HEARTLAND FINANCIAL USA INC
Form 10-Q
May 06, 2016

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

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

For quarterly period ended March 31, 2016

o 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 x No o

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 x No o

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.

Large accelerated filer ¨ Accelerated Filer x

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 o No x

Indicate the number of shares outstanding of each of the classes of Registrant's common stock as of the latest practicable date: As of May 5, 2016, the Registrant had outstanding 24,521,747 shares of common stock, $1.00 par value per share.

HEARTLAND FINANCIAL USA, INC.
Form 10-Q Quarterly Report
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PART I

ITEM 1. FINANCIAL STATEMENTS

HEARTLAND FINANCIAL USA, INC.
CONSOLIDATED BALANCE SHEETS
(Dollars in thousands, except per share data)

	March 31, 2016 (Unaudited)	December 31, 2015
ASSETS		
Cash and due from banks	$124,060	$237,841
Federal funds sold and other short-term investments	9,168	20,958
Cash and cash equivalents	133,228	258,799
Time deposits in other financial institutions	2,355	2,355
Securities:		
Available for sale, at fair value (cost of $1,680,299 at March 31, 2016, and $1,584,703 at December 31, 2015)	1,690,516	1,578,434
Held to maturity, at cost (fair value of $289,446 at March 31, 2016, and $294,513 at December 31, 2015)	271,300	279,117
Other investments, at cost	22,325	21,443
Loans held for sale	76,565	74,783
Loans and leases receivable:		
Held to maturity	5,503,005	5,001,486
Allowance for loan and lease losses	(49,738)	(48,685)
Loans and leases receivable, net	5,453,267	4,952,801
Premises, furniture and equipment, net	160,899	146,259
Premises, furniture and equipment held for sale	3,889	3,889
Other real estate, net	11,338	11,524
Goodwill	127,699	97,852
Other intangible assets, net	61,420	56,945
Cash surrender value on life insurance	110,834	110,297
Other assets	128,144	100,256
TOTAL ASSETS	$8,253,779	$7,694,754
LIABILITIES AND EQUITY		
LIABILITIES:		
Deposits:		
Demand	$2,079,521	$1,914,141
Savings	3,702,431	3,367,479
Time	1,142,368	1,124,203
Total deposits	6,924,320	6,405,823
Short-term borrowings	325,741	293,898
Other borrowings	265,760	263,214
Accrued expenses and other liabilities	68,415	68,646
TOTAL LIABILITIES	7,584,236	7,031,581
STOCKHOLDERS' EQUITY:		
Series C Senior Non-Cumulative Perpetual Preferred Stock (par value $1 per share; 0 shares and 81,698 shares outstanding at March 31, 2016 and December 31, 2015, respectively)	—	81,698

Series D Senior Non-Cumulative Perpetual Convertible Preferred Stock (par value $1 per share; authorized, issued and outstanding 3,000 shares at March 31, 2016, and 0 shares authorized, issued and outstanding at December 31, 2015)	3,777	—
Common stock (par value $1 per share; 30,000,000 shares authorized at both March 31, 2016, and December 31, 2015; issued 24,519,928 shares at March 31, 2016, and 22,435,693 shares at December 31, 2015)	24,520	22,436
Capital surplus	273,310	216,436
Retained earnings	366,014	348,630
Accumulated other comprehensive income (loss)	1,924	(6,027)
Treasury stock at cost (65 shares at March 31, 2016, and 0 shares at December 31, 2015)	(2)	—
TOTAL STOCKHOLDERS' EQUITY	669,543	663,173
TOTAL LIABILITIES AND EQUITY	$ 8,253,779	$ 7,694,754

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 March 31,	
	2016	2015
INTEREST INCOME:		
Interest and fees on loans and leases	$68,425	$53,049
Interest on securities:		
Taxable	8,735	7,132
Nontaxable	3,510	2,916
Interest on federal funds sold	10	1
Interest on interest bearing deposits in other financial institutions	4	4
TOTAL INTEREST INCOME	80,684	63,102
INTEREST EXPENSE:		
Interest on deposits	4,173	4,172
Interest on short-term borrowings	329	198
Interest on other borrowings (includes $506 and $564 of interest expense related to derivatives reclassified from accumulated other comprehensive income (loss) for the three months ended March 31, 2016 and 2015, respectively)	3,475	4,802
TOTAL INTEREST EXPENSE	7,977	9,172
NET INTEREST INCOME	72,707	53,930
Provision for loan and lease losses	2,067	1,671
NET INTEREST INCOME AFTER PROVISION FOR LOAN AND LEASE LOSSES	70,640	52,259
NONINTEREST INCOME:		
Service charges and fees	7,162	5,404
Loan servicing income	1,268	1,041
Trust fees	3,813	3,631
Brokerage and insurance commissions	1,022	1,087
Securities gains, net (includes $3,756 and $4,353 of net security gains reclassified from accumulated other comprehensive income for the three months ended March 31, 2016 and 2015, respectively)	3,526	4,353
Net gains on sale of loans held for sale	11,065	13,742
Income on bank owned life insurance	522	524
Other noninterest income	1,200	881
TOTAL NONINTEREST INCOME	29,578	30,663
NONINTEREST EXPENSES:		
Salaries and employee benefits	41,714	36,638
Occupancy	5,003	4,259
Furniture and equipment	2,113	2,106
Professional fees	7,010	6,044
FDIC insurance assessments	1,168	956
Advertising	1,284	1,181
Intangible assets amortization	1,895	631
Other real estate and loan collection expenses	572	465
Loss on sales/valuations of assets, net	313	353
Other noninterest expenses	9,237	6,981
TOTAL NONINTEREST EXPENSES	70,309	59,614

INCOME BEFORE INCOME TAXES	29,909	23,308
Income taxes (includes $1,212 and $1,413 of income tax expense reclassified from accumulated other comprehensive income for the three months ended March 31, 2016 and 2015, respectively)	9,900	7,599
NET INCOME	20,009	15,709
Preferred dividends	(168)	(204)
NET INCOME AVAILABLE TO COMMON STOCKHOLDERS	$19,841	$15,505
EARNINGS PER COMMON SHARE - BASIC	$0.84	$0.77
EARNINGS PER COMMON SHARE - DILUTED	$0.82	$0.76
CASH DIVIDENDS DECLARED PER COMMON SHARE	$0.10	$0.10

See accompanying notes to consolidated financial statements.

HEARTLAND FINANCIAL USA, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)
(Dollars in thousands)

	Three Months Ended March 31,	
	2016	2015
NET INCOME	$20,009	$15,709
OTHER COMPREHENSIVE INCOME		
Securities:		
Net change in unrealized gain on securities	20,067	11,478
Reclassification adjustment for net gains realized in net income	(3,756)	(4,353)
Net change in non-credit related other than temporary impairment	7	24
Income taxes	(6,524)	(2,859)
Other comprehensive income on securities	9,794	4,290
Derivatives used in cash flow hedging relationships:		
Net change in unrealized loss on derivatives	(3,423)	(1,454)
Reclassification adjustment for net loss on derivatives realized in net income	506	564
Income taxes	1,074	327
Other comprehensive loss on cash flow hedges	(1,843)	(563)
Other comprehensive income	7,951	3,727
TOTAL COMPREHENSIVE INCOME	$27,960	$19,436

See accompanying notes to consolidated financial statements.

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

	Three Months Ended March 31,	
	2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$20,009	$15,709
Adjustments to reconcile net income to net cash provided (used) by operating activities:		
Depreciation and amortization	7,713	5,747
Provision for loan and lease losses	2,067	1,671
Net amortization of premium on securities	7,846	6,949
Securities gains, net	(3,526)	(4,353)
Stock based compensation	1,087	1,139
Write downs and losses on repossessed assets, net	313	353
Loans originated for sale	(227,823)	(311,140)
Proceeds on sales of loans held for sale	234,516	287,768
Net gains on sale of loans held for sale	(8,475)	(11,056)
Decrease in accrued interest receivable	787	3,234
(Increase) decrease in prepaid expenses	598	(513)
Increase in accrued interest payable	637	627
Capitalization of servicing rights	(2,590)	(2,818)
Other, net	(9,855)	(11,472)
NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	23,304	(18,155)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from the sale of securities available for sale	303,448	289,466
Proceeds from the sale of securities held to maturity	4,057	—
Proceeds from the sale of other investments	2,830	5,489
Proceeds from the maturity of and principal paydowns on securities available for sale	35,379	37,479
Proceeds from the maturity of and principal paydowns on securities held to maturity	3,254	208
Purchase of securities available for sale	(362,764)	(232,422)
Purchase of other investments	(226)	(2,004)
Net increase in loans and leases	78,502	25,684
Capital expenditures	(898)	(2,919)
Net cash and cash equivalents received in acquisition	8,084	7,103
Proceeds from the sale of equipment	—	13
Proceeds on sale of OREO and other repossessed assets	2,384	2,312
NET CASH PROVIDED BY INVESTING ACTIVITIES	74,050	130,409

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

	Three Months Ended March 31, 2016	Three Months Ended March 31, 2015
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net increase in demand deposits and savings accounts	1,759	90,075
Net decrease in time deposit accounts	(131,373)	(25,618)
Net increase (decrease) in short-term borrowings	1,077	(31,765)
Proceeds from short term FHLB advances	5,000	60,000
Repayments of short term FHLB advances	(10,000)	(124,000)
Proceeds from other borrowings	—	4,000
Repayments of other borrowings	(5,501)	(44,488)
Redemption of preferred stock	(81,698)	—
Purchase of treasury stock	(1,227)	(1,780)
Proceeds from issuance of common stock	563	832
Excess tax benefits on exercised stock options	1,100	612
Dividends paid	(2,625)	(2,261)
NET CASH USED BY FINANCING ACTIVITIES	(222,925)	(74,393)
Net increase (decrease) in cash and cash equivalents	(125,571)	37,861
Cash and cash equivalents at beginning of year	258,799	73,871
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$133,228	$111,732
Supplemental disclosures:		
Cash paid for income/franchise taxes	$2,305	$840
Cash paid for interest	$7,340	$8,545
Loans transferred to OREO	$442	$2,371
Purchases of securities available for sale, accrued, not paid	$—	$5,149
Sales of securities available for sale, accrued, not settled	$17,189	$—
Stock consideration granted for acquisition	$57,433	$53,052

See accompanying notes to consolidated financial statements.

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	Accumulated 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				15,709	3,727		19,436
Cash dividends declared:							
Series C Preferred, $2.50 per share				(204)			(204)
Common, $0.10 per share				(2,057)			(2,057)
Purchase of 24,886 shares of common stock						(1,780)	(1,780)
Issuance of 2,098,833 shares of common stock		2,075	50,687			1,734	54,496
Stock based compensation			1,139				1,139
Balance at March 31, 2015	$81,698	$20,586	$147,642	$312,212	$ 5,255	$ (46)	$567,347
Balance at January 1, 2016	$81,698	$22,436	$216,436	$348,630	$ (6,027)	$ —	$663,173
Comprehensive income				20,009	7,951		27,960
Cash dividends declared:							
Series C Preferred, $2.50 per share				(168)			(168)
Common, $0.10 per share				(2,457)			(2,457)
Redemption of Series C preferred stock	(81,698)						(81,698)
Issuance of Series D preferred stock	3,777						3,777
Purchase of 20,070 shares of common stock						(1,227)	(1,227)
Issuance of 2,104,305 shares of common stock		2,084	55,787			1,225	59,096
Stock based compensation			1,087				1,087
Balance at March 31, 2016	$3,777	$24,520	$273,310	$366,014	$ 1,924	$ (2)	$669,543

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 March 31, 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 months ended March 31, 2016 and 2015, are shown in the table below:

	Three Months Ended March 31, 2016	
(Dollars and number of shares in thousands, except per share data)	2016	2015
Net income attributable to Heartland	$20,009	$15,709
Preferred dividends	(168)	(204)
Net income available to common stockholders	$19,841	$15,505
Weighted average common shares outstanding for basic earnings per share	23,657	20,215
Assumed incremental common shares issued upon exercise of stock options and non-vested restricted stock units	460	278
Weighted average common shares for diluted earnings per share	24,117	20,493
Earnings per common share — basic	$0.84	$0.77
Earnings per common share — diluted	$0.82	$0.76
Number of antidilutive common stock equivalents excluded from diluted earnings per share computation	57	—

Stock-Based Compensation

Heartland may grant, through its Nominating and Compensation Committee (the "Compensation Committee"), non-qualified and incentive stock options, stock appreciation rights, stock awards, restricted stock, restricted stock units and cash incentive awards, under its 2012 Long-Term Incentive Plan (the "Plan"). The Plan, which was approved by stockholders in May 2012 and replaced Heartland's 2005 Long-Term Incentive Plan with respect to grants after such approval, reserved 162,868 shares of common stock at March 31, 2016, for issuance under future awards that may be granted under the Plan to employees and directors of, and service providers to, Heartland or its subsidiaries.

Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 718, "Compensation-Stock Compensation" requires the measurement of the cost of employee services received in exchange for an award of equity instruments based upon the fair value of the award on the grant date. The cost of the award is based upon its fair value estimated on the date of grant and recognized in the consolidated statements of income over the vesting period of the award. The fair market value of restricted stock and restricted stock units is based on the fair value of the underlying shares of common stock on the date of grant. The fair value of stock options is estimated on the date of grant using the Black-Scholes model.

The amount of tax benefit related to the exercise, vesting, and forfeiture of equity-based awards reflected in additional paid-in-capital, not taxes payable, was $1.1 million and $612,000 during the three months ended March 31, 2016 and 2015, respectively.

Restricted Stock Units

The Plan permits the Compensation Committee to grant restricted stock units ("RSUs"). In the first quarter of 2016, the Compensation Committee granted time-based RSUs with respect to 72,644 shares of common stock, and in the first quarter of 2015, the Compensation Committee granted time-based RSUs with respect to 78,220 shares of common stock to selected officers. The time-based RSUs represent the right, without payment, to receive shares of Heartland common stock at a specified date in the future. The time-based RSUs granted in 2016 vest over three years in equal installments on the first, second and third anniversaries of the grant date. The time-based RSUs granted in 2015 vest over five years in equal installments on the third, fourth, and fifth anniversaries of the grant date. The time-based RSUs will be settled in common stock upon vesting, and will not be entitled to dividends until vested. The time-based RSUs may also vest upon death or disability, upon a change in control or upon a "qualified retirement" (as defined in the RSU agreement). The retiree is required to sign a non-solicitation and non-compete agreement as a condition to vesting.

In addition to the time-based RSUs referenced in the preceding paragraph, the Compensation Committee granted performance-based RSUs with respect to 35,516 shares of common stock in the first quarter of 2016, and 39,075 shares of common stock in the first quarter of 2015. These performance-based RSUs are earned based on satisfaction of performance targets for the fiscal years ended December 31, 2016, and December 31, 2015, respectively, and then fully vest two years after the end of the performance period. For the grants awarded in 2016, the portion of the RSUs earned based on performance vests on December 31, 2018, and for the grants awarded in 2015, the portion of the RSUs earned based on performance vests on December 31, 2017, subject to employment on the respective vesting dates. The performance-based RSUs vest to the extent that they are earned upon death or disability, upon a change in control or upon a "qualified retirement."

The Compensation Committee also granted performance-based RSUs with respect to 11,408 shares of common stock in the first quarter of 2016. These performance-based RSUs will be earned based on satisfaction of performance targets for the three-year performance period ended December 31, 2018. These performance-based RSUs will vest in 2019 after measurement of performance in relation to the performance targets. The performance-based RSUs vest to the extent that they are earned upon death or disability, upon a change in control or upon a "qualified retirement."

The Compensation Committee also grants RSUs under the Plan to directors as part of their compensation, to new management level employees at commencement of employment, and to other employees and service providers as incentives. During the three months ended March 31, 2016, and March 31, 2015, 150 and 300 RSUs, respectively, were granted to directors and new employees.

A summary of the RSUs outstanding as of March 31, 2016 and 2015, and changes during the three months ended March 31, 2016 and 2015, follows:

	2016		2015	
	Shares	Weighted-Average Grant Date Fair Value	Shares	Weighted-Average Grant Date Fair Value
Outstanding at January 1	353,195	$ 25.53	396,555	$ 21.48
Granted	119,718	29.05	117,595	27.87
Vested	(83,982)	20.79	(126,847)	16.66
Forfeited	(2,078)	27.17	(2,531)	23.82

Outstanding at March 31	386,853	$	27.53	384,772	$	25.00

Total compensation costs recorded for RSUs were $1.1 million for both three month periods ended March 31, 2016 and 2015. As of March 31, 2016, there were $5.2 million of total unrecognized compensation costs related to the 2005 and 2012 Long-Term Incentive Plans for RSUs which are expected to be recognized through 2019.

Options

Although the Plan provides authority to the Compensation Committee to grant stock options, no options were granted during the first three months of 2016 and 2015. Prior to 2009, options were typically granted annually with an expiration date ten years after the date of grant. Vesting was generally over a five-year service period with equal portions of a grant becoming exercisable at three years, four years, and five years after the date of grant. A summary of the stock options outstanding as of March 31, 2016 and 2015, and changes during the three months ended March 31, 2016 and 2015, follows:

	2016		2015	
	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Outstanding at January 1	125,950	$ 24.08	215,851	$ 23.85
Granted	—	—	—	—
Exercised	(19,750)	21.60	(32,400)	20.85
Forfeited	(1,250)	21.60	(1,500)	21.00
Outstanding at March 31	104,950	$ 24.58	181,951	$ 24.37
Options exercisable at March 31	104,950	$ 24.58	181,951	$ 24.37

At March 31, 2016, the vested options totaled 104,950 shares with a weighted average exercise price of $24.58 per share and a weighted average remaining contractual life of 1.15 years. The intrinsic value (the difference between the market price and the aggregate exercise price) for the vested options as of March 31, 2016, was $652,000. The intrinsic value for the total of all options exercised during the three months ended March 31, 2016, was $155,000.

The exercise price of stock options granted is established by the Compensation Committee, but the exercise price for the stock options may not be less than the fair market value of the shares on the date that the option is granted or, if greater, the par value of a share of stock. Each option granted is exercisable in full at any time or from time to time, subject to vesting provisions, as determined by the Compensation Committee and as provided in the option agreement, but such time may not exceed ten years from the grant date. Cash received from options exercised was $427,000 for the three months ended March 31, 2016, and $676,000 for the three months ended March 31, 2015.

Total compensation costs recorded for options were $0 for both three month periods ended March 31, 2016 and 2015. There are no unrecorded compensation costs related to options at March 31, 2016. No stock options vested during the three-month periods ended March 31, 2016 and 2015.

Subsequent Events

Heartland had no subsequent events through the filing date of this quarterly report on Form 10-Q with the SEC.

Effect of New Financial Accounting Standards

In May 2014, the FASB issued ASU 2014-09, "Revenue from Contracts with Customers." The amendment clarifies the principles for recognizing revenue and develops a common revenue standard. The amendment outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The core principle of the revenue model is that “an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services.” In applying the revenue model to contracts within its scope, an entity should apply the following steps: (i) identify the contract(s) with a customer, (ii) identify the performance obligations in the contract, (iii) determine the transaction price, (iv) allocate the transaction price to the performance obligations in the contract, and (v) recognize revenue when (or as) the entity satisfies a performance obligation. The amendment applies to all contracts with customers except those that are within the scope of other topics in the FASB Codification. The standard also requires significantly expanded disclosures about revenue recognition. The amendment is effective for annual reporting periods beginning after December 15, 2017 (including interim reporting periods within those periods). Early application is not permitted. Heartland intends to adopt the accounting standard during the first quarter of 2018, as required, and is currently evaluating the impact on its results of operations, financial position, and liquidity.

In November 2014, the FASB issued ASU 2014-16, "Derivatives and Hedging (Topic 815): Determining Whether a Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share is More Akin to Debt or to Equity." The amendment clarifies how current guidance should be interpreted in evaluating the characteristics and risks of a host contract in a hybrid financial instrument issued in the form of a share. One criterion requires evaluating whether the nature of the host contract is more akin to debt or to equity and whether the economic characteristics and risks of the embedded derivative feature are "clearly and closely related" to the host contract. In making that evaluation, an issuer or investor must consider all terms and features in a hybrid financial instrument including the embedded derivative feature that is being evaluated for separate accounting or may consider all terms and features in the hybrid financial instrument except for the embedded derivative feature that is being evaluated for separate accounting. This ASU is effective for annual periods and interim periods within those annual periods beginning after December 15, 2015, with early adoption permitted. Heartland adopted this standard on January 1, 2016, and the adoption of this standard did not have a material impact on its results of operations, financial position, and liquidity.

In January 2015, the FASB issued ASU 2015-01, "Income Statement-Extraordinary and Unusual Items." The amendment eliminates from U.S. GAAP the concept of extraordinary items. Presently, an event or transaction is presumed to be an ordinary and usual activity of the reporting entity unless evidence clearly supports its classification as an extraordinary item. If an event or transaction meets the criteria for extraordinary classification, an entity is required to segregate the extraordinary item from the results of ordinary operations and show the item separately in the income statement, net of tax, after income from continuing operations. This amended guidance will prohibit separate disclosure of extraordinary items in the income statement. This amendment is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. Entities may apply the amendment prospectively or retrospectively to all prior periods presented in the financial statements. Early adoption is permitted provided that the guidance is applied from the beginning of the fiscal year of adoption. Heartland adopted this standard on January 1, 2016, and the adoption of this standard did not have a material impact on the results of operations, financial position, and liquidity.

In April 2015, the FASB issued ASU 2015-05, "Intangibles-Goodwill and Other-Internal-Use Software." The amendment intends to provide guidance to customers about whether a cloud computing arrangement includes a software license. If a cloud computing arrangement includes a software license, then the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If a cloud computing arrangement does not include a software license, the customer should account for the arrangement as a service contract. The guidance will not change GAAP for a customer's accounting for service contracts. As a result, all software licenses within the scope of this guidance will be accounted for consistently with other licenses of intangible assets. This amendment is effective for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. Entities can elect to adopt the standard either retrospectively or prospectively to all cloud computing arrangements entered into or materially modified after the adoption date. Early adoption is permitted. Heartland adopted this standard on January 1, 2016 and the adoption did not have a material impact on the results of operations, financial position, and liquidity.

In September 2015, the FASB issued ASU 2015-16, "Simplifying the Accounting for Measurement-Period Adjustments." The amendment eliminates the requirement of Topic 805, Business Combinations, to retrospectively adjust the financial statements for measurement-period adjustments that occur in periods after a business combination is consummated. Measurement-period adjustments are calculated as if they were known at the acquisition date, but are recognized in the reporting period in which they are determined. Prior period information is not revised. Additional disclosures are required about the impact on current period income statement line items of adjustments that would have been recognized in prior periods if prior period information had been revised. This amendment is effective for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. Early adoption is permitted if financial statements have not been issued. Heartland adopted this standard effective September 30, 2015. The adoption of this standard did not have a material impact on the results of operations, financial position, and liquidity.

In January 2016, the FASB issued guidance ASU 2016-01, "Recognition and Measurement of Financial Assets and Financial Liabilities." The amendments in ASU 2016-01 to Subtopic 825-10, Financial Instruments, contain the following elements: (1) requires equity investments to be measured at fair value with changes in fair value recognized in net income; (2) simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment; (3) eliminates the requirement for public entities to disclose the methods and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet; (4) requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes; (5) requires an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments; (6) requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset on the balance sheet or accompanying notes to the financial statements; (7) clarifies that the entity should evaluate the need for a valuation allowance on a deferred tax asset related to available for sale securities in combination with the entity's other deferred tax assets. The amendments are effective for fiscal years beginning after December 15, 2017, and for interim periods within those fiscal years. Except for the early application of the amendment noted in item (5) above, early adoption of the amendments in this update is not permitted. Heartland intends to adopt the accounting standard in 2018, as required, and is currently evaluating the impact on its results of operations, financial position, and liquidity.

In February 2016, the FASB issued ASU 2016-02, "Leases (Topic 842)." Topic 842 requires a lessee to recognize a lease liability and a right of use asset for each lease, with the exception of short term leases, at the commencement date of the lease and disclose key information about the leasing arrangement. Accounting requirements applied by lessors is largely unchanged. The amendment is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years, and will be applied on a modified retrospective basis. Heartland intends to adopt the accounting standard in 2019, as required, and is currently evaluating the impact on its results of operations, financial position, and liquidity.

In March 2016, the FASB issued ASU 2016-09, "Compensation-Stock Compensation (Topic 718)." The amendments in this ASU simplify several aspects of the accounting for share-based payments, including income tax consequences, classification of awards as either equity or liabilities and classification on the statement of cash flows. The amendments in this ASU are effective for annual periods beginning after December 15, 2016 and interim periods within those annual periods. Early adoption is permitted for any interim or annual period prior to the effective date. An entity that elects early adoption must adopt all of the amendments in the same period. Heartland intends to adopt this ASU in 2017, as required, and believes the adoption will not have an impact on its results of operations, financial position, and liquidity.

NOTE 2: ACQUISITIONS

CIC Bancshares, Inc.
On February 5, 2016, Heartland completed the acquisition of CIC Bancshares, Inc., parent company of Centennial Bank, headquartered in Denver, Colorado. The purchase price was approximately $76.9 million, which was paid by delivery of 2,003,235 shares of Heartland common stock and cash of $15.7 million. In addition, Heartland issued a new series of convertible preferred stock with a fair value of $3.8 million and assumed convertible notes and subordinated debt totaling approximately $7.9 million. Simultaneous with the closing of the transaction, Centennial Bank merged into Heartland's Summit Bank & Trust, with the resulting institution operating under the name, Centennial Bank and Trust. As of the close date, the transaction included, at fair value, total assets of $772.6 million, total loans of $581.5 million, and total deposits of $648.1 million. The transaction was a tax-free reorganization with respect to the stock consideration received by the stockholders of CIC Bancshares, Inc.

The assets and liabilities of CIC Bancshares, Inc. were recorded on the consolidated balance sheet at estimated fair value on the acquisition date. The following table represents, in thousands, the amounts recorded on the consolidated balance sheet as of February 5, 2016:

	As of February 5, 2016
Fair value of consideration paid:	
Common Stock (2,003,235 shares)	$ 57,433
Preferred Stock (3,000 shares)	3,777
Cash	15,672
Total consideration paid	76,882
Fair value of assets acquired:	
Cash and due from banks	23,756
Securities:	
Securities available for sale	92,831
Other securities	3,486
Loans held to maturity	581,477
Premises, furniture and equipment, net	16,450
Other real estate, net	1,934
Other intangible assets, net	6,576
Other assets	16,276
Total assets	742,786
Fair value of liabilities assumed:	
Deposits	648,111
Short term borrowings	35,766
Other borrowings	7,924
Other liabilities	3,951
Total liabilities assumed	695,752
Fair value of net assets acquired	47,034
Goodwill resulting from acquisition	$ 29,848

Heartland recognized $29.8 million of goodwill in conjunction with the acquisition of CIC Bancshares, Inc., which is calculated as the excess of both the consideration exchanged and the liabilities assumed as compared to the fair value of identifiable assets acquired. Goodwill resulted from the expected operational synergies, enhanced market area, cross-selling opportunities and expanded business lines. See Note 6 for further information on goodwill.

Pro Forma Information (unaudited): The following pro forma information presents the results of operations for the years ended December 31, 2015, and December 31, 2014, as if the CIC Bancshares, Inc. acquisition occurred on January 1, 2014:

(Dollars in thousands, except per share data), unaudited	For the Years Ended	
	December 31, 2015	December 31, 2014
Net interest income	$259,531	$221,808
Net income available to common shareholders	$59,491	$41,004
Basic earnings per share	$2.63	$2.00
Diluted earnings per share	$2.58	$1.96

The above pro forma results are presented for illustrative purposes and are not intended to represent or be indicative of the actual results of operations of the merged companies that would have been achieved had the acquisition occurred at January 1, 2014, nor are they intended to represent or be indicative of future results of operations. The pro forma results do not include expected operating cost savings as a result of the acquisition. These pro forma results require significant estimates and judgments particularly with respect to valuation and accretion of income associated with the acquired loans.

Heartland incurred $551,000 of pre-tax merger related expenses in 2016 associated with the Centennial Bank acquisition. The merger expenses are reflected on the consolidated statements of income for the applicable period and are reported primarily in the categories of professional fees and other noninterest expenses.

Acquired loans were preliminarily recorded at fair value based on a discounted cash flow valuation methodology that considers, among other things, projected default rates, loss given defaults and recovery rates. No allowance for credit losses was carried over from the acquisition. The balance of nonaccrual loans on the acquisition date was $1.6 million.

Premier Valley Bank
On November 30, 2015, Heartland completed the purchase of Premier Valley Bank in Fresno, California. The purchase price was approximately $95.5 million, which was paid by delivery of 1,758,543 shares of Heartland common stock and cash of $28.5 million. The transaction included, at fair value, total assets of $692.7 million, loans of $389.8 million, and deposits of $622.7 million. Premier Valley Bank continues to operate under its current name and management team as Heartland's tenth, wholly-owned state-chartered bank. The transaction was a tax-free reorganization with respect to the stock consideration received by the stockholders of Premier Valley Bank.

Heartland recognized $41.0 million of goodwill in conjunction with the acquisition of Premier Valley Bank, which is calculated as the excess of both the consideration exchanged and the liabilities assumed as compared to the fair value of identifiable assets acquired. Goodwill resulted from the expected operational synergies, enhanced market area, cross-selling opportunities and expanded business lines. See Note 6 for further information on goodwill.

First Scottsdale Bank, N.A.
On September 11, 2015, Heartland completed the purchase of First Scottsdale Bank, N.A., in Scottsdale, Arizona, in an all cash transaction valued at approximately $17.7 million. Simultaneous with the closing of the transaction, First Scottsdale Bank, N.A., merged into Heartland's Arizona Bank & Trust subsidiary. The transaction included, at fair value, total assets of $81.2 million, loans of $54.7 million, and deposits of $65.9 million on the acquisition date.

Community Bancorporation of New Mexico, Inc.
On August 21, 2015, Heartland acquired Community Bancorporation of New Mexico, Inc., parent company of Community Bank in Santa Fe, New Mexico, in an all cash transaction valued at approximately $11.1 million. Simultaneous with the closing of the transaction, Community Bank merged into Heartland's New Mexico Bank & Trust subsidiary. The transaction included, at fair value, total assets of $166.3 million, loans of $99.5 million, and deposits of $147.4 million on the acquisition date. Also included in this transaction is one bank building with a fair value of $3.4 million that Heartland intends to sell. The bank building is part of the balance of premises, furniture and equipment held for sale on the consolidated balance sheet.

Community Banc-Corp of Sheboygan, Inc.
On January 16, 2015, Heartland completed the acquisition of Community Banc-Corp of Sheboygan, Inc., parent company of Community Bank & Trust in Sheboygan, Wisconsin. Under the terms of the merger agreement for this transaction, the aggregate purchase price was based upon 155% of the December 31, 2014, adjusted tangible book value, as defined in the merger agreement, of Community Banc-Corp of Sheboygan, Inc. The purchase price was approximately $53.1 million, which was paid by delivery of 1,970,720 shares of Heartland common stock. The transaction included, at fair value, total assets of $506.8 million, including loans of $395.0 million, and deposits of $433.9 million. Simultaneous with the close of the transaction, Community Bank & Trust merged into Heartland’s Wisconsin Bank & Trust subsidiary. The transaction was a tax-free reorganization with respect to the stock consideration received by the stockholders of Community Banc-Corp of Sheboygan, Inc.

Heartland recognized goodwill of $18.6 million in conjunction with the acquisition of Community Banc-Corp of Sheboygan, Inc., which is calculated as the excess of both the consideration exchanged and the liabilities assumed as compared to the fair value of identifiable assets acquired. See Note 6 for further information on goodwill.