QCR HOLDINGS INC
Form 10-K
March 11, 2016

U.S. SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES

EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2015.

Commission file number: 0-22208

QCR HOLDINGS, INC.

(Exact name of registrant as specified in its charter)

Delaware 42-1397595

(State of incorporation) (I.R.S. Employer Identification No.)

3551 7th Street, Moline, Illinois 61265

(Address of principal executive offices)

(309) 743-7724

(Registrant's telephone number, including area code)

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

Common stock, $1.00 Par Value The NASDAQ Global Market

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

Preferred Share Purchase Rights

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes [ ] No [X]

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act.

Yes [ ] No [X]

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 past 90 days. Yes [X] 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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes [X] No [ ]

Indicate by check mark if disclosure of delinquent filers in response to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of 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. [X]

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

Large accelerated filer [ ] Accelerated filer [X] Non-accelerated filer [ ] 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 [X]

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant, based on the last sales price quoted on The NASDAQ Global Market on June 30, 2015, the last business day of the registrant’s most recently completed second fiscal quarter, was approximately $235,581,715.

As of February 29, 2016, the Registrant had outstanding 11,812,011 shares of common stock, $1.00 par value per share.

Documents incorporated by reference:

Part III of Form 10-K - Proxy statement for annual meeting of stockholders to be held in May 2016.

QCR HOLDINGS, INC. AND SUBSIDIARIES

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Throughout the Notes to the Consolidated Financial Statements, Management's Discussion and Analysis of Financial Condition and Results of Operations, and remaining sections of this Form 10-K (including appendices), we use certain acronyms and abbreviations, as defined in Note 1 to the Consolidated Financial Statements.

Part I

Item 1. Business

General. QCR Holdings, Inc. is a multi-bank holding company headquartered in Moline, Illinois, that was formed in February 1993 under the laws of the state of Delaware. The Company serves the Quad Cities, Cedar Rapids, Waterloo/Cedar Falls and Rockford communities through the following three wholly-owned banking subsidiaries, which provide full-service commercial and consumer banking and trust and asset management services:

QCBT, which is based in Bettendorf, Iowa, and commenced operations in 1994;
CRBT, which is based in Cedar Rapids, Iowa, and commenced operations in 2001; and
RB&T, which is based in Rockford, Illinois, and commenced operations in 2005.

On May 13, 2013, the Company acquired Community National and its banking subsidiary, CNB. Community National and CNB commenced operations in 1997 and historically provided full-service commercial and consumer banking, and trust and asset management services, to Cedar Falls, Mason City, and Waterloo, Iowa and Austin, Minnesota. At acquisition, CNB had a total of eight branch facilities with four in the Waterloo/Cedar Falls area where CNB was headquartered, two in Mason City, and two in Austin. On October 4, 2013, the Company finalized the sale of the two branches in Mason City. On October 11, 2013, the Company finalized the sale of the two branches in Austin. On October 26, 2013, CNB merged with and into CRBT. CNB's merged branch offices operate as a division of CRBT under the name "Community Bank & Trust." In December 2013, one of the branch facilities in Cedar Falls was closed due to lack of sufficient customer activity. See Note 2 to the consolidated financial statements for further discussion of the acquisition of Community National and sales of certain CNB branches.

The Company also engages in direct financing lease contracts through m2, a wholly-owned subsidiary of QCBT based in Brookfield, Wisconsin. QCBT previously owned 80% of m2. In August 2012, QCBT entered into an amendment to the operating agreement of m2 and purchased the remaining 20% noncontrolling interest. See Note 23 to the consolidated financial statements for further discussion of the acquisition.

Subsidiary Banks. QCBT was capitalized on October 13, 1993, and commenced operations on January 7, 1994. QCBT is an Iowa-chartered commercial bank that is a member of the Federal Reserve System with depository accounts insured by the FDIC to the maximum amount permitted by law. QCBT provides full service commercial, correspondent, and consumer banking and trust and asset management services in the Quad Cities and adjacent communities through its five offices that are located in Bettendorf and Davenport, Iowa and in Moline, Illinois. QCBT, on a consolidated basis with m2, had total segment assets of $1.34 billion and $1.32 billion as of December 31, 2015 and 2014, respectively.

CRBT is an Iowa-chartered commercial bank that is a member of the Federal Reserve System with depository accounts insured by the FDIC to the maximum amount permitted by law. The Company commenced operations in Cedar Rapids in June 2001, operating a branch of QCBT. The Cedar Rapids branch operation then began functioning under the CRBT charter in September 2001. As previously discussed, the merged branches of CNB operate as a division of CRBT under the name “Community Bank & Trust.” CRBT provides full-service commercial and consumer banking and trust and asset management services to Cedar Rapids and Waterloo/Cedar Falls, Iowa and adjacent communities through its five facilities. The headquarters for CRBT is located in downtown Cedar Rapids with one other branch located in northern Cedar Rapids, two branches located in Waterloo and one branch located in Cedar Falls. CRBT had total segment assets of $866.9 million and $840.3 million as of December 31, 2015 and 2014, respectively.

RB&T is an Illinois-chartered commercial bank that is a member of the Federal Reserve System with depository accounts insured by the FDIC to the maximum amount permitted by law. The Company commenced operations in Rockford, Illinois in September 2004, operating a branch of QCBT, and that operation began functioning under the RB&T charter in January 2005. RB&T provides full-service commercial and consumer banking and trust and asset management services to Rockford and adjacent communities through its headquarters located on Guilford Road at Alpine Road in Rockford and its branch facility located in downtown Rockford. RB&T had total segment assets of $367.5 million and $353.4 million as of December 31, 2015 and 2014, respectively.

See Note 22 to the consolidated financial statements for additional business segment information.

Other Operating Subsidiaries. m2, which is based in Brookfield, Wisconsin, is engaged in the business of leasing machinery and equipment to C&I businesses under direct financing lease contracts.

Trust Preferred Subsidiaries. Following is a listing of the Company's non-consolidated subsidiaries formed for the issuance of trust preferred securities, including pertinent information as of December 31, 2015 and 2014:

Name	Date Issued	Amount Issued as of 12/31/15	Amount Issued as of 12/31/14	Interest Rate	Interest Rate as of 12/31/2015	Interest Rate as of 12/31/2014
QCR Holdings Statutory Trust II	February 2004	$10,310,000	$12,372,000	2.85% over 3-month LIBOR	3.18%	3.08%
QCR Holdings Statutory Trust III	February 2004	8,248,000	8,248,000	2.85% over 3-month LIBOR	3.18%	3.08%
QCR Holdings Statutory Trust IV	May 2005	5,155,000	5,155,000	1.80% over 3-month LIBOR	2.12%	2.03%
QCR Holdings Statutory Trust V	February 2006	10,310,000	10,310,000	1.55% over 3-month LIBOR	1.87%	1.78%
Community National Statutory Trust II	September 2004	3,093,000	3,093,000	2.17% over 3-month LIBOR	2.74%	2.42%
Community National Statutory Trust III	March 2007	3,609,000	3,609,000	1.75% over 3-month LIBOR	2.26%	1.99%
		$40,725,000	$42,787,000	Weighted Average Rate	2.60%	2.50%

Securities issued by all of the trusts listed above mature thirty years from the date of issuance, but are all currently callable at par at any time. Interest rate reset dates vary by trust.

QCR Holdings Statutory Trust IV was dissolved in 2016 after the Company purchased the related security at auction, as noted in Note 25 to the Consolidated Financial Statements.

Other Ownership Interests. In addition to its wholly-owned subsidiaries, the Company owns a 20% equity position in Nobel Real Estate Investors, LLC. In June 2005, CRBT entered into a joint venture as a 50% owner of Cedar Rapids Mortgage Company, LLC, which provided residential real estate mortgage lending services. During the first quarter of 2013, CRBT and the partner mutually terminated the joint venture. CRBT continues to provide residential real estate mortgage lending services through its consumer banking division. In December 2014, QCBT entered into a joint venture as a 20% owner of Ruhl Mortgage, to provide residential real estate mortgage lending services and products to QCBT clients.

Business. The Company's principal business consists of attracting deposits and investing those deposits in loans/leases and securities. The deposits of the subsidiary banks are insured to the maximum amount allowable by the FDIC. The Company's results of operations are dependent primarily on net interest income, which is the difference between the interest earned on its loans/leases and securities and the interest paid on deposits and borrowings. The Company's operating results are affected by economic and competitive conditions, particularly changes in interest rates, government policies and actions of regulatory authorities, as described more fully in this Form 10-K. Its operating results also can be affected by trust fees, investment advisory and management fees, deposit service charge fees, gains on the sale of residential real estate and government guaranteed loans, earnings from BOLI and other noninterest income. Operating expenses include employee compensation and benefits, occupancy and equipment expense, professional and data processing fees, advertising and marketing expenses, bank service charges, FDIC and other insurance, loan/lease expenses and other administrative expenses.

The Company and its subsidiaries collectively employed 406 and 409 FTEs at December 31, 2015 and 2014, respectively.

The Federal Reserve is the primary federal regulator of the Company and its subsidiaries. In addition, QCBT and CRBT are regulated by the Iowa Superintendent and RB&T is regulated by the IDFPR. The FDIC, as administrator of the Deposit Insurance Fund, also has regulatory authority over the subsidiary banks. See Appendix A for more information on the federal and state statutes and regulations that are applicable to the Company and its subsidiaries.

Lending/Leasing. The Company and its subsidiaries provide a broad range of commercial and retail lending/leasing and investment services to corporations, partnerships, individuals, and government agencies. The subsidiary banks actively market their services to qualified lending and deposit clients. Officers actively solicit the business of new clients entering their market areas as well as long-standing members of the local business community. The Company has an established lending/leasing policy which includes a number of underwriting factors to be considered in making a loan/lease, including, but not limited to, location, loan-to-value ratio, cash flow, collateral and the credit history of the borrower.

In accordance with Iowa regulation, the legal lending limit to one borrower for QCBT and CRBT, calculated as 15% of aggregate capital, was $19.7 million and $15.8 million, respectively, as of December 31, 2015. In accordance with Illinois regulation, the legal lending limit to one borrower for RB&T, calculated as 25% of aggregate capital, totaled $9.6 million as of December 31, 2015.

The Company recognizes the need to prevent excessive concentrations of credit exposure to any one borrower or group of related borrowers. As such, the Company has established an in-house lending limit, which is lower than each subsidiary bank’s legal lending limit, in an effort to manage individual borrower exposure levels.

The in-house lending limit is the maximum amount of credit each subsidiary bank will extend to a single borrowing entity or group of related entities. Under the in-house limit, total credit exposure to a single borrowing entity or group of related entities will not exceed the following, subject to certain exceptions:

QCBT:	$ 10.0 million
CRBT:	$ 7.5 million
RB&T:	$ 3.7 million

On a consolidated basis, the in-house lending limit is $15.0 million, which is the maximum amount of credit that all affiliated banks, when combined, will extend to a single borrowing entity or group of related entities, subject to certain exceptions.

In addition, m2’s in-house lending limit is $1.0 million to a single leasing entity or group of related entities.

As part of the loan monitoring activity at the three subsidiary banks, credit administration personnel interact closely with senior bank management. For example, the internal loan committee of each subsidiary bank meets weekly. The Company has a separate in-house loan review function to analyze credits of the subsidiary banks. To complement the in-house loan review, an independent third-party performs external loan reviews. Historically, management has attempted to identify problem loans at an early stage and to aggressively seek a resolution of those situations.

The Company recognizes that a diversified loan/lease portfolio contributes to reducing risk in the overall loan/lease portfolio. The specific loan/lease portfolio mix is subject to change based on loan/lease demand, the business environment and various economic factors. The Company actively monitors concentrations within the loan/lease portfolio to ensure appropriate diversification and concentration risk is maintained.

Specifically, each subsidiary bank's total loans as a percentage of average assets may not exceed 85%. In addition, following are established policy limits and the actual allocations for the three subsidiary banks as of December 31, 2015 for the loan portfolio on a per loan type basis, reflected as a percentage of the subsidiary bank's average gross loans:

Type of Loan *	QCBT Maximum Percentage per Loan Policy	As of December 31, 2015	CRBT Maximum Percentage per Loan Policy	As of December 31, 2015	RB&T Maximum Percentage per Loan Policy	As of December 31, 2015
One-to-four family residential	30%	14 %	25%	11 %	30%	20 %
Multi-family	15%	2 %	15%	7 %	15%	3 %
Farmland	5 %	1 %	5 %	1 %	5 %	0 %
Non-farm, nonresidential	50%	26 %	50%	34 %	50%	43 %
Construction and land development	20%	3 %	15%	6 %	20%	3 %
C&I	60%	20 %	60%	30 %	60%	26 %
Loans to individuals	10%	1 %	10%	1 %	10%	1 %
Lease financing	30%	21 %	5 %	0 %	20%	0 %
Bank stock loans	**	**	10%	1 %	10%	0 %
All other loans	15%	12 %	10%	9 %	10%	4 %
		100 %		100 %		100 %

* The loan types above are as defined and reported in the subsidiary banks' quarterly Reports of Condition and Income (also known as Call Reports).

** QCBT's maximum percentage for bank stock loans is 150% of aggregate capital (bank stock loan commitments are limited to 200% of aggregate capital). At December 31, 2015, QCBT's bank stock loans totaled 50% of aggregate capital.

The following table presents total loans/leases by major loan/lease type and subsidiary as of December 31, 2015 and 2014. Residential real estate loans held for sale are included in residential real estate loans below.

	QCBT		m2 Lease Funds		CRBT		RBT		Intercompany Eliminations	Consolidated Total	
	$	%	$	%	$	%	$	%	$	$	%
	(dollars in thousands)										
As of December 31, 2015:											
C&I loans	$267,367	39%	$20,120	10%	$263,792	43%	$96,881	33%	$-	$648,160	36%
CRE loans	296,157	43%	-	0%	285,866	46%	142,346	48%	-	724,369	40%
Direct financing leases	-	0%	173,656	86%	-	0%	-	0%	-	173,656	10%
Residential real estate loans	86,920	13%	-	0%	43,345	7%	40,168	14%	-	170,433	9%
Installment and other consumer loans	35,862	5%	-	0%	23,970	4%	13,837	5%	-	73,669	4%
Deferred loan/lease origination costs, net of fees	457	0%	7,343	4%	(358)	0%	294	0%	-	7,736	0%
	$686,763	100%	$201,119	100%	$616,615	100%	$293,526	100%	$-	$1,798,023	100%
As of December 31, 2014:											
C&I loans	$238,495	39%	$4,739	3%	$212,208	37%	$68,485	25%	$-	$523,927	32%
CRE loans	256,195	42%	-	0%	297,377	51%	150,031	55%	(1,463)	702,140	43%
Direct financing leases	-	0%	166,032	93%	-	0%	-	0%	-	166,032	10%
Residential real estate loans	75,095	13%	-	0%	43,863	8%	39,675	15%	-	158,633	10%
Installment and other consumer loans	35,213	6%	-	0%	24,252	4%	13,142	5%	-	72,607	5%
Deferred loan/lease origination costs, net of fees	80	0%	6,673	4%	(337)	0%	248	0%	-	6,664	0%

$605,078	100%	$177,444	100%	$577,363	100%	$271,581	100%	$(1,463)	$1,630,003	100%

Proper pricing of loans is necessary to provide adequate return to the Company's stockholders. Loan pricing, as established by the subsidiary banks' internal loan committees, includes consideration for the cost of funds, loan maturity and risk, origination and maintenance costs, appropriate stockholder return, competitive factors, and the economic environment. The portfolio contains a mix of loans with fixed and floating interest rates. Management attempts to maximize the use of interest rate floors on its variable rate loan portfolio. Refer to Item 7A. Quantitative and Qualitative Disclosures about Market Risk for more discussion on the Company's management of interest rate risk.

C&I Lending

As noted above, the subsidiary banks are active C&I lenders. The current areas of emphasis include loans to small and mid-sized businesses with a wide range of operations such as wholesalers, manufacturers, building contractors, business services companies, other banks, and retailers. The banks provide a wide range of business loans, including lines of credit for working capital and operational purposes, and term loans for the acquisition of facilities, equipment and other purposes. Since 2010, the subsidiary banks have been active in participating in lending programs offered by the SBA and USDA. Under these programs, the government entities will generally provide a guarantee of repayment ranging from 50% to 85% of the principal amount of the qualifying loan.

Loan approval is generally based on the following factors:

- Ability and stability of current management of the borrower;
- Stable earnings with positive financial trends;
- Sufficient cash flow to support debt repayment;
- Earnings projections based on reasonable assumptions;
- Financial strength of the industry and business; and
- Value and marketability of collateral.

For C&I loans, the Company assigns internal risk ratings which are largely dependent upon the aforementioned approval factors. The risk rating is reviewed annually or on an as needed basis depending on the specific circumstances of the loan. See Note 1 to the consolidated financial statements for additional information, including the internal risk rating scale.

As part of the underwriting process, management reviews current borrower financial statements. When appropriate, certain C&I loans may contain covenants requiring maintenance of financial performance ratios such as, but not limited to:

- Minimum debt service coverage ratio;
- Minimum current ratio;
- Maximum debt to tangible net worth ratio; and/or
- Minimum tangible net worth.

Establishment of these financial performance ratios depends on a number of factors, including risk rating and the specific industry.

Collateral for these loans generally includes accounts receivable, inventory, equipment, and real estate. The Company's lending policy specifies approved collateral types and corresponding maximum advance percentages. The value of collateral pledged on loans must exceed the loan amount by a margin sufficient to absorb potential erosion of its value in the event of foreclosure and cover the loan amount plus costs incurred to convert it to cash. Approved non-real estate collateral types and corresponding maximum advance percentages for each are listed below.

Approved Collateral Type	**Maximum Advance %**
Financial Instruments	
U.S. Government Securities	90% of market value
Securities of Federal Agencies	90% of market value
Municipal Bonds rated by Moody's As "A" or better	80% of market value
Listed Stocks	75% of market value
Mutual Funds	75% of market value
Cash Value Life Insurance	95%, less policy loans
Savings/Time Deposits (Bank)	100% of current value
General Business	
Accounts Receivable	80% of eligible accounts
Inventory	50% of value
Fixed Assets (Existing)	50% of net book value, or 75% of orderly liquidation appraised value
Fixed Assets (New)	80% of cost
Leasehold Improvements	0%

Generally, if the above collateral is part of a cross-collateralization with other approved assets, then the maximum advance percentage may be higher.

The Company's lending policy specifies maximum term limits for C&I loans. For term loans, the maximum term is generally seven years. Generally, term loans range from three to five years. For lines of credit, the maximum term is typically 365 days.

In addition, the subsidiary banks often take personal guarantees or cosignors to help assure repayment. Loans may be made on an unsecured basis if warranted by the overall financial condition of the borrower.

CRE Lending

The subsidiary banks also make CRE loans. CRE loans are subject to underwriting standards and processes similar to C&I loans, in addition to those standards and processes specific to real estate loans. Collateral for these loans generally includes the underlying real estate and improvements, and may include additional assets of the borrower. The Company’s lending policy specifies maximum loan-to-value limits based on the category of CRE (commercial real estate loans on improved property, raw land, land development, and commercial construction). These limits are the same limits as, or in some situations, more conservative than, those established by regulatory authorities. Following is a listing of these limits as well as some of the other guidelines included in the Company’s lending policy for the major categories of CRE loans:

CRE Loan Types	**Maximum Advance Rate ****	**Maximum Term**
CRE Loans on Improved Property *	80%	7 years
Raw Land	Lesser of 90% of project cost, or 65% of "as is" appraised value	12 months
Land Development	Lesser of 90% of project cost, or 75% of appraised value	24 months
Commercial Construction Loans	Lesser of 90% of project cost, or 80% of appraised value	365 days

* Generally, the debt service coverage ratio must be a minimum of 1.25x for non-owner occupied loans and 1.15x for owner-occupied loans. For loans greater than $500 thousand, the subsidiary banks sensitize this ratio for deteriorated economic conditions, major changes in interest rates, and/or significant increases in vacancy rates.

** These maximum rates are consistent with, or in some situations, more conservative than, those established by regulatory authorities.

The Company’s lending policy also includes guidelines for real estate appraisals and evaluations, including minimum appraisal and evaluation standards based on certain transactions. In addition, the subsidiary banks often take personal guarantees to help assure repayment.

In addition, management tracks the level of owner-occupied CRE loans versus non-owner occupied CRE loans. Owner-occupied CRE loans are generally considered to have less risk. As of December 31, 2015 and 2014, approximately 35% and 37%, respectively, of the CRE loan portfolio was owner-occupied.

The Company's lending policy limits non-owner occupied CRE lending to 300% of total risk-based capital, and limits construction, land development, and other land loans to 100% of total risk-based capital. Exceeding these limits warrants the use of heightened risk management practices in accordance with regulatory guidelines. As of December 31, 2015, all three subsidiary banks were in compliance with these limits.

Following is a listing of the significant industries within the Company's CRE loan portfolio as of December 31, 2015 and 2014:

	2015 Amount	%	2014 Amount	%
	(dollars in thousands)			
Lessors of Nonresidential Buildings	$264,133	37 %	$248,326	35%
Lessors of Residential Buildings	89,189	12 %	73,781	11%
Lessors of Other Real Estate Property	22,009	3 %	17,553	3 %
Hotels	19,228	3 %	16,252	2 %
Land Subdivision	17,839	2 %	19,504	3 %
Nursing Care Facilities	17,288	2 %	17,078	2 %
New Car Dealers	11,656	2 %	16,090	2 %
Other *	283,027	39 %	293,556	42%
Total Commercial Real Estate Loans	$724,369	100%		