

HEARTLAND FINANCIAL USA INC  
Form 10-Q  
November 09, 2016

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

FORM 10-Q  
 QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For quarterly period ended September 30, 2016

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

For transition period \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 001-15393

HEARTLAND FINANCIAL USA, INC.  
(Exact name of Registrant as specified in its charter)

Delaware  
(State or other jurisdiction of incorporation or organization)

42-1405748  
(I.R.S. employer identification number)

1398 Central Avenue, Dubuque, Iowa 52001  
(Address of principal executive offices)(Zip Code)

(563) 589-2000  
(Registrant's telephone number, including area code)

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

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

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "accelerated filer," "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Act.

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Large accelerated filer  Accelerated Filer

Non-accelerated filer  Smaller reporting company   
(Do not check if a smaller reporting company)

Indicate by check mark whether the Registrant is a shell company (as defined by Rule 12b-2 of the Securities Exchange Act of 1934). Yes  No

Indicate the number of shares outstanding of each of the classes of Registrant's common stock as of the latest practicable date: As of November 8, 2016, the Registrant had outstanding 26,062,541 shares of common stock, \$1.00 par value per share.

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HEARTLAND FINANCIAL USA, INC.  
Form 10-Q Quarterly Report  
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31.1 Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act.

31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act.

32.1 Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

101 Financial statements formatted in Extensible Business Reporting Language: (i) the Consolidated Balance Sheets, (ii) the Consolidated Statements of Income, (iii) the Consolidated Statements of Comprehensive Income, (iv) the Consolidated Statements of Cash Flows, (v) the Consolidated Statements of Changes in Equity, and (vi) the Notes to Consolidated Financial Statements.

## PART I

## ITEM 1. FINANCIAL STATEMENTS

HEARTLAND FINANCIAL USA, INC.  
CONSOLIDATED BALANCE SHEETS

(Dollars in thousands, except per share data)

	September 30, 2016 (Unaudited)	December 31, 2015
<b>ASSETS</b>		
Cash and due from banks	\$ 196,234	\$ 237,841
Federal funds sold and other short-term investments	5,855	20,958
Cash and cash equivalents	202,089	258,799
Time deposits in other financial institutions	2,105	2,355
Securities:		
Available for sale, at fair value (cost of \$1,652,938 at September 30, 2016, and \$1,584,703 at December 31, 2015)	1,655,696	1,578,434
Held to maturity, at cost (fair value of \$284,948 at September 30, 2016, and \$294,513 at December 31, 2015)	265,302	279,117
Other investments, at cost	22,082	21,443
Loans held for sale	78,317	74,783
Loans receivable:		
Held to maturity	5,438,715	5,001,486
Allowance for loan losses	(54,653)	(48,685)
Loans receivable, net	5,384,062	4,952,801
Premises, furniture and equipment, net	162,207	146,259
Premises, furniture and equipment held for sale	3,634	3,889
Other real estate, net	10,740	11,524
Goodwill	127,699	97,852
Core deposit intangibles, net	23,922	22,019
Servicing assets, net	35,906	34,926
Cash surrender value on life insurance	112,060	110,297
Other assets	116,394	100,256
<b>TOTAL ASSETS</b>	<b>\$ 8,202,215</b>	<b>\$ 7,694,754</b>
<b>LIABILITIES AND EQUITY</b>		
<b>LIABILITIES:</b>		
Deposits:		
Demand	\$ 2,238,736	\$ 1,914,141
Savings	3,753,300	3,367,479
Time	920,657	1,124,203
Total deposits	6,912,693	6,405,823
Short-term borrowings	214,105	293,898
Other borrowings	294,493	263,214
Accrued expenses and other liabilities	76,536	68,646
<b>TOTAL LIABILITIES</b>	<b>7,497,827</b>	<b>7,031,581</b>
<b>STOCKHOLDERS' EQUITY:</b>		
Series C Senior Non-Cumulative Perpetual Preferred Stock (par value \$1 per share; 0 shares and 81,698 shares outstanding at September 30, 2016, and December 31, 2015,	—	81,698

respectively)

Series D Senior Non-Cumulative Perpetual Convertible Preferred Stock (par value \$1 per share; 3,000 shares authorized and 1,078 shares issued and outstanding at September 30, 2016; 0 shares authorized, issued and outstanding at December 31, 2015)	1,357	—
Common stock (par value \$1 per share; 30,000,000 shares authorized at both September 30, 2016, and December 31, 2015; issued 24,683,277 shares at September 30, 2016, and 22,435,693 shares at December 31, 2015)	24,683	22,436
Capital surplus	279,316	216,436
Retained earnings	402,179	348,630
Accumulated other comprehensive income (loss)	(3,079	) (6,027 )
Treasury stock at cost (1,897 shares at September 30, 2016, and 0 shares at December 31, 2015)	(68	) —
<b>TOTAL STOCKHOLDERS' EQUITY</b>	<b>704,388</b>	<b>663,173</b>
<b>TOTAL LIABILITIES AND EQUITY</b>	<b>\$ 8,202,215</b>	<b>\$ 7,694,754</b>

See accompanying notes to consolidated financial statements.

HEARTLAND FINANCIAL USA, INC.  
CONSOLIDATED STATEMENTS OF INCOME (Unaudited)  
(Dollars in thousands, except per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
<b>INTEREST INCOME:</b>				
Interest and fees on loans	\$70,046	\$58,328	\$208,280	\$167,201
Interest on securities:				
Taxable	7,917	5,858	24,604	19,729
Nontaxable	3,717	3,077	10,793	8,867
Interest on federal funds sold	1	1	12	3
Interest on interest bearing deposits in other financial institutions	6	4	13	11
<b>TOTAL INTEREST INCOME</b>	<b>81,687</b>	<b>67,268</b>	<b>243,702</b>	<b>195,811</b>
<b>INTEREST EXPENSE:</b>				
Interest on deposits	4,001	3,767	12,195	11,758
Interest on short-term borrowings	235	228	1,083	638
Interest on other borrowings (includes \$492 and \$557 of interest expense related to derivatives reclassified from accumulated other comprehensive income for the three months ended September 30, 2016 and 2015, respectively, and \$1,463 and \$1,680 of interest expense related to derivatives reclassified from accumulated other comprehensive income for the nine months ended September 30, 2016 and 2015, respectively)	3,770	3,549	10,918	12,117
<b>TOTAL INTEREST EXPENSE</b>	<b>8,006</b>	<b>7,544</b>	<b>24,196</b>	<b>24,513</b>
<b>NET INTEREST INCOME</b>	<b>73,681</b>	<b>59,724</b>	<b>219,506</b>	<b>171,298</b>
Provision for loan losses	5,328	3,181	9,513	10,526
<b>NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES</b>	<b>68,353</b>	<b>56,543</b>	<b>209,993</b>	<b>160,772</b>
<b>NONINTEREST INCOME:</b>				
Service charges and fees	8,278	6,350	23,462	17,654
Loan servicing income	873	1,368	3,433	3,572
Trust fees	3,689	3,507	11,127	11,051
Brokerage and insurance commissions	1,006	869	2,914	2,872
Securities gains, net (includes \$1,586 and \$1,807 of net security gains reclassified from accumulated other comprehensive income for the three months ended September 30, 2016 and 2015, respectively, and \$9,964 and \$9,270 of net security gains reclassified from accumulated other comprehensive income for the nine months ended September 30, 2016 and 2015, respectively)	1,584	1,767	9,732	9,230
Net gains on sale of loans held for sale	11,459	9,823	33,794	38,164
Valuation allowance on commercial servicing rights	5	—	(41)	—
Income on bank owned life insurance	620	372	1,733	1,355
Other noninterest income	1,028	924	2,992	2,406
<b>TOTAL NONINTEREST INCOME</b>	<b>28,542</b>	<b>24,980</b>	<b>89,146</b>	<b>86,304</b>
<b>NONINTEREST EXPENSES:</b>				
Salaries and employee benefits	40,733	37,033	124,432	110,522
Occupancy	5,099	4,307	15,322	12,594
Furniture and equipment	2,746	2,121	7,301	6,403
Professional fees	5,985	5,251	20,481	16,544

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FDIC insurance assessments	1,180	1,018	3,468	2,873
Advertising	1,339	1,327	4,174	3,841
Intangible assets amortization	1,291	734	4,483	2,080
Other real estate and loan collection expenses	640	496	1,871	1,714
(Gain)/loss on sales/valuations of assets, net	794	721	1,064	2,583
Other noninterest expenses	8,620	8,988	27,160	25,938
<b>TOTAL NONINTEREST EXPENSES</b>	<b>68,427</b>	<b>61,996</b>	<b>209,756</b>	<b>185,092</b>
<b>INCOME BEFORE INCOME TAXES</b>	<b>28,468</b>	<b>19,527</b>	<b>89,383</b>	<b>61,984</b>
Income taxes (includes \$408 and \$451 of income tax expense reclassified from accumulated other comprehensive income for the three months ended September 30, 2016 and 2015, respectively, and \$3,171 and \$2,816 of income tax expense reclassified from accumulated other comprehensive income for the nine months ended September 30, 2016 and 2015, respectively)	8,260	4,945	28,196	16,533
<b>NET INCOME</b>	<b>20,208</b>	<b>14,582</b>	<b>61,187</b>	<b>45,451</b>
Preferred dividends	(53 )	(205 )	(273 )	(613 )
Interest expense on convertible preferred debt	17	—	48	—
<b>NET INCOME AVAILABLE TO COMMON STOCKHOLDERS</b>	<b>\$20,172</b>	<b>\$14,377</b>	<b>\$60,962</b>	<b>\$44,838</b>
<b>EARNINGS PER COMMON SHARE - BASIC</b>	<b>\$0.82</b>	<b>\$0.70</b>	<b>\$2.51</b>	<b>\$2.19</b>
<b>EARNINGS PER COMMON SHARE - DILUTED</b>	<b>\$0.81</b>	<b>\$0.69</b>	<b>\$2.48</b>	<b>\$2.16</b>
<b>CASH DIVIDENDS DECLARED PER COMMON SHARE</b>	<b>\$0.10</b>	<b>\$0.10</b>	<b>\$0.30</b>	<b>\$0.30</b>

See accompanying notes to consolidated financial statements.

## HEARTLAND FINANCIAL USA, INC.

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)

(Dollars in thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
NET INCOME	\$20,208	\$14,582	\$61,187	\$45,451
OTHER COMPREHENSIVE INCOME				
Securities:				
Net change in unrealized gain (loss) on securities	(5,696 )	2,202	18,274	10,916
Reclassification adjustment for net gains realized in net income	(1,586 )	(1,807 )	(9,964 )	(9,270 )
Net change in non-credit related other than temporary impairment	—	24	7	72
Income taxes	2,871	(169 )	(3,364 )	(667 )
Other comprehensive income (loss) on securities	(4,411 )	250	4,953	1,051
Derivatives used in cash flow hedging relationships:				
Net change in unrealized gain (loss) on derivatives	844	(3,071 )	(4,623 )	(3,016 )
Reclassification adjustment for net losses on derivatives realized in net income	492	557	1,463	1,680
Income taxes	(517 )	936	1,155	488
Other comprehensive income (loss) on cash flow hedges	819	(1,578 )	(2,005 )	(848 )
Other comprehensive income (loss)	(3,592 )	(1,328 )	2,948	203
TOTAL COMPREHENSIVE INCOME	\$16,616	\$13,254	\$64,135	\$45,654

See accompanying notes to consolidated financial statements.



HEARTLAND FINANCIAL USA, INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)  
(Dollars in thousands)

	Nine Months Ended September 30,	
	2016	2015
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net income	\$61,187	\$45,451
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	22,975	16,325
Provision for loan losses	9,513	10,526
Net amortization of premium on securities	24,093	21,339
Securities gains, net	(9,732 )	(9,230 )
Stock based compensation	3,073	2,635
Write downs and losses on repossessed assets, net	1,094	1,686
Loans originated for sale	(863,354)	(1,087,510)
Proceeds on sales of loans held for sale	883,758	1,083,285
Net gains on sale of loans held for sale	(23,938 )	(27,102 )
Increase (decrease) in accrued interest receivable	(1,054 )	170
Increase in prepaid expenses	(128 )	(1,021 )
Increase (decrease) in accrued interest payable	332	(177 )
Capitalization of servicing rights	(9,856 )	(11,766 )
Valuation adjustment on commercial servicing rights	41	—
Write downs and losses on sales of assets, net	(30 )	897
Other, net	(2,419 )	8,137
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>95,555</b>	<b>53,645</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Proceeds from the sale of securities available for sale	768,617	877,077
Proceeds from the sale of securities held to maturity	4,557	—
Proceeds from the sale of other investments	4,722	12,917
Proceeds from the sale of time deposits in other financial institutions	—	2,925
Proceeds from the maturity of and principal paydowns on securities available for sale	130,549	124,084
Proceeds from the maturity of and principal paydowns on securities held to maturity	8,271	1,338
Proceeds from the maturity of and principal paydowns on time deposits in other financial institutions	250	250
Proceeds from the maturity of and principal paydowns on other investments	—	619
Purchase of securities available for sale	(888,903)	(774,657 )
Purchase of other investments	(1,875 )	(9,833 )
Net (increase) decrease in loans	138,725	(225,356 )
Purchase of bank owned life insurance policies	—	(1,100 )
Proceeds from bank owned life insurance policies	111	—
Capital expenditures	(8,318 )	(4,982 )
Net cash and cash equivalents received (paid) in acquisitions	8,084	(6,861 )
Proceeds from the sale of equipment	686	1,108
Proceeds on sale of OREO and other repossessed assets	3,266	6,328
<b>NET CASH PROVIDED BY INVESTING ACTIVITIES</b>	<b>168,742</b>	<b>3,857</b>



HEARTLAND FINANCIAL USA, INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS, CONTINUED (Unaudited)  
(Dollars in thousands)

	Nine Months Ended September 30,	
	2016	2015
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Net increase in demand deposits	160,313	191,361
Net increase (decrease) in savings deposits	51,530	(73,050 )
Net decrease in time deposit accounts	(353,084 )	(26,326 )
Net decrease in short-term borrowings	(101,409 )	(25,901 )
Proceeds from short term FHLB advances	243,100	276,100
Repayments of short term FHLB advances	(257,250 )	(270,000)
Proceeds from other borrowings	40,000	29,000
Repayments of other borrowings	(15,562 )	(134,803)
Redemption of preferred stock	(81,698 )	—
Purchase of treasury stock	(2,293 )	(2,856 )
Proceeds from issuance of common stock	1,863	2,330
Excess tax benefits on exercised stock options	1,121	671
Dividends paid	(7,638 )	(6,794 )
<b>NET CASH USED BY FINANCING ACTIVITIES</b>	<b>(321,007 )</b>	<b>(40,268 )</b>
Net increase (decrease) in cash and cash equivalents	(56,710 )	17,234
Cash and cash equivalents at beginning of year	258,799	73,871
<b>CASH AND CASH EQUIVALENTS AT END OF PERIOD</b>	<b>\$202,089</b>	<b>\$91,105</b>
Supplemental disclosures:		
Cash paid for income/franchise taxes	\$16,550	\$7,305
Cash paid for interest	\$23,864	\$24,690
Loans transferred to OREO	\$1,359	\$5,206
Purchases of securities available for sale, accrued, not paid	\$—	\$3,523
Sales of securities available for sale, accrued, not settled	\$250	\$—
Stock consideration granted for acquisition	\$57,433	\$53,052

See accompanying notes to consolidated financial statements.

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## HEARTLAND FINANCIAL USA, INC.

## CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY (Unaudited)

(Dollars in thousands, except per share data)

	Heartland Financial USA, Inc. Stockholders' Equity						
	Preferred Stock	Common Stock	Capital Surplus	Retained Earnings	Other Comprehensive Income (Loss)	Treasury Stock	Total Equity
Balance at January 1, 2015	\$81,698	\$18,511	\$95,816	\$298,764	\$1,528	\$—	\$496,317
Comprehensive income				45,451	203		45,654
Cash dividends declared:							
Series C Preferred, \$7.50 per share				(613)			(613)
Common, \$0.30 per share				(6,181)			(6,181)
Purchase of 54,389 shares of common stock						(2,856)	(2,856)
Issuance of 2,180,585 shares of common stock		2,129	51,162			2,762	56,053
Stock based compensation			2,635				2,635
Balance at September 30, 2015	\$81,698	\$20,640	\$149,613	\$337,421	\$1,731	\$(94)	\$591,009
Balance at January 1, 2016	\$81,698	\$22,436	\$216,436	\$348,630	\$(6,027)	\$—	\$663,173
Comprehensive income				61,187	2,948		64,135
Cash dividends declared:							
Series C Preferred, \$2.50 per share				(168)			(168)
Series D Preferred, \$35.00 per share				(105)			(105)
Common, \$0.30 per share				(7,365)			(7,365)
Redemption of Series C preferred stock (81,698)							(81,698)
Issuance of Series D preferred stock 3,777							3,777
Redemption of Series D preferred stock (2,420)							(2,420)
Purchase of 49,785 shares of common stock						(2,293)	(2,293)
Issuance of 2,295,472 shares of common stock		2,247	59,807			2,225	64,279
Stock based compensation			3,073				3,073
Balance at September 30, 2016	\$1,357	\$24,683	\$279,316	\$402,179	\$(3,079)	\$(68)	\$704,388

See accompanying notes to consolidated financial statements.

HEARTLAND FINANCIAL USA, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1: BASIS OF PRESENTATION

The interim unaudited consolidated financial statements contained herein should be read in conjunction with the audited consolidated financial statements and accompanying notes to the consolidated financial statements for the fiscal year ended December 31, 2015, included in the Form 10-K of Heartland Financial USA, Inc. ("Heartland") filed with the Securities and Exchange Commission ("SEC") on March 11, 2016. Accordingly, footnote disclosures which would substantially duplicate the disclosure contained in the audited consolidated financial statements have been omitted.

The financial information of Heartland included herein has been prepared in accordance with U.S. generally accepted accounting principles for interim financial reporting and has been prepared pursuant to the rules and regulations for reporting on Form 10-Q and Rule 10-01 of Regulation S-X. Such information reflects all adjustments (consisting of normal recurring adjustments), that are, in the opinion of management, necessary for a fair presentation of the financial position and results of operations for the periods presented. The results of the interim period ended September 30, 2016, are not necessarily indicative of the results expected for the year ending December 31, 2016.

Earnings Per Share

Basic earnings per share is determined using net income available to common stockholders and weighted average common shares outstanding. Diluted earnings per share is computed by dividing net income available to common stockholders by the weighted average common shares and assumed incremental common shares issued. Amounts used in the determination of basic and diluted earnings per share for the three- and nine-month periods ended September 30, 2016 and 2015, are shown in the table below:

	Three Months Ended September 30,	
(Dollars and number of shares in thousands, except per share data)	2016	2015
Net income attributable to Heartland	\$20,208	\$14,582
Preferred dividends and discount	(53 )	(205 )
Interest expense on convertible preferred debt	17	—
Net income available to common stockholders	\$20,172	\$14,377
Weighted average common shares outstanding for basic earnings per share	24,601	20,620
Assumed incremental common shares issued upon exercise of stock options and non-vested restricted stock units	322	273
Weighted average common shares for diluted earnings per share	24,923	20,893
Earnings per common share — basic	\$0.82	\$0.70
Earnings per common share — diluted	\$0.81	\$0.69
Number of antidilutive common stock equivalents excluded from diluted earnings per share computation	—	—
	Nine Months Ended September 30,	
(Dollars and number of shares in thousands, except per share data)	2016	2015
Net income attributable to Heartland		