaling $69 thousand and the largest individual write-down totaling $490 thousand. The weighted-average percentage write-down was 18.0%. During 2012, the Corporation recognized write-downs on 33 different properties/relationships with the average write-down totaling $63 thousand and the largest individual write-down totaling $575 thousand. The weighted-average percentage write-down was 17.3%. There were no significant concentrations of any properties, to which the aforementioned write-downs relate, in any single geographic region.

Potential problem loans consist of loans that are performing in accordance with contractual terms but for which management has concerns about the ability of an obligor to continue to comply with repayment terms because of the obligor's potential operating or financial difficulties. Management monitors these loans closely and reviews their performance on a regular basis. At December 31, 2013 and 2012, the Corporation had $13.8 million and $10.7 million in loans of this type which are not included in any one of the non-accrual, restructured or 90 days past due loan categories. At December 31, 2013, potential problem loans consisted of six credit relationships. Of the total outstanding balance at December 31, 2013, 28.3% related to a customer in manufacturing, 20.3% related to a municipality and 20.0% related to a customer in the health care industry. Weakness in these borrowers' operating performance has caused the Corporation to heighten the attention given to these credits.

Allowance For Loan Losses

The allowance for loan losses is a reserve established through a provision for loan losses charged to expense, which represents management's best estimate of probable losses that have been incurred within the existing portfolio of loans. The allowance, in the judgment of management, is necessary to reserve for estimated loan losses and risks inherent in the loan portfolio. The Corporation's allowance for loan loss methodology includes allowance allocations calculated in accordance with ASC Topic 310, "Receivables" and allowance allocations calculated in accordance with ASC Topic 450, "Contingencies." Accordingly, the methodology is based on historical loss experience by type of credit and internal risk grade, specific homogeneous risk pools and specific loss allocations, with adjustments for current events and conditions. The Corporation's process for determining the appropriate level of the allowance for loan losses is designed to account for credit deterioration as it occurs. The provision for loan losses reflects loan quality trends, including the levels of and trends related to non-accrual loans, past due loans, potential problem loans, classified and criticized loans and net charge-offs or recoveries, among other factors. The provision for loan losses also reflects the totality of actions taken on all loans for a particular period. In other words, the amount of the provision reflects not only the necessary increases in the allowance for loan losses related to newly identified criticized loans, but it also reflects actions taken related to other loans including, among other things, any necessary increases or decreases in required allowances for specific loans or loan pools. See Note 3 - Loans in the accompanying notes to consolidated financial statements included elsewhere in this report for further details regarding the Corporation's methodology for estimating the appropriate level of the allowance for loan losses.

The table below provides an allocation of the year-end allowance for loan losses by loan type; however, allocation of a portion of the allowance to one category of loans does not preclude its availability to absorb losses in other categories. Prior to 2012, certain general valuation allowances were not allocated to specific loan portfolio segments and were included in unallocated allowances. See Note 3 - Loans for details of amounts allocated to specific portfolio segments.

2013		2012		2011		2010		2009	
Allowance for Loan Losses	Percentage of Loans in each Category to Total Loans	Allowance for Loan Losses	Percentage of Loans in each Category to Total Loans	Allowance for Loan Losses	Percentage of Loans in each Category to Total Loans	Allowance for Loan Losses	Percentage of Loans in each Category to Total Loans	Allowance for Loan Losses	Percentage of Loans in each Category to Total Loans
$52,790	51.6 %	$54,164	52.3 %	$42,774	49.0 %	$57,789	46.7 %	$57,394	46.5 %

Commercial and industrial										
Commercial real estate	22,590	36.4	29,346	36.0	20,912	37.8	28,534	39.5	28,514	38.8
Consumer real estate	5,230	8.5	5,252	8.4	3,540	9.5	3,223	9.8	2,560	9.9
Consumer and other	5,010	3.5	3,507	3.3	12,635	3.7	11,974	4.0	16,929	4.8
Unallocated	6,818	—	12,184	—	30,286	—	24,796	—	19,912	—
Total	$92,438	100.0 %	$104,453	100.0 %	$110,147	100.0 %	$126,316	100.0 %	$125,309	100.0 %

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The reserve allocated to commercial and industrial loans at December 31, 2013 decreased $1.4 million compared to December 31, 2012. The decrease was primarily related to a decreases in the reserve allocated for excessive industry concentrations, historical valuation allowances, the environmental risk adjustment and specific valuation allowances, partly offset by increases in the distressed industries allocation and the reserve allocated for highly leveraged credit relationships and a decrease in the adjustment for recoveries. The decrease in the reserve allocated for excessive industry concentrations was primarily related to a decrease in the volumes of industry concentrations combined with a decrease in the allocation factors applied to certain categories of industry concentrations. The decrease in historical valuation allowances was primarily due to decreases in the historical loss allocation factors applied to certain categories of non-classified and classified commercial and industrial loans. The environmental risk adjustment decreased $1.1 million from $6.6 million at December 31, 2012 to $5.5 million at December 31, 2013. Although the environmental risk adjustment factor increased at December 31, 2013 compared to December 31, 2012, the dollar amount of the environmental risk adjustment decreased as a result of the aforementioned decreases in the base historical loss allocation factors to which the environmental risk adjustment factor is applied. The distressed industries allocation related to commercial and industrial loans increased $1.9 million from $5.9 million at December 31, 2012 to $7.8 million at December 31, 2013. The increase was primarily related to an increase in the volume of loans to contractors combined with an increase in the spread by which the weighted-average risk grade of this portfolio exceeds the weighted-average risk grade of the commercial and industrial loan portfolio as a whole. The reserve allocated for highly leveraged credit relationships increased $1.6 million from $2.9 million at December 31, 2012 to $4.5 million at December 31, 2013 primarily due to an increase in the volume of such credit relationships. The adjustment for recoveries decreased $1.3 million from $4.9 million at December 31, 2012 to $3.6 million at December 31, 2013 primarily due to the lower level of recoveries experienced in 2013 relative to 2012.

Classified commercial and industrial loans (loans having a risk grade of 11, 12 or 13) totaled $120.2 million at December 31, 2013 compared to $100.1 million at December 31, 2012. Specific allocations of the allowance for loan losses related to commercial and industrial loans totaled $4.1 million at December 31, 2013 compared to $5.1 million at December 31, 2012.

The reserve allocated to commercial real estate loans at December 31, 2013 decreased $6.8 million compared to December 31, 2012. The decrease was primarily related to decreases in the historical valuation allowances related to pass and watch grade commercial real estate loans due, in part, to decreases in the historical loss allocation factors applied to such loans. The reserve allocated to commercial real estate loans at December 31, 2013 compared to December 31, 2012 was also partly impacted by a decrease in the allocation for excessive industry concentrations (down $2.4 million), a decrease in the reserve allocation for distressed industries (down $798 thousand) and a decrease in the environmental risk adjustment (down $368 thousand).

Classified commercial real estate loans totaled $80.8 million at December 31, 2013 compared to $118.1 million at December 31, 2012. Specific allocations of the allowance for loan losses related to commercial real estate loans totaled $2.8 million at December 31, 2013 compared to $3.1 million at December 31, 2012. The environmental adjustment factor resulted in additional general valuation allowances for commercial real estate loans totaling $3.3 million at December 31, 2013 and $3.7 million at December 31, 2012. The distressed industries allocation related to commercial real estate loans totaled $384 thousand at December 31, 2013 and $1.2 million at December 31, 2012.

The reserve allocated to consumer real estate loans at December 31, 2013 did not significantly fluctuate compared to December 31, 2012 as decreases in historical valuation allowances as well as decreases in the allocation for loans that did not undergo a separate, independent concurrence review during the underwriting process and the environmental risk adjustment were mostly offset by a decrease in the adjustment for recoveries.

The reserve allocated to consumer and other loans at December 31, 2013 increased $1.5 million compared to December 31, 2012. The increase was primarily related to an increase in historical valuation allowances due to an increase in the historical loss allocation factor applied to consumer and other loans, combined with the effect of a higher volume of such loans, and an increase in the environmental risk adjustment. The increase from these items was partly offset by a decrease in the allocation for loans that did not undergo a separate, independent concurrence review during the underwriting process and an increase in the adjustment for recoveries.

The unallocated portion of the allowance for loan losses represents general valuation allowances that are not allocated to specific loan portfolio segments. See Note 3 – Loans in the accompanying notes to consolidated financial statements for information regarding the components of the unallocated portion of the allowance. The unallocated portion of the allowance for loan losses at December 31, 2013 decreased \$5.4 million compared to December 31, 2012. This decrease was primarily due to a decrease in the allocation for general macroeconomic risk (down \$5.2 million). This is reflective of improving trends in certain components of the Texas Leading Index and, aside from the \$18.8 million in charge-offs discussed below related to a single customer relationship which was not considered to be indicative of a decline in the overall credit quality of the Corporation's loan portfolio, the trend in net charge-offs has stabilized at improved levels compared to recent years. The overall level of classified commercial and industrial and commercial real estate loans decreased approximately \$17.3 million, or 7.9%, at December 31, 2013 compared to December 31, 2012 while the overall weighted-average risk grades of these portfolios was 6.40% at December 31, 2013 and 6.39% December 31, 2012.

As of December 31, 2012, the reserve allocated to commercial and industrial loans increased \$11.4 million compared to December 31, 2011. As of December 31, 2012, the reserve allocated to commercial and industrial loans included \$6.0 million related to certain general valuation allowances that were previously reported as components of the unallocated portion of the allowance for loan losses. Excluding the impact of this reclassification of certain general valuation allowances, the reserve allocated to commercial and industrial loans at December 31, 2012 increased $5.4 million from December 31, 2011. The increase was primarily related to increases in historical valuation allowances due to an increase in the volume of non-classified commercial and industrial loans, an increase in allocations for specific loans, an increase in the allocation for distressed industries and an increase in the environmental risk adjustment partly offset by a decrease in classified loans.

As of December 31, 2012, the reserve allocated to commercial real estate loans increased $8.4 million compared to December 31, 2011. The reserve allocated to commercial real estate loans included $5.7 million related to certain general valuation allowances that were previously reported as components of the unallocated portion of the allowance for loan losses. Excluding the impact of this reclassification of certain general valuation allowances, the reserve allocated to commercial real estate loans at December 31, 2012 increased $2.8 million compared to December 31, 2011. The increase was primarily related to an increase in allocations for specific loans, an increase in historical valuation allowances due to an increase in the volume of non-classified commercial real estate loans and an increase in the allocation for distressed industries partly offset by the effect of a decrease in classified loans. The allowance allocated to commercial real estate loans at December 31, 2012 was also impacted by a decrease in the historical loss allocation factors applied to certain categories of non-classified and classified commercial real estate loans compared to the historical loss allocation factors used in 2011.

The reserve allocated to consumer real estate loans at December 31, 2012 increased $1.7 million compared to December 31, 2011. The reserve allocated to consumer real estate loans included $1.6 million related to certain general valuation allowances that were previously reported as components of the unallocated portion of the allowance for loan losses. Excluding the impact of this reclassification of certain general valuation allowances, the reserve allocated to consumer real estate loans at December 31, 2012 did not significantly fluctuate compared to December 31, 2011 as the impact of factors requiring an increase in the level of allowance required for consumer real estate loans were for the most part offset by the impact of factors requiring a decrease in the level of allowance required for consumer real estate loans.

The reserve allocated to consumer and other loans at December 31, 2012 decreased $9.1 million compared to December 31, 2011. As of December 31, 2012, the reserve allocated to consumer and other loans included a reduction of $5.7 million related to certain general valuation allowances that were previously reported as components of the unallocated portion of the allowance for loan losses. Excluding the impact of this reclassification of certain general valuation allowances, the reserve allocated to consumer and other loans at December 31, 2012 decreased $3.5 million compared to December 31, 2011. The decrease was primarily related to a decrease in the historical loss allocation factor applied to consumer and other loans combined with a decrease in the environmental risk adjustment factor partly offset by the effect of an increase in the volume of consumer and other loans.

The unallocated portion of the allowance for loan losses at December 31, 2012 decreased $18.1 million compared to December 31, 2011. Excluding certain general valuation allowances that were reclassified to specific loan portfolio segments, as discussed above, the unallocated portion of the allowance for loan losses at December 31, 2012 would have decreased $9.4 million compared to December 31, 2011 primarily due to a decrease in the allocation for general macroeconomic risk, down $9.8 million at December 31, 2012 compared to December 31, 2011. The decrease in the allocation for general macroeconomic risk was reflective of improving trends in certain components of the Texas Leading Index and an improved outlook on the credit quality of the Corporation’s loan portfolio.

During 2011, the reserve allocated to commercial and industrial loans and commercial real estate loans decreased $15.0 million and $7.6 million, respectively, compared to 2010 primarily due to decreases in the level of classified loans and allocations for specific loans. The decreases in reserves allocated to commercial and industrial and commercial real estate loans were also partly due to decreases in the historical loss allocation factors applied to non-classified loans in these loan categories. The impact of these reductions was partly offset by the effect of a new allocation for distressed industries, which was implemented in 2011, and an increase in the environmental adjustment factor. The reserve allocated to consumer real estate loans increased $317 thousand in 2011 compared to 2010, while the reserve allocated to consumer and other loans increased $661 thousand in 2011 compared to 2010. The increases in the reserves allocated to consumer real estate loans and consumer and other loans were primarily related to increases in the historical loss allocation factors applied to these loan segments and an increase in the environmental adjustment factor, partly offset by the effect of a decrease in the volume of loans in each of these segments. The unallocated portion of the allowance for loan losses increased $5.5 million in 2011 compared to 2010. This fluctuation was primarily due to an increase in the allocation for excessive industry concentrations which totaled $7.0 million at December 31, 2011 compared to $1.7 million at December 31, 2010. The increase was primarily related to new industry concentrations that were not considered to be excessive industry concentrations in 2010. In addition, during 2011, the Corporation refined its methodology for the determination of general valuation allowances to (i) provide additional allocations for loans that did not undergo a separate, independent concurrence review during the underwriting process (generally those loans under $1.0 million at origination), (ii) reduce the minimum balance/commitment threshold for which allocations are made for highly leveraged credit relationships that exceed specified risk grades, (iii) lower the maximum risk grade thresholds for highly leveraged credit relationships, and (iv) include a reduction factor for recoveries of prior charge-offs to compensate for the fact that historical loss allocations are based upon gross charge-offs rather than net. The net effect of these changes to the Corporation’s methodology for the determination of general valuation allowances did not significantly impact the level of the unallocated portion of the allowance for loan losses at December 31, 2011 compared to December 31, 2010.

During 2010, the reserve allocated to commercial and industrial loans and commercial and consumer real estate loans did not significantly fluctuate compared to 2009 as the effect of a slight decrease in the level of classified loans as well as decreases in the overall volume of commercial and industrial loans and real estate loans was offset by the effect of increases in the historical loss allocation factors applied to both classified and non-classified loans. The historical loss allocation factors for non-classified loans determined based upon actual historical experience were adjusted upwards given the continued higher levels of net charge-offs relative to historical average and the continued uncertain economic conditions. Additionally, an increase in specific valuation allowances related to commercial real estate loans was offset by a decrease in specific valuation allowances related to commercial and industrial loans. The decrease in the reserve allocated to consumer and other loans during 2010 compared to 2009 was primarily related to a decrease in the volume of such loans. Despite improving economic conditions relative to 2009, the increase in the unallocated portion of the allowance for loan losses during 2010 compared to 2009 was reflective of continued economic uncertainty resulting from weakness in certain business sectors (including contractors, builders, commercial real estate, manufacturing and healthcare), high unemployment and relatively low consumer spending activity. The Corporation primarily monitors communications and statistical data from the Federal Reserve and other agencies of the U.S. government in assessing the status of these factors. By the end of 2010, management believed that the improving trends seen in certain components of the Texas Leading Index, as well as in the national economy as a whole, were primarily driven by government stimulus programs, the extension of tax cuts and the monetary policy of the Federal Reserve with regards to quantitative easing. Such measures were expected to act as a catalyst for long-term growth; however, while short-term improvements were seen, management believed that these measures did not lead to private-sector employment growth and increased consumer spending levels as they were expected.

Activity in the allowance for loan losses is presented in the following table.

	2013		2012		2011		2010		2009	
Balance of allowance for loan losses at beginning of year	$104,453		$110,147		$126,316		$125,309		$110,244	
Provision for loan losses	20,582		10,080		27,445		43,611		65,392	
Charge-offs:										
Commercial and industrial	(32,932	)	(18,493	)	(33,678	)	(31,324	)	(35,432	)
Real estate	(2,376	)	(5,446	)	(13,565	)	(10,206	)	(12,132	)
Consumer and other	(9,489	)	(9,101	)	(9,442	)	(11,893	)	(12,047	)
Total charge-offs	(44,797	)	(33,040	)	(56,685	)	(53,423	)	(59,611	)
Recoveries:										
Commercial and industrial	3,588		4,870		4,526		2,794		2,525	
Real estate	1,532		5,584		1,838		1,603		497	
Consumer and other	7,080		6,812		6,707		6,422		6,262	
Total recoveries	12,200		17,266		13,071		10,819		9,284	
Net charge-offs	(32,597	)	(15,774	)	(43,614	)	(42,604	)	(50,327	)
Balance at end of year	$92,438		$104,453		$110,147		$126,316		$125,309	
Net charge-offs as a percentage of average loans	0.35	%	0.19	%	0.54	%	0.52	%	0.58	%
Allowance for loan losses as a percentage of year-end loans	0.97		1.13		1.38		1.56		1.50	
Allowance for loan losses as a percentage of year-end non-accrual loans	162.97		116.39		116.76		92.11		85.32	
Average loans outstanding during the year	$9,229,574		$8,456,818		$8,042,968		$8,125,150		$8,652,563	
Loans outstanding at year-end	9,515,700		9,223,848		7,995,129		8,117,020		8,367,780	

Non-accrual loans outstanding at year-end	56,720	89,744	94,338	137,140	146,867

As stated above, the provision for loan losses reflects loan quality trends, including the level of net charge-offs or recoveries, among other factors. The provision for loan losses increased $10.5 million in 2013 compared to 2012. During 2013, the Corporation recognized charge-offs totaling $18.8 million related to a single commercial and industrial loan relationship. The loan was not past due or previously considered to be a non-performing, impaired or potential problem loan prior to the initial charge-off in the first quarter of 2013; however, in April 2013, the borrower entered into bankruptcy proceedings. The level of the provision for loan losses during 2013 was impacted by this charge-off. The provision for loan losses decreased $17.4 million in 2012 compared to 2011, which was reflective of the decreasing trend in classified loans and a decrease in net charge-offs. The provision for loan losses decreased $16.2 million in 2011 compared to 2010, which was reflective of the decreasing trend in classified loans. The provision for loan losses decreased $21.8 million in 2010 compared to 2009, which was reflective of a decrease in the level of net charge-offs as well as decreases in the level of classified loans and overall loan volumes.

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Net charge-offs during 2013 increased $16.8 million compared to 2012. Excluding the aforementioned $18.8 million in charge-offs related to a single commercial and industrial loan relationship, net charge-offs would have been $13.8 million, or 0.15% of average loans during 2013. This compares to net charge-offs of $15.8 million, or 0.19% of average loans during 2012, evidencing the otherwise positive trend in net charge-offs and the overall credit quality of the Corporation's loan portfolio. Net charge-offs for 2012 decreased $27.8 million compared to 2011, while net charge-offs for 2011 increased $1.0 million compared to 2010 and net charge-offs for 2010 decreased $7.7 million compared to 2009. As a percentage of average loans, net charge-offs increased 16 basis points in 2013 compared to 2012 (or decreased 4 basis points in 2013 compared to 2012 when excluding the aforementioned $18.8 million in charge-offs related to a single commercial and industrial loan relationship), decreased 35 basis points in 2012 compared to 2011, increased 2 basis points in 2011 compared to 2010 and decreased 6 basis points in 2010 compared to 2009. The level of net charge-offs in 2011 was partly related to the charge-off of several large credit relationships during the third quarter of 2011. Aside from these charge-offs and the $18.8 million charge-off in 2013, the overall trend in net charge-offs since 2009 reflects the continued improvement in the level of classified loans since the deterioration of economic conditions which began in 2008.

The ratio of the allowance for loan losses to total loans decreased 16 basis points from 1.13% at December 31, 2012 to 0.97% at December 31, 2013 and decreased 25 basis points from 1.38% at December 31, 2011 to 1.13% at December 31, 2012, which is reflective of continued improvement in the level of classified loans. Management believes the recorded amount of the allowance for loan losses is appropriate based upon management's best estimate of probable losses that have been incurred within the existing portfolio of loans. Should any of the factors considered by management in evaluating the appropriate level of the allowance for loan losses change, the Corporation's estimate of probable loan losses could also change, which could affect the level of future provisions for loan losses and charge-offs.

Securities

Year-end securities were as follows:

	2013			2012			2011		
	Amount	Percentage of Total		Amount	Percentage of Total		Amount	Percentage of Total	
Held to maturity:									
U.S. Treasury	$248,592	2.7	%	$248,188	2.7	%	$247,797	3.0	%
Residential mortgage-backed securities	9,674	0.1		10,725	0.1		11,874	0.2	
States and political subdivisions	2,880,482	31.8		2,696,468	29.4		105,325	1.3	
Other	1,000	—		1,000	—		1,000	—	
Total	3,139,748	34.6		2,956,381	32.2		365,996	4.5	
Available for sale:									
U.S. Treasury	2,540,554	28.1		3,057,921	33.3		2,056,732	25.2	
U.S. government agencies/corporations	53,980	0.6		—	—		250,884	3.1	
Residential mortgage-backed securities	1,776,016	19.6		2,518,003	27.4		3,289,270	40.2	
States and political subdivisions	1,488,914	16.5		591,483	6.4		2,154,813	26.4	
Other	35,972	0.4		35,892	0.4		38,001	0.4	
Total	5,895,436	65.2		6,203,299	67.5		7,789,700	95.3	
Trading:									
U.S. Treasury	15,389	0.2		14,038	0.1		13,609	0.2	
States and political subdivisions	1,009	—		16,036	0.2		—	—	

Total	16,398	0.2		30,074	0.3		13,609	0.2	
Total securities	$9,051,582	100.0	%	$9,189,754	100.0	%	$8,169,305	100.0	%

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The following tables summarize the maturity distribution schedule with corresponding weighted-average yields of securities held to maturity and securities available for sale as of December 31, 2013. Weighted-average yields have been computed on a fully taxable-equivalent basis using a tax rate of 35%. 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 available for sale include stock in the Federal Reserve Bank and the Federal Home Loan Bank, which have no maturity date. These securities have been included in the total column only.

	Within 1 Year		1-5 Years		5-10 Years		After 10 Years		Total	
	Amount	Weighted Average Yield	Amount	Weighted Average Yield	Amount	Weighted Average Yield	Amount	Weighted Average Yield	Amount	Weighted Average Yield
Held to maturity:										
U.S. Treasury	$—	— %	$248,592	3.44%	$—	— %	$—	— %	$248,592	3.44%
Residential mortgage-backed securities	—	—	359	3.94	2,238	1.59	7,077	3.12	9,674	2.80
States and political subdivisions	117,581	6.63	243,550	6.16	145,483	5.07	2,373,868	5.53	2,880,482	5.61
Other	—	—	1,000	1.20	—	—	—	—	1,000	1.20
Total	$117,581	6.63	$493,501	4.78	$147,721	5.02	$2,380,945	5.52	$3,139,748	5.42
Available for sale:										
U.S. Treasury	$1,501,679	0.39%	$1,038,875	1.54%	$—	— %	$—	— %	$2,540,554	0.86%
U.S. Government agencies/corporations	—	—	53,980	0.26	—	—	—	—	53,980	0.26
Residential mortgage-backed securities	1	9.59	113,437	4.61	606,819	2.02	1,055,759	3.85	1,776,016	3.26
States and political subdivisions	29,710	6.11	40,370	5.99	964,144	3.26	454,690	6.26	1,488,914	4.29
Other	—	—	—	—	—	—	—	—	35,972	—
Total	$1,531,390	0.50	$1,246,662	1.89	$1,570,963	2.79	$1,510,449	4.59	$5,895,436	2.44

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. Securities are classified as available for sale when they might be sold before maturity. Securities available for sale are carried at fair value, with unrealized holding gains and losses reported in other comprehensive income, net of tax. The remaining securities are classified as trading. Trading securities are held primarily for sale in the near term and are carried at their fair values, with unrealized gains and losses included immediately in other income. Management determines the appropriate classification of securities at the time of purchase. Securities with limited marketability, such as stock in the Federal Reserve Bank and the Federal Home Loan Bank, are carried at cost.

All mortgage-backed securities included in the above tables were issued by U.S. government agencies and corporations. At December 31, 2013, approximately 96.3% of the securities in the Corporation's municipal bond portfolio were issued by political subdivisions or agencies within the State of Texas, of which approximately 72.0% are either guaranteed by the Texas Permanent School Fund, which has a "triple-A" insurer financial strength rating, or secured by U.S. Treasury securities via defeasance of the debt by the issuers. At December 31, 2013, the Corporation held securities with an aggregate carrying value of $252.7 million and an aggregate fair value of $252.0 million issued by the Dallas, Texas Independent School District. Such amounts were in excess of 10% of the Corporation's shareholders' equity at December 31, 2013. At such date, all of these securities were either guaranteed by the Texas Permanent School Fund or secured by U.S. Treasury securities via defeasance of the debt. At December 31, 2013, there were no other holdings of any one issuer, other than the U.S. government and its agencies, in an amount greater than 10% of the Corporation's shareholders' equity.

The average taxable-equivalent yield on the securities portfolio was 3.48% in 2013 compared to 3.31% in 2012 and 4.57% in 2011. The increase, from 2012 to 2013, was primarily related to an increase in the relative proportion of investments held in higher-yielding, tax-exempt municipal securities. The decrease, from 2011 to 2012, was primarily related to a decrease in the yield on taxable securities as proceeds from principal repayments were reinvested at lower market rates. Tax-exempt municipal securities totaled 40.7% of average securities in 2013 compared to 27.4% in 2012 and 35.2% in 2011. The average yield on taxable securities was 1.90% in 2013 compared to 2.10% in 2012 and 3.27% in 2011, while the average taxable-equivalent yield on tax-exempt securities was 5.75% in 2013 compared to 6.68% in 2012 and 6.97% in 2011. See the section captioned "Net Interest Income" included elsewhere in this discussion. The overall growth in the securities portfolio since 2011 was primarily funded by deposit growth.

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Deposits

The table below presents the daily average balances of deposits by type and weighted-average rates paid thereon during the years presented:

	2013		2012		2011	
	Average Balance	Average Rate Paid	Average Balance	Average Rate Paid	Average Balance	Average Rate Paid
Non-interest-bearing demand deposits:						
Commercial and individual	$6,967,933		$6,300,944		$5,093,948	
Correspondent banks	323,706		332,136		324,954	