QCR HOLDINGS INC
Form 10-K
March 15, 2019
Table of Contents

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, 2018.

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) 736 3580

(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 every Interactive Data File required to be submitted 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, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b 2 of the Exchange Act.

Large accelerated filer [ ]	Accelerated filer [X]	Non-accelerated filer [ ]	Smaller reporting company [ ]	Emerging growth company [ ]

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. [ ]

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, 2018, the last business day of the registrant's most recently completed second fiscal quarter, was approximately $624,586,534.

As of February 28, 2019 the Registrant had outstanding 15,738,761 shares of common stock, $1.00 par value per share.

Documents incorporated by reference:

Part III of Form 10 K incorporates by reference portions of the proxy statement for annual meeting of stockholders to be held in May 2019.

Table of Contents

QCR HOLDINGS, INC. AND SUBSIDIARIES

INDEX

			Page Number(s)
Part I			
	Item 1.	Business	4
	Item 1A.	Risk Factors	12
	Item 1B.	Unresolved Staff Comments	23
	Item 2.	Properties	24
	Item 3.	Legal Proceedings	25
	Item 4.	Mine Safety Disclosures	25
Part II			
	Item 5.	Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	26
	Item 6.	Selected Financial Data	28
	Item 7.	Management's Discussion and Analysis of Financial Condition and Results of Operations	29
		General	29
		Executive Overview	29
		Long-Term Financial Goals	30
		Strategic Developments	31
		GAAP to Non-GAAP Reconciliations	32
		Net Interest Income and Margin (Tax Equivalent Basis)(Non-GAAP)	34
		Critical Accounting Policies	36
		Results of Operations	38
		Interest Income	38
		Interest Expense	38
		Provision for Loan/Lease Losses	38
		Noninterest Income	39
		Noninterest Expenses	41
		Income Tax Expense	43
		Financial Condition	43
		Overview	43
		Investment Securities	43
		Loans/Leases	44
		Allowance for Estimated Losses on Loans/Leases	46
		Nonperforming Assets	48
		Deposits	49
		Short-Term Borrowings	49
		FHLB Advances and Other Borrowings	49
		Stockholders' Equity	50
		Liquidity and Capital Resources	51
		Commitments, Contingencies, Contractual Obligations, and Off-Balance Sheet Arrangements	53
		Impact of Inflation and Changing Prices	54

	Forward-Looking Statements	54
Item 7A.	Quantitative and Qualitative Disclosures About Market Risk	55
Item 8.	Consolidated Financial Statements	57
	Consolidated Balance Sheets as of December 31, 2018 and 2017	59
	Consolidated Statements of Income for the years ended December 31, 2018, 2017 and 2016	60
	Consolidated Statements of Comprehensive Income for the years ended December 31, 2018, 2017 and 2016	61

Table of Contents

	Consolidated Statements of Changes in Stockholders' Equity for the years ended December 31, 2018, 2017 and 2016	62
	Consolidated Statements of Cash Flows for the years ended December 31, 2018, 2017 and 2016	63
	Notes to Consolidated Financial Statements	65
	Note 1 Nature of Business and Significant Accounting Policies	65
	Note 2 Mergers/Acquisitions	79
	Note 3 Investment Securities	90
	Note 4 Loans/Leases Receivable	94
	Note 5 Premises and Equipment	105
	Note 6 Goodwill and Intangibles	106
	Note 7 Derivatives and Hedging Activities	108
	Note 8 Deposits	109
	Note 9 Short-Term Borrowings	110
	Note 10 FHLB Advances	111
	Note 11 Other Borrowings and Unused Lines of Credit	112
	Note 12 Junior Subordinated Debentures	114
	Note 13 Federal and State Income Taxes	115
	Note 14 Employee Benefit Plans	117
	Note 15 Stock-Based Compensation	118
	Note 16 Regulatory Capital Requirements and Restrictions on Dividends	120
	Note 17 Earnings Per Share	122
	Note 18 Commitments and Contingencies	123
	Note 19 Quarterly Results of Operations (Unaudited)	124
	Note 20 Parent Company Only Financial Statements	125
	Note 21 Fair Value	128
	Note 22 Business Segment Information	131
	Note 23 Subsequent Event Subordinated Notes	132
Item 9.	Changes in and Disagreements With Accountants on Accounting and Financial Disclosure	133
Item 9A.	Controls and Procedures	133
Item 9B.	Other Information	136
Part III		
Item 10.	Directors, Executive Officers and Corporate Governance	137
Item 11.	Executive Compensation	137
Item 12.	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	137
Item 13.	Certain Relationships and Related Transactions, and Director Independence	137
Item 14.	Principal Accountant Fees and Services	138
Part IV		
Item 15.	Exhibits and Financial Statement Schedules	139
Item 16.	Form 10 K Summary	143
	Signatures	144
	Appendix A. Supervision and Regulation	146
	Appendix B. Guide 3 Information	157

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.

Table of Contents

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. In 2016, the Company elected to operate as a financial holding company under the BHCA. The Company serves the Quad Cities, Cedar Rapids, Waterloo/Cedar Falls, Des Moines/Ankeny, Rockford and Springfield communities through the following five 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;
- CSB, which is based in Ankeny, Iowa, and was acquired in 2016;
- SFC Bank, which is based in Springfield, Missouri, and was acquired in 2018; and
- RB&T, which is based in Rockford, Illinois, and commenced operations in 2005.

On October 1, 2018, the Company acquired the Bates Companies, headquartered in Rockford, Illinois. The acquisition of the Bates Companies enhances the wealth management services of the Company by adding approximately $704 million of assets under management as of October 1, 2018.

On July 1, 2018, the Company merged with Springfield Bancshares, the holding company of SFC Bank, headquartered in Springfield, Missouri.

On October 1, 2017, the Company acquired Guaranty Bank, headquartered in Cedar Rapids, Iowa. On December 2, 2017, the Company merged Guaranty Bank with and into CRBT with CRBT as the surviving bank.

On August 31, 2016, the Company acquired CSB, located in Ankeny, Iowa (Des Moines MSA).

See Note 2 to the Consolidated Financial Statements for further discussion on mergers and acquisitions.

The Company engages in direct financing lease contracts through m2, a wholly-owned subsidiary of QCBT based in Brookfield, Wisconsin.

Subsidiary Banks. Segments of the Company have been established by management as defined by the structure of the Company's internal organization, focusing on the financial information that the Company's operating decision-makers routinely use to make decisions about operating matters. The Company's primary segment, Commercial Banking, is geographically divided by markets into secondary segments which correspond to the five subsidiary banks wholly-owned by the Company: QCBT, CRBT, CSB, SFC Bank and RB&T. See the Consolidated Financial Statements incorporated herein generally, and Note 22 to the Consolidated Financial Statements specifically, for additional business segment information.

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. 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 $1.62 billion and $1.54 billion as of December 31, 2018 and 2017, respectively.

CRBT is an Iowa-chartered commercial bank that is a member of the Federal Reserve System. The Company commenced operations in Cedar Rapids in June 2001, operating as a branch of QCBT. The Cedar Rapids branch operation then began functioning under the CRBT charter in September 2001. Acquired 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 eight facilities. The headquarters for CRBT is located in downtown Cedar Rapids with three other branches located in Cedar Rapids, one branch in Marion, two branches located in Waterloo and one branch located in Cedar Falls. CRBT had total segment assets of $1.38 billion and $1.31 billion as of December 31, 2018 and 2017, respectively.

Table of Contents

CSB is an Iowa-chartered commercial bank that is a member of the Federal Reserve System. CSB was acquired by the Company in 2016. CSB provides full-service commercial and consumer banking to Des Moines and adjacent communities through its headquarters located in Ankeny and its nine other branch facilities throughout the greater Des Moines area. CSB had total segment assets of $785.4 million and $670.5 million as of December 31, 2018 and 2017, respectively.

SFC Bank is a Missouri-chartered commercial bank that is a member of the Federal Reserve System. SFC Bank was acquired by the the Company in 2018 through a merger with Springfield Bancshares. SFC Bank provides full-service commercial and consumer banking to the Springfield, Missouri area through its headquarters located on Glenstone Avenue in Springfield and its branch facility located on East Primrose in Springfield. SFC Bank had total segment assets of $632.8 million as of December 31, 2018.

RB&T is an Illinois-chartered commercial bank that is a member of the Federal Reserve System. The Company commenced operations in Rockford, Illinois in September 2004, operating as 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 $509.6 million and $461.7 million as of December 31, 2018 and 2017, respectively.

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. The Bates Companies, which are based in Rockford, Illinois, are engaged in the business of wealth management services.

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, 2018 and 2017:

Name	Date Issued	Amount Outstanding as of December 31, 2018	Amount Outstanding as of December 31, 2017	Interest Rate	Interest Rate as of December 31, 2018	Interest Rate as of December 31, 2017
QCR Holdings Statutory Trust II	February 2004	$ 10,310,000	$ 10,310,000	2.85% over 3-month LIBOR	5.65 %	4.54 %
QCR Holdings Statutory Trust III	February 2004	8,248,000	8,248,000	2.85% over 3-month LIBOR	5.65 %	4.54 %
QCR Holdings Statutory Trust V	February 2006	10,310,000	10,310,000	1.55% over 3-month LIBOR	3.99 %	2.91 %
Community National Statutory Trust II	September 2004	3,093,000	3,093,000	2.17% over 3-month LIBOR	4.96 %	3.80 %
Community National	March 2007	3,609,000	3,609,000	1.75% over 3-month	4.54 %	3.32 %

Statutory Trust III				LIBOR		
Guaranty Bankshares Statutory Trust I	May 2005	4,640,000	4,640,000	1.75% over 3-month LIBOR	4.54 %	3.34 %
		$ 40,210,000	$ 40,210,000	Weighted Average Rate	4.94 %	3.82 %

Securities issued by all of the trusts listed above mature 30 years from the date of issuance, but are all currently callable at par at any time. Interest rate reset dates vary by trust. The Company entered into interest rate swaps to hedge against rising rates on its variable rate trust preferred securities. See Note 7 to the Consolidated Financial Statements for additional information regarding these interest rate swaps.

Guaranty Bankshares Statutory Trust I was acquired in 2017 as part of the acquisition of Guaranty Bank and is further discussed in Note 12 to the Consolidated Financial Statements.

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.

Table of Contents

The Company and its subsidiaries collectively employed 755 and 641 FTEs at December 31, 2018 and 2017, respectively. The majority of the increase in FTEs during 2018 was the result of the additions of SFC Bank and the Bates Companies and new positions created to accommodate the increased scale of our operations.

The Federal Reserve is the primary federal regulator of the Company, QCBT, CRBT, CSB, SFC Bank and RB&T. QCBT, CRBT and CSB are also regulated by the Iowa Superintendent of Banking, SFC Bank is regulated by the Missouri Division of Finance and RB&T is regulated by the IDFPR. The FDIC, as administrator of the DIF, 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, CRBT and CSB, calculated as 15% of aggregate capital, was $24.3 million, $25.2 million, and $12.9 million, respectively, as of December 31, 2018. In accordance with Missouri regulation, the legal lending limit to one borrower for SFC Bank, calculated as 15% of aggregate capital, totaled $8.6 million as of December 31, 2018. In accordance with Illinois regulation, the legal lending limit to one borrower for RB&T, calculated as 25% of aggregate capital, totaled $12.6 million as of December 31, 2018.

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. As of January 1, 2017, the Company implemented a tiered approach, based on the risk rating of the borrower. Under the most recent 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:

	High Quality (Risk Ratings 1-3)	Medium Quality (Risk Rating 4)	Low Quality (Risk Ratings 5-8)
	(dollars in thousands)		
QCBT	$ 14,000	$ 11,750	$ 8,000
CRBT	$ 13,000	$ 11,000	$ 7,500
CSB	$ 9,500	$ 8,000	$ 5,500
SFC Bank	$ 9,000	$ 7,500	$ 5,000
RB&T	$ 4,500	$ 3,750	$ 2,500
QCRH Consolidated	$ 25,000	$ 19,000	$ 12,500

The QCRH Consolidated amount represents 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, subject to certain exceptions.

As part of the loan monitoring activity at the five 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

Table of Contents

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 subsidiary banks as of December 31, 2018 for the loan portfolio organized by loan type, reflected as a percentage of the subsidiary bank's gross loans:

As of December 31, 2018		CRBT Maximum Percentage per Loan Policy		As of December 31, 2018		CSB Maximum Percentage per Loan Policy		As of December 31, 2018		SFC Bank Maximum Percentage per Loan Policy		As of December 31, 2018		RB& Maxi Perce per L Polic
13	%	25	%	11	%	35	%	13	%	20	%	18	%	30
3	%	15	%	8	%	15	%	1	%	10	%	7	%	15
1	%	5	%	—	%	15	%	2	%	2	%	1	%	5
26	%	50	%	29	%	50	%	33	%	50	%	45	%	50
4	%	15	%	7	%	35	%	16	%	15	%	8	%	20
28	%	60	%	36	%	50	%	24	%	20	%	18	%	60
1	%	10	%	1	%	10	%	—	%	5	%	1	%	10
10	%	5	%	—	%	5	%	—	%	N/A	%	—	%	20
**		10	%	—	%	—	%	—	%	N/A	%	—	%	10
14	%	10	%	8	%	10	%	11	%	6	%	2	%	10
100	%			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 risk-based capital (bank stock loan commitments are limited to 200% of risk-based capital). At December 31, 2018, QCBT's bank stock loans totaled 32% of risk-based capital.

The following table presents total loans/leases by major loan/lease type and subsidiary as of December 31, 2018 and 2017. Residential real estate loans held for sale are included in residential real estate loans below.

	QCBT		m2 Lease Funds		CRBT		CSB		SFC
	$	%	$	%	$	%	$	%	$
(dollars in thousands)									

As of December 31, 2018														
C&I loans	$	425,500	42	%	$	103,404	45	%	$	458,170	44	%	$	201,871	35	%	$	9
CRE loans		421,032	42	%		—	—	%		486,084	47	%		327,775	56	%		3
Direct financing leases		—	—	%		117,968	52	%		—	—	%		—	—	%		-
Residential real estate loans		120,855	12	%		—	—	%		57,469	6	%		39,190	7	%		3
Installment and other consumer loans		35,325	4	%		—	—	%		36,563	3	%		13,696	2	%		1
Deferred loan/lease origination costs, net of fees		1,759	—	%		7,274	3	%		(815)	—	%		(81)	—	%		1
	$	1,004,471	100	%	$	228,646	100	%	$	1,037,471	100	%	$	582,451	100	%	$	4
As of December 31, 2017																		
C&I loans	$	384,401	42	%	$	66,758	31	%	$	402,146	41	%	$	148,198	30	%	$	N
CRE loans		384,684	42	%		—	—	%		455,443	47	%		291,254	60	%		N
Direct financing leases		—	—	%		141,290	66	%		—	—	%		158	—	%		N
Residential real estate loans		114,818	12	%		—	—	%		62,755	6	%		38,831	8	%		N
Installment and other consumer loans		36,360	4	%		—	—	%		54,448	6	%		10,814	2	%		N
Deferred loan/lease origination costs, net of fees		1,254	—	%		7,188	3	%		(821)	—	%		(180)	—	%		N
	$	921,517	100	%	$	215,236	100	%	$	973,971	100	%	$	489,075	100	%	$	N

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.

Table of Contents

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
Penny Stocks	0%
General Business	
Accounts Receivable	80% of eligible accounts
Inventory	50% of value
Crop and Grain Inventories	80% of current market value
Livestock	

	80% of purchase price, or current market value; or higher if cross-collateralized with other assets
Fixed Assets (Existing)	50% of net book value, or 75% of orderly liquidation appraised value
Fixed Assets (New)	80% of cost, or higher if cross-collateralized with other assets
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. For low income housing tax credits permanent loans, the maximum term is generally up to 20 years.

Table of Contents

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

Following is a summary of the five largest industry concentrations within the C&I portfolio as of December 31, 2018 and 2017:

	2018 Amount	2017 Amount
	(dollars in thousands)	
Administration of urban planning & rural development	$ 111,579	$ 83,344
Hotels & motels	83,106	73,200
Bank holding companies	75,601	66,950
Skilled nursing care facilities	53,134	60,989
General medical & surgical hospitals	36,895	35,217

These loan categories are defined by industry-standard NAICS codes – refer to NAICS.com for category descriptions.

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 85% of project cost, or 75% of "as-completed" appraised value	24 months
Commercial Construction Loans	Lesser of 85% of project cost, or 80% of "as-completed" appraised value	12 months
Residential Construction Loans to Builders	Lesser of 90% of project cost, or 80% of "as-completed" appraised value	12 months

* 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.

*** Generally, the maximum term for land development loans is 12 months but there are some situations where the maximum term would be 24 months.

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, 2018 and 2017, approximately 28% and 26%, respectively, of the CRE loan portfolio was owner-occupied.

In accordance with regulatory guidelines, the Company exercises heightened risk management practices when non-owner occupied CRE lending exceeds 300% of total risk-based capital or construction, land development and other land loans exceed 100% of total risk-based capital. Although CSB's loan portfolio has historically been real estate dominated and its real estate portfolio levels exceed these policy limits, it has established a Credit Risk Committee to routinely monitor its real estate loan portfolio.

Table of Contents

Following is a listing of the significant industries within the Company's CRE loan portfolio as of December 31, 2018 and 2017:

	2018 Amount (dollars in thousands)	%	2017 Amount	%
Lessors of Nonresidential Buildings	$ 612,327	34 %	$ 388,648	30 %
Lessors of Residential Buildings	346,270	19 %	199,047	15 %
Hotels	81,345	5 %	70,447	5 %
Nonresidential Property Managers	69,885	4 %	51,621	4 %
Land Subdivision	48,378	3 %	44,192	3 %
New Housing For-Sale Builders	47,598	3 %	61,480	5 %
Other *	560,308	32 %	488,057	38 %
Total CRE Loans	$ 1,766,111	100 %	$ 1,303,492	100 %

* "Other" consists of all other industries. None of these had concentrations greater than $42.6 million, or 2.4%, of total CRE loans as of December 31, 2018.

Following is a breakdown of non owner-occupied CRE by property type as of December 31, 2018 and 2017:

	2018 Amount (dollars in thousands)	%	2017 Amount	%
Office	$ 255,452	25 %	$ 169,655	22 %
Retail	232,022	23 %	143,685	18 %
Multi-family	189,137	18 %	133,174	17 %
Industrial/warehouse	93,503	9 %	76,186	10 %
Hotel/motel	89,906	9 %	37,401	5 %
Other	168,650	16 %	224,246	29 %
Total income-producing CRE	$ 1,028,670	100 %	$ 784,347	100 %

A portion of the Company's construction portfolio is considered non-residential construction. Following is a summary of industry concentrations within that category as of December 31, 2018 and 2017:

	2018 Amount (dollars in thousands)	%	2017 Amount	%
Multi-family	$ 61,055	30 %	$ 16,416	19 %
Office	17,692	9 %	12,033	14 %
Retail	10,285	5 %	11,580	13 %

Hotel/motel	5,679	3	%	3,604	4	%
Industrial/warehouse	4,591	2	%	8,407	10	%
Other	106,532	51	%	36,195	41	%
Total non-residential construction loans	$ 205,834	100	%	$ 88,235	100	%

Additionally, the Company had approximately $52.3 million and $81.3 million of residential construction loans outstanding as of December 31, 2018 and 2017, respectively. Of this amount, approximately 72% was considered speculative, while 28% was pre-sold at December 31, 2018 and approximately 79% was considered speculative, while 21% was pre-sold at December 31, 2017.

Table of Contents

Direct Financing Leasing

m2 leases machinery and equipment to C&I customers under direct financing leases. All lease requests are subject to the credit requirements and criteria as set forth in the lending/leasing policy. In all cases, a formal independent credit analysis of the lessee is performed.

The following private and public sector business assets are generally acceptable to consider for lease funding:

- Computer systems;
- Photocopy systems;
- Fire trucks;
- Specialized road maintenance equipment;
- Medical equipment;
- Commercial business furnishings;
- Vehicles classified as heavy equipment;
- Trucks and trailers;
- Equipment classified as plant or office equipment; and
- Marine boat lifts.

m2 will generally refrain from funding leases of the following type:

- Leases collateralized by non-marketable items;
- Leases collateralized by consumer items, such as vehicles, household goods, recreational vehicles, boats, etc.;
- Leases collateralized by used equipment, unless its remaining useful life can be readily determined; and
- Leases with a repayment schedule exceeding seven years.

Residential Real Estate Lending

Generally, the subsidiary banks' residential real estate loans conform to the underwriting requirements of Freddie Mac and Fannie Mae to allow the subsidiary banks to resell loans in the secondary market. The subsidiary banks structure most loans that will not conform to those underwriting requirements as adjustable rate mortgages that adjust in one to five years, and then retain these loans in their portfolios. Servicing rights are generally not retained on the loans sold in the secondary market. The Company's lending policy establishes minimum appraisal and other credit guidelines.

The following table presents the originations and sales of residential real estate loans for the Company. Included in originations is activity related to the refinancing of previously held in-house mortgages.

	For the year ended December 31,		
	2018	2017	2016
	(dollars in thousands)		
Originations of residential real estate loans	$ 87,133	$ 38,079	$ 52,721
Sales of residential real estate loans	$ 51,010	$ 33,165	$ 35,499
Percentage of sales to originations	59 %	87 %	67 %

Installment and Other Consumer Lending

The consumer lending department of each subsidiary bank provides many types of consumer loans, including home improvement, home equity, motor vehicle, signature loans and small personal credit lines. The Company's lending policy addresses specific credit guidelines by consumer loan type. In particular, for home equity loans and home equity lines of credit, the minimum credit bureau score is 650. For both home equity loans and lines of credit, the maximum advance rate is 90% of value with a minimum credit bureau score of 650. The maximum term on home equity loans is 10 years and maximum amortization is 15 years. The maximum term on home equity lines of credit is 10 years.

In some instances for all loans/leases, it may be appropriate to originate or purchase loans/leases that are exceptions to the guidelines and limits established within the Company's lending policy described above. In general, exceptions to the

Table of Contents

lending policy do not significantly deviate from the guidelines and limits established within the lending policy and, if there are exceptions, they are generally noted as such and specifically identified in loan/lease approval documents.

Competition. The Company currently operates in the highly competitive Quad Cities, Cedar Rapids, Waterloo/Cedar Falls, Des Moines, Springfield, and Rockford markets. Competitors include not only other commercial banks, credit unions, thrift institutions, and mutual funds, but also insurance companies, FinTech companies, finance companies, brokerage firms, investment banking companies, and a variety of other financial services and advisory companies. Many of these competitors are not subject to the same regulatory restrictions as the Company. Many of these unregulated competitors compete across geographic boundaries and provide customers increasing access to meaningful alternatives to banking services. The Company competes in markets with a number of much larger financial institutions with substantially greater resources and larger lending limits.

Appendices. The commercial banking business is a highly regulated business. See Appendix A for a summary of the federal and state statutes and regulations that are applicable to the Company and its subsidiaries. Supervision, regulation and examination of banks and bank holding companies by bank regulatory agencies are intended primarily for the protection of depositors rather than stockholders of bank holding companies and banks.

See Appendix B for tables and schedules that show selected financial statistical information relating to the business of the Company required to be presented pursuant to federal securities laws. Consistent with the information presented in the Form 10 K, results are presented as of and for the fiscal years ended December 31, 2018, 2017, and 2016, as applicable.

Internet Site, Securities Filings and Governance Documents. The Company maintains an Internet site at www.qcrh.com. The Company makes available free of charge through this site its annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and other reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 as soon as reasonably practicable after it electronically files such material with, or furnishes it to, the SEC. These filings are available at http://www.snl.com/IRW/Docs/1024092. Also available are many of its corporate governance documents, including the Code of Conduct (http://www.snl.com/IRW/govdocs/1024092).

Item 1A. Risk Factors

In addition to the other information in this Annual Report on Form 10 K, stockholders or prospective investors should carefully consider the following risk factors:

Conditions in the financial market and economic conditions, including conditions in the markets in which we operate, generally may adversely affect our business.

Our general financial performance is highly dependent upon the business environment in the markets where we operate 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 it offers. 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.

While economic conditions have improved since the recession, there can be no assurance that this improvement will continue. Uncertainty regarding continuing economic improvement may result in changes in consumer and business spending, borrowing, and savings habits. Downturns in the markets where our banking operations occur could result in a decrease in demand for our products and services, an increase in loan delinquencies and defaults, high or increased levels of problem assets and foreclosures and reduced wealth management fees resulting from lower asset values. Such conditions could adversely affect the credit quality of our loans, financial condition and results of operations.

Potential future acquisitions could be difficult to integrate, divert the attention of key personnel, disrupt our business, dilute stockholder value and adversely affect our financial results.

As part of our business strategy, we may consider acquisitions of other banks or financial institutions or branches, assets or deposits of such organizations. There is no assurance, however, that we will determine to pursue any of these

Table of Contents

opportunities or that if we determine to pursue them that we will be successful. Acquisitions involve numerous risks, any of which could harm our business, including:

- difficulties in integrating the operations, technologies, products, existing contracts, accounting processes and personnel of the target company and realizing the anticipated synergies of the combined businesses;

- difficulties in supporting and transitioning customers of the target company;

- diversion of financial and management resources from existing operations;

- the price we pay or other resources that we devote may exceed the value we realize, or the value we could have realized if we had allocated the purchase price or other resources to another opportunity;

- risks of entering new markets or areas in which we have limited or no experience or are outside our core competencies;

- potential loss of key employees, customers and strategic alliances from either our current business or the business of the target company;

- risks of acquiring loans with deteriorated credit quality;

- assumption of unanticipated problems or latent liabilities; and

- inability to generate sufficient revenue to offset acquisition costs.

Future acquisitions may involve the issuance of our equity securities as payment or in connection with financing the business or assets acquired, and as a result, could dilute the ownership interests of existing stockholders. In addition, consummating these transactions could result in the incurrence of additional debt and related interest expense, as well as unforeseen liabilities, all of which could have a material adverse effect on our business, results of operations and financial condition. The failure to successfully evaluate and execute acquisitions or otherwise adequately address the risks associated with acquisitions could have a material adverse effect on our business, results of operations and financial condition.

We must effectively manage our credit risk.

There are risks inherent in making any loan, including risks inherent in dealing with specific borrowers, risks of nonpayment, risks resulting from uncertainties as to the future value of collateral and risks resulting from changes in economic and industry conditions. We attempt to minimize our credit risk through prudent loan application approval procedures, careful monitoring of the concentration of our loans within specific industries and periodic independent reviews of outstanding loans by our credit review department and an external third party. However, we cannot assure you that such approval and monitoring procedures will reduce these credit risks.

The majority of our subsidiary banks' loan portfolios are invested in C&I and CRE loans, and we focus on lending to small to medium-sized businesses. The size of the loans we can offer to commercial customers is less than the size of the loans that our competitors with larger lending limits can offer. This may limit our ability to establish relationships with the area's largest businesses. Smaller companies tend to be at a competitive disadvantage and generally have limited operating histories, less sophisticated internal record keeping and financial planning capabilities and fewer financial resources than larger companies. As a result, we may assume greater lending risks than financial institutions that have a lesser concentration of such loans and tend to make loans to larger, more established businesses. Collateral for these loans generally includes accounts receivable, inventory, equipment and real estate. However, depending on the overall financial condition of the borrower, some loans are made on an unsecured basis. In addition to C&I and CRE loans, our subsidiary banks are also active in residential mortgage and consumer lending. Our borrowers may experience financial difficulties, and the level of nonperforming loans, charge-offs and delinquencies could rise, which could negatively impact our business through increased provision, reduced interest income on loans/leases, and increased expenses incurred to carry and resolve problem loans/leases.

Table of Contents

C&I loans make up a large portion of our loan/lease portfolio.

C&I loans were $1.4 billion, or approximately 38% of our total loan/lease portfolio, as of December 31, 2018. Our C&I loans are primarily made based on the identified cash flow of the borrower and secondarily on the underlying collateral provided by the borrower. Most often, this collateral is accounts receivable, inventory, equipment and real estate. Credit support provided by the borrower for most of these loans and the probability of repayment is based on the liquidation value of the pledged collateral and enforcement of a personal guarantee, if any exists. Whenever possible, we require a personal guarantee or cosigner on commercial loans. In the case of loans secured by accounts receivable, the availability of funds for the repayment of these loans may be substantially dependent on the ability of the borrower to collect amounts due from its customers. The collateral securing these loans may lose value over time, may be difficult to appraise, and may fluctuate in value based on the success of the business. In addition, a prolonged recovery period could harm or continue to harm the businesses of our C&I customers and reduce the value of the collateral securing these loans.

Our loan/lease portfolio has a significant concentration of CRE loans, which involve risks specific to real estate values.

CRE lending comprises a significant portion of our lending business. Specifically, CRE loans were $1.8 billion, or approximately 48% of our total loan/lease portfolio, as of December 31, 2018. Of this amount, $500.7 million, or approximately 28%, was owner-occupied. The market value of real estate securing our CRE loans can fluctuate significantly in a short period of time as a result of market conditions in the geographic area in which the real estate is located. Adverse developments affecting real estate values in one or more of our markets could increase the credit risk associated with our loan portfolio. Additionally, real estate lending typically involves higher loan principal amounts and the repayment of the loans generally is dependent, in large part, on sufficient income from the properties securing the loans to cover operating expenses and debt service. Economic events or governmental regulations outside of the control of the borrower or lender could negatively impact the future cash flow and market values of the affected properties.

The problems that have occurred in the residential real estate and mortgage markets throughout much of the U.S. in prior years also affected the commercial real estate market. In our market areas, we generally experienced a downturn in credit performance by our CRE loan customers in prior years relative to historical norms, and despite recent improvements in certain aspects of the economy, a level of uncertainty continues to exist in the economy and credit markets. There can be no guarantee that we will not experience further deterioration in the performance of CRE and other real estate loans in the future. In such case, we may not be able to realize the amount of security that we anticipated at the time of originating the loan, which could cause us to increase our provision for loan losses and adversely affect our operating results, financial condition and/or capital.

Our allowance may prove to be insufficient to absorb losses in our loan/lease portfolio.

We establish our allowance for loan and lease losses in consultation with management of our subsidiaries and maintain it at a level considered adequate by management to absorb loan/lease losses that are inherent in the portfolio. The amount of future loan/lease losses is susceptible to changes in economic, operating and other conditions, including changes in interest rates, which may be beyond our control, and such losses may exceed current estimates. At December 31, 2018, our allowance as a percentage of total gross loans/leases was 1.07%, and as a percentage of total NPLs was 214.80%. In accordance with GAAP for acquisition accounting, the loans acquired through the acquisitions of SFC Bank, Guaranty Bank and CSB were recorded at fair value; therefore, there was no allowance associated with SFC Bank’s, Guaranty Bank’s and CSB’s loans at acquisition. Management continues to evaluate the allowance needed on the acquired loans factoring in the net remaining discount ($11.6 million at December 31, 2018).

In addition, we had net charge-offs as a percentage of gross average loans/leases of 0.21% for the year ended December 31, 2018. Because of the concentration of C&I and CRE loans in our loan portfolio, which tend to be larger in amount than residential real estate and installment loans, the movement of a small number of loans to nonperforming status can have a significant impact on these ratios. Although management believes that the allowance as of December 31, 2018 was adequate to absorb losses on any existing loans/leases that may become uncollectible, we cannot predict loan/lease losses with certainty, and we cannot assure you that our allowance will prove sufficient to cover actual loan/lease losses in the future, particularly if economic conditions are more difficult than what management currently expects. Additional provisions and loan/lease losses in excess of our allowance may adversely affect our business, financial condition and results of operations.

Table of Contents

The Company's information systems may experience an interruption or breach in security and cyber-attacks, all of which could have a material adverse effect on the Company's business.

The Company relies heavily on internal and outsourced technologies, communications, and information systems to conduct its business. Additionally, in the normal course of business, the Company collects, processes and retains sensitive and confidential information regarding our customers. As the Company's reliance on technology has increased, so have the potential risks of a technology-related operation interruption (such as disruptions in the Company's customer relationship management, general ledger, deposit, loan, or other systems) or the occurrence of a cyber-attacks (such as unauthorized access to the Company's systems). These risks have increased for all financial institutions as new technologies, the use of the Internet and telecommunications technologies (including mobile devices) to conduct financial and other business transactions and the increased sophistication and activities of organized crime, perpetrators of fraud, hackers, terrorists and others have also increased. In addition to cyber-attacks or other security breaches involving the theft of sensitive and confidential information, hackers have engaged in attacks against financial institutions, retailers and government agencies, particularly denial of service attacks that are designed to disrupt key business or government services, such as customer-facing web sites. The Company is not able to anticipate or implement effective preventive measures against all security breaches of these types, especially because the techniques used change frequently and because attacks can originate from a wide variety of sources. It is also possible that a cyber incident, such as a security breach, may remain undetected for a period of time, further exposing the Company to technology-related risks. However, applying guidance from the Federal Financial Institutions Examination Council, the Company has analyzed and will continue to analyze security related to device specific considerations, user access topics, transaction-processing and network integrity.

The Company also faces risks related to cyber-attacks and other security breaches in connection with credit card and debit card transactions that typically involve the transmission of sensitive information regarding the Company's customers through various third parties, including merchant acquiring banks, payment processors, payment card networks and its processors. Some of these parties have in the past been the target of security breaches and cyber-attacks, and because the transactions involve third parties and environments such as the point of sale that the Company does not control or secure, future security breaches or cyber-attacks affecting any of these third parties could impact the Company through no fault of its own, and in some cases it may have exposure and suffer losses for breaches or attacks relating to them. Despite third-party security risks that are beyond our control, the Company offers its customers protection against fraud and attendant losses for unauthorized use of debit cards in order to stay competitive in the marketplace. Offering such protection (including the cost of replacing compromised cards) to our customers exposes the Company to potential losses which, in the event of a data breach at one or more retailers of considerable magnitude, may adversely affect its business, financial condition, and results of operations. Further cyber-attacks or other breaches in the future, whether affecting the Company or others, could intensify consumer concern and regulatory focus and result in increased costs, all of which could have a material adverse effect on the Company's business. To the extent we are involved in any future cyber-attacks or other breaches, the Company's reputation could be affected, which could also have a material adverse effect on the Company's business, financial condition or results of operations.

System failure or breaches of our network security could subject us to increased operating costs as well as litigation and other liabilities.

The computer systems and network infrastructure we use could be vulnerable to unforeseen problems. Our operations are dependent upon our ability to protect our computer equipment against damage from physical theft, fire, power loss, telecommunications failure or a similar catastrophic event, as well as from security breaches, denial of service attacks, viruses, worms and other disruptive problems caused by hackers. Any damage or failure that causes an interruption in our operations could have a material adverse effect on our financial condition and results of operations. Computer break-ins, phishing and other disruptions could also jeopardize the security of information stored in and

transmitted through our computer systems and network infrastructure, as well as that of our customers engaging in internet banking activities, which may result in significant liability to us and may cause existing and potential customers to refrain from doing business with us. Although we, with the help of third-party service providers, intend to continue to implement security technology and establish operational procedures to prevent such damage, there can be no assurance that these security measures will be successful. In addition, advances in computer capabilities, new discoveries in the field of cryptography or other developments could result in a compromise or breach of the algorithms we and our third-party service providers use to encrypt and protect customer transaction data. Any interruption in, or breach of security of, our computer systems and network infrastructure, or that of our internet banking customers, could damage our reputation, result in a loss of customer business, subject us to additional regulatory scrutiny, or expose us to civil litigation and possible financial liability, any of which could have a material adverse effect on our financial condition and results of operations. The Company may also

Table of Contents

need to spend additional resources to enhance protective and detective measures or to conduct investigations to remediate any vulnerabilities that arise.

We are subject to certain operational risks, including, but not limited to, customer or employee fraud and data processing system failures and errors.

Employee errors and employee and customer misconduct could subject us to financial losses or regulatory sanctions and seriously harm our reputation. Misconduct by our employees could include hiding unauthorized activities from us, improper or unauthorized activities on behalf of our customers or improper use of confidential information. It is not always possible to prevent employee errors and misconduct, and the precautions we take to prevent and detect this activity may not be effective in all cases. Employee errors could also subject us to financial claims for negligence.

We maintain a system of internal controls and insurance coverage to mitigate operational risks, including data processing system failures and errors and customer or employee fraud. Despite having business continuity plans and other safeguards, the Company could still be affected. Should our internal controls fail to prevent or detect an occurrence, and if any resulting loss is not insured or exceeds applicable insurance limits, such failure could have a material adverse effect on our business, financial condition and results of operations.

We may be materially and adversely affected by the highly regulated environment in which we operate.

The Company and its bank subsidiaries are subject to extensive federal and state regulation, supervision and examination. Banking regulations are primarily intended to protect depositors' funds, FDIC funds, customers and the banking system as a whole, rather than stockholders. These regulations affect our lending practices, capital structure, investment practices, dividend policy and growth, among other things.

As a bank holding company, we are subject to regulation and supervision primarily by the Federal Reserve. QCBT, CRBT and CSB, as Iowa-chartered state member banks, are subject to regulation and supervision primarily by both the Iowa Superintendent and the Federal Reserve. RB&T, as an Illinois-chartered state member bank, is subject to regulation and supervision primarily by both the IDFPR and the Federal Reserve. SFC Bank, as a Missouri-chartered commercial bank, is subject to regulation by both the Missouri Division of Finance and the Federal Reserve. We and our banks undergo periodic examinations by these regulators, who have extensive discretion and authority to prevent or remedy unsafe or unsound practices or violations of law by banks and bank holding companies.

The primary federal and state banking laws and regulations that affect us are described in Appendix A to this report. These laws, regulations, rules, standards, policies and interpretations are constantly evolving and may change significantly over time. For example, the Dodd-Frank Act significantly changed the regulation of financial institutions and the financial services industry. In addition, in recent years the Federal Reserve has adopted numerous new regulations addressing banks' overdraft and mortgage lending practices. Further, the Basel III regulatory capital reforms increased both the amount and quality of capital that financial institutions must hold.

U.S. financial institutions are also subject to numerous monitoring, recordkeeping, and reporting requirements designed to detect and prevent illegal activities such as money laundering and terrorist financing. These requirements are imposed primarily through the Bank Secrecy Act which was most recently amended by the Patriot Act. We have instituted policies and procedures to protect us and our employees, to the extent reasonably possible, from being used to facilitate money laundering, terrorist financing and other financial crimes. There can be no guarantee, however, that these policies and procedures are effective.

Failure to comply with applicable laws, regulations or policies could result in sanctions by regulatory agencies, civil monetary penalties, and/or damage to our reputation, which could have a material adverse effect on us. Although we

have policies and procedures designed to mitigate the risk of any such violations, there can be no assurance that such violations will not occur.

Future legislation, regulation, and government policy could affect the banking industry as a whole, including our business and results of operations, in ways that are difficult to predict. In addition, our results of operations also could be adversely affected by changes in the way in which existing statutes and regulations are interpreted or applied by courts and government agencies.

Table of Contents

Monetary policies and regulations of the Federal Reserve could adversely affect our business, financial condition and results of operations.

In addition to being affected by general economic conditions, our earnings and growth are affected by the policies of the Federal Reserve. An important function of the Federal Reserve is to regulate the money supply and credit conditions. Among the instruments used by the Federal Reserve to implement these objectives are open market operations in U.S. government securities, adjustments of the discount rate and changes in reserve requirements against bank deposits. These instruments are used in varying combinations to influence overall economic growth and the distribution of credit, bank loans, investments and deposits. Their use also affects interest rates charged on loans or paid on deposits.

The monetary policies and regulations of the Federal Reserve have had a significant effect on the operating results of commercial banks in the past and are expected to continue to do so in the future. The effects of such policies upon our business, financial condition and results of operations cannot be predicted.

Interest rates and other conditions impact our results of operations.

Our profitability is in large part a function of the spread between the interest rates earned on investments and loans/leases and the interest rates paid on deposits and other interest bearing liabilities. Like most banking institutions, our net interest spread and margin will be affected by general economic conditions and other factors, including fiscal and monetary policies of the federal government that influence market interest rates and our ability to respond to changes in such rates. At any given time, our assets and liabilities will be such that they are affected differently by a given change in interest rates. As a result, an increase or decrease in rates, the length of loan/lease terms, the mix of adjustable and fixed rate loans/leases in our portfolio, the length of time deposits and borrowings, and the rate sensitivity of our deposit customers could have a positive or negative effect on our net income, capital and liquidity. We measure interest rate risk under various rate scenarios using specific criteria and assumptions. A summary of this process, along with the results of our net interest income simulations is presented at “Quantitative and Qualitative Disclosures about Market Risk” included under Item 7A of Part II of this Form 10 K. Although we believe our current level of interest rate sensitivity is reasonable and effectively managed, significant fluctuations in interest rates may have an adverse effect on our business, financial condition and results of operations.

We are required to maintain capital to meet regulatory requirements, and if we fail to maintain sufficient capital, whether due to losses, an inability to raise additional capital or otherwise, our financial condition, liquidity and results of operations, as well as our ability to maintain regulatory compliance, would be adversely affected.

The Company and each of its banking subsidiaries are required by federal and state regulatory authorities to maintain adequate levels of capital to support their operations, which have recently increased due to the effectiveness of the Basel III regulatory capital reforms. We intend to grow our business organically and to explore opportunities to grow our business by taking advantage of attractive acquisition opportunities, and such growth plans may require us to raise additional capital to ensure that we have adequate levels of capital to support such growth on top of our current operations. Our ability to raise additional capital, when and if needed or desired, will depend on conditions in the capital markets, economic conditions and a number of other factors, including investor perceptions regarding the banking industry and market conditions, and governmental activities, many of which are outside our control, and on our financial condition and performance. Accordingly, we cannot assure you that we will be able to raise additional capital if needed or on terms acceptable to us. Our failure to meet these capital and other regulatory requirements could affect customer confidence, our ability to grow, our costs of funds and FDIC insurance costs, our ability to pay dividends on common and preferred stock and to make distributions on our trust preferred securities, our ability to make acquisitions, and our business, results of operations and financial condition.

Failure to pay interest on our debt may adversely impact our ability to pay common stock dividends.

As of December 31, 2018, we had $40.2 million of junior subordinated debentures held by six business trusts that we control. Interest expense on the debentures, which totaled $2.0 million for 2018, must be paid before we pay dividends on our capital stock, including our common stock. We have the right to defer interest payments on the debentures for up to 20 consecutive quarters. However, if we elect to defer interest payments, all deferred interest must be paid before we may pay dividends on our capital stock. Deferral of interest payments on the debentures could cause a subsequent decline in the market price of our common stock because we would not be able to pay dividends on our common stock.

Table of Contents

As a bank holding company, our sources of funds are limited.

We are a bank holding company, and our operations are primarily conducted by our subsidiary banks, which are subject to significant federal and state regulation. When available, cash to pay dividends to our stockholders is derived primarily from dividends received from our subsidiary banks. Our ability to receive dividends or loans from our subsidiary banks is restricted. Dividend payments by our subsidiaries to us in the future will require generation of future earnings by them and could require regulatory approval if any proposed dividends are in excess of prescribed guidelines. Further, as a structural matter, our right to participate in the assets of our subsidiary banks in the event of a liquidation or reorganization of any of the banks would be subject to the claims of the creditors of such bank, including depositors, which would take priority except to the extent we may be a creditor with a recognized claim. As of December 31, 2018, our subsidiary banks had deposits, borrowings and other liabilities in the aggregate of approximately $4.5 billion.

Declines in asset values may result in impairment charges and adversely affect the value of our investments, financial performance and capital.

The market value of investments in our securities portfolio has become increasingly volatile in recent years, and as of December 31, 2018, we had gross unrealized losses of $12.9 million, or 1.9% of amortized cost, in our investment portfolio (partially offset by gross unrealized gains of $6.2 million). The market value of investments may be affected by factors other than the underlying performance of the servicer of the securities or the mortgages underlying the securities, such as ratings downgrades, adverse changes in the business climate and a lack of liquidity in the secondary market for certain investment securities. On a quarterly basis, we formally evaluate investments and other assets for impairment indicators. We may be required to record additional impairment charges if our investments suffer a decline in value that is considered other-than-temporary. If we determine that a significant impairment has occurred, we would be required to charge against earnings the credit-related portion of the OTTI, which could have a material adverse effect on our results of operations in the periods in which the write-offs occur. Based on management’s evaluation, it was determined that the gross unrealized losses at December 31, 2018 were temporary and primarily a function of the changes in certain market interest rates.

Liquidity risks could affect operations and jeopardize our business, results of operations and financial condition.

Liquidity is essential to our business. An inability to raise funds through deposits, borrowings, the sale of securities and/or loans and other sources could have a substantial negative effect on our liquidity. Our primary sources of funds consist of cash from operations, deposits, investment maturities, repayments, and calls, and loan/lease repayments. Additional liquidity is provided by federal funds purchased from the FRB or other correspondent banks, FHLB advances, wholesale and customer repurchase agreements, brokered deposits, and the ability to borrow at the FRB’s Discount Window. Our access to funding sources in amounts adequate to finance or capitalize our activities or on terms that are acceptable to us could be impaired by factors that affect us directly or the financial services industry or economy in general, such as disruptions in the financial markets or negative views and expectations about the prospects for the financial services industry.

During periods of economic turmoil, the financial services industry and the credit markets generally may be materially and adversely affected by significant declines in asset values and depressed levels of liquidity. Furthermore, regional and community banks generally have less access to the capital markets than do the national and super-regional banks because of their smaller size and limited analyst coverage. Any decline in available funding could adversely impact our ability to originate loans/leases, invest in securities, meet our expenses, pay dividends to our stockholders, or fulfill obligations such as repaying our borrowings or meeting deposit withdrawal demands, any of which could have a material adverse impact on our liquidity, business, results of operations and financial condition.

The success of our SBA lending program is dependent upon the continued availability of SBA loan programs, our status as a preferred lender under the SBA loan programs and our ability to comply with applicable SBA lending requirements.

As an SBA Preferred Lender, we enable our clients to obtain SBA loans without being subject to the potentially lengthy SBA approval process necessary for lenders that are not SBA Preferred Lenders. The SBA periodically reviews the lending operations of participating lenders to assess, among other things, whether the lender exhibits prudent risk management. When weaknesses are identified, the SBA may request corrective actions or impose other restrictions, including revocation of the lender's SBA Preferred Lender status. If we lose our status as an SBA Preferred Lender, we may lose our ability to compete effectively with other SBA Preferred Lenders, and as a result we would experience a material adverse effect to

Table of Contents

our financial results. Any changes to the SBA program, including changes to the level of guaranty provided by the federal government on SBA loans or changes to the level of funds appropriated by the federal government to the various SBA programs, may also have an adverse effect on our business, results of operations and financial condition.

Historically we have sold the guaranteed portion of our SBA 7(a) loans in the secondary market. These sales have resulted in our earning premium income and/or have created a stream of future servicing income. There can be no assurance that we will be able to continue originating these loans, that a secondary market will exist or that we will continue to realize premiums upon the sale of the guaranteed portion of these loans. When we sell the guaranteed portion of our SBA 7(a) loans, we incur credit risk on the retained, non-guaranteed portion of the loans.

In the event of a loss resulting from default and the SBA determines there is a deficiency in the manner in which the loan was originated, funded or serviced by the us, the SBA may require us to repurchase the loan, deny its liability under the guaranty, reduce the amount of the guaranty, or, if it has already paid under the guaranty, seek recovery of the principal loss related to the deficiency from us, any of which could adversely affect our business, results of operations and financial condition.

A prolonged U.S. government shutdown or default by the U.S. on government obligations would harm our results of operations.

Our results of operations, including revenue, non-interest income, expenses and net interest income, would be adversely affected in the event of widespread financial and business disruption on account of a default by the United States on U.S. government obligations or a prolonged failure to maintain significant U.S. government operations, including the recent partial shutdown of the U.S. government which ended on January 25, 2019. Of particular impact to the Company are the operations pertaining to the SBA or the FDIC. Any such failure to maintain such U.S. government operations, and the after-effects of such shutdown, could impede our ability to originate SBA loans and our ability to sell such loans in the secondary market, which would materially adversely affect our business, results of operations and financial condition.

In addition, many of our investment securities are issued by and some of our loans are made to the U.S. government and government agencies and sponsored entities. Uncertain domestic political conditions, including prior federal government shutdowns and potential future federal government shutdowns or other unresolved political issues, may pose credit default and liquidity risks with respect to investments in financial instruments issued or guaranteed by the federal government and loans to the federal government. Any downgrade in the sovereign credit rating of the United States, as well as sovereign debt issues facing the governments of other countries, could have a material adverse impact on financial markets and economic conditions in the United States and worldwide. Any such adverse impact could have a material adverse effect on our liquidity, financial condition and results of operations.

Changes in U.S. trade policies, such as the implementation of tariffs, and other factors beyond the Company’s control may adversely impact our business, financial condition and results of operations.

In 2018, the U.S. government implemented tariffs on certain products, and certain countries or entities, such as Mexico, Canada, China and the European Union, have issued or continue to threaten retaliatory tariffs against products from the United States, including agricultural products. Additional tariffs and retaliatory tariffs may be imposed in the future by the United States and these and other countries. Tariffs, retaliatory tariffs or other trade restrictions on products and materials that our customers import or export, including among others, agricultural products, could cause the prices of our customers' products to increase which could reduce demand for such products, or reduce our customer margins, and adversely impact their revenues, financial results and ability to service debt, which, in turn, could adversely affect our financial condition and results of operations. In addition, to the extent changes in the political environment have a negative impact on us or on the markets in which we operate, our business, results of operations and financial condition could be materially and adversely impacted in the future.

Our business is concentrated in and dependent upon the continued growth and welfare of the Quad Cities, Cedar Rapids, Waterloo/Cedar Falls, Des Moines/Ankeny, Springfield, and Rockford markets.

We operate primarily in the Quad Cities, Cedar Rapids, Waterloo/Cedar Falls, Des Moines/Ankeny, Iowa, Springfield, Missouri and Rockford, Illinois markets, and as a result, our financial condition, results of operations and cash flows are subject to changes in the economic conditions in those areas. We have developed a particularly strong presence in Bettendorf, Cedar Falls, Cedar Rapids, Davenport, Waterloo, and Ankeny, Iowa and Moline, Rock Island, Springfield, Missouri and Rockford, Illinois and their surrounding communities. Our success depends upon the business activity,

Table of Contents

population, income levels, deposits and real estate activity in these markets. Although our customers' business and financial interests may extend well beyond these market areas, adverse economic conditions that affect these market areas could reduce demand for our products and services, affect the ability of our customers to repay their loans to us, increase the levels of our nonperforming and problem loans, and generally affect our financial condition and results of operations. Because of our geographic concentration, we are less able than other regional or national financial institutions to diversify our credit risks across multiple markets.

We face intense competition in all phases of our business from other banks and financial institutions.

The banking and financial services businesses in our markets are highly competitive. Our competitors include large regional banks, local community banks, savings and loan associations, securities and brokerage companies, mortgage companies, insurance companies, finance companies, money market mutual funds, credit unions, online lenders and other non-bank financial services providers. Many of these competitors are not subject to the same regulatory restrictions as we are. Many of our unregulated competitors compete across geographic boundaries and are able to provide customers with a feasible alternative to traditional banking services.

Increased competition in our markets may result in a decrease in the amounts of our loans and deposits, reduced spreads between loan/lease rates and deposit rates or loan/lease terms that are more favorable to the borrower. Any of these results could have a material adverse effect on our ability to grow and remain profitable. If increased competition causes us to significantly discount the interest rates we offer on loans or increase the amount we pay on deposits, our net interest income could be adversely impacted. If increased competition causes us to modify our underwriting standards, we could be exposed to higher losses from lending and leasing activities. Additionally, many of our competitors are much larger in total assets and capitalization, have greater access to capital markets, have larger lending limits and offer a broader range of financial services than we can offer.

The stock market can be volatile, and fluctuations in our operating results and other factors, could cause our stock price to decline.

The stock market has experienced, and may continue to experience, fluctuations that significantly impact the market prices of securities issued by many companies. Most recently, like the stock of other financial institutions generally, the price of the Company's common stock as reported on the Nasdaq Global Market has increased substantially since the U.S. presidential election. Market fluctuations could also adversely affect our stock price. These fluctuations have often been unrelated or disproportionate to the operating performance of particular companies. These broad market fluctuations, as well as general economic, systemic, political and market conditions, such as recessions, loss of investor confidence, interest rate changes, or international currency fluctuations, may negatively affect the market price of our common stock. Moreover, our operating results may fluctuate and vary from period to period due to the risk factors set forth herein. As a result, period-to-period comparisons should not be relied upon as an indication of future performance. Our stock price could fluctuate significantly in response to our quarterly or annual results and the impact of these risk factors on our operating results or financial position.

The transition to an alternative reference rate could cause instability and have a negative effect on financial market conditions.

The LIBOR represents the interest rate at which banks offer to lend funds to one another in the international interbank market for short-term loans. Beginning in 2008, concerns were expressed that some of the member banks surveyed by the BBA in connection with the calculation of LIBOR rates may have been under-reporting or otherwise manipulating the interbank lending rates applicable to them. Regulators and law enforcement agencies from a number of

governments have conducted investigations relating to the calculation of LIBOR across a range of maturities and currencies. If manipulation of LIBOR or another inter-bank lending rate occurred, it may have resulted in that rate being artificially lower (or higher) than it otherwise would have been. Responsibility for the calculation of LIBOR was transferred to ICE Benchmark Administration Limited, as independent LIBOR administrator, effective February 1, 2014.

On July 27, 2017, the U.K. Financial Conduct Authority announced that it will no longer persuade or compel banks to submit rates for the calculation of LIBOR rates after 2021 (the “July 27th Announcement”). The July 27th Announcement indicates that the continuation of LIBOR on the current basis cannot and will not be guaranteed after 2021. Consequently, at this time, it is not possible to predict whether and to what extent banks will continue to provide LIBOR submissions to the administrator of LIBOR or whether any additional reforms to LIBOR may be enacted in the United Kingdom or elsewhere. Similarly, it is not possible to predict whether LIBOR will continue to be viewed as an acceptable benchmark,

Table of Contents

what rate or rates may become accepted alternatives to LIBOR or the effect of any such changes in views or alternatives on the value of LIBOR-linked securities.

Although the Financial Stability Oversight Council has recommended a transition to an alternative reference rate in the event LIBOR is no longer available after 2021, such plans are still in development and, if enacted, could present challenges. Moreover, contracts linked to LIBOR are vast in number and value, are intertwined with numerous financial products and services, and have diverse parties. The downstream effect of unwinding or transitioning such contracts could cause instability and negatively impact the financial markets and individual institutions. The uncertainty surrounding the sustainability of LIBOR more generally could undermine market integrity and threaten individual financial institutions and the U.S. financial system more broadly.

If securities or industry analysts do not publish or cease publishing research reports about us, if they adversely change their recommendations regarding our stock or if our operating results do not meet their expectations, the price of our stock could decline.

The trading market for our common stock can be influenced by the research and reports that industry or securities analysts may publish about us, our business, our market or our competitors. If there is limited or no securities or industry analyst coverage of us, the market price for our stock could be negatively impacted. Moreover, if any of the analysts who elect to cover us downgrade our common stock, provide more favorable relative recommendations about our competitors or if our operating results or prospects do not meet their expectations, the market price of our common stock may decline. If one or more of these analysts ceases coverage of us or fails to publish reports on us regularly, demand for our stock could decrease, which could cause our stock price and trading volume to decline.

The soundness of other financial institutions could negatively affect us.

Our ability to engage in routine funding and other transactions could be negatively affected by the actions and commercial soundness of other financial institutions. Financial services institutions are interrelated as a result of trading, clearing, counterparty or other relationships. Defaults by, or even rumors or questions about, one or more financial services institutions, or the financial services industry generally, have led to market-wide liquidity problems and losses of depositor, creditor and counterparty confidence and could lead to losses or defaults by us or by other institutions. We could experience increases in deposits and assets as a result of the difficulties or failures of other banks and government-sponsored financial institutions, which would increase the capital we need to support our growth.

Our community banking strategy relies heavily on our subsidiaries' independent management teams, and the unexpected loss of key managers may adversely affect our operations.

We rely heavily on the success of our bank subsidiaries' independent management teams. Accordingly, much of our success to date has been influenced strongly by our ability to attract and to retain senior management experienced in banking and financial services and familiar with the communities in our market areas. Our ability to retain the executive officers and current management teams of our operating subsidiaries will continue to be important to the successful implementation of our strategy. It is also critical, as we manage our existing portfolio and grow, to be able to attract and retain qualified additional management and loan officers with the appropriate level of experience and knowledge about our market areas to implement our community-based operating strategy. The unexpected loss of services of any key management personnel, or the inability to recruit and retain qualified personnel in the future, could

have an adverse effect on our business, financial condition and results of operations. Effective succession planning is also important to our long-term success. Failure to ensure effective transfer of knowledge and smooth transitions involving key employees could hinder our strategic planning and execution.

We have a continuing need for technological change, and we may not have the resources to effectively implement new technology.

The financial services industry continues to undergo rapid technological changes with frequent introductions of new technology-driven products and services. In addition to enabling us to better serve our customers, the effective use of technology increases efficiency and the potential for cost reduction. Our future success will depend in part upon our ability to address the needs of our customers by using technology to provide products and services that will satisfy customer demands for convenience as well as to create additional efficiencies in our operations as we continue to grow our market share. Many of our larger competitors have substantially greater resources to invest in technological improvements. As a

Table of Contents

result, they may be able to offer additional or superior products to those that we will be able to offer, which would put us at a competitive disadvantage. Accordingly, we cannot provide you with assurance that we will be able to effectively implement new technology-driven products and services or be successful in marketing such products and services to our customers.

Our reputation could be damaged by negative publicity.

Reputational risk, or the risk to our business, financial condition or results of operations from negative publicity, is inherent in our business. Negative publicity can result from actual or alleged conduct in a number of areas, including legal and regulatory compliance, lending practices, corporate governance, litigation, inadequate protection of customer data, ethical behavior of our employees, and from actions taken by regulators, ratings agencies and others as a result of that conduct. Damage to our reputation could impact our ability to attract new or maintain existing loan and deposit customers, employees and business relationships.

The preparation of our Consolidated Financial Statements requires us to make estimates and judgments, which are subject to an inherent degree of uncertainty and which may differ from actual results.

Our Consolidated Financial Statements are prepared in accordance with U.S. GAAP and general reporting practices within the financial services industry, which require us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses and related disclosure of contingent assets and liabilities. Some accounting policies, such as those pertaining to our allowance, require the application of significant judgment by management in selecting the appropriate assumptions for calculating financial estimates. By their nature, these estimates and judgments are subject to an inherent degree of uncertainty and actual results may differ from these estimates and judgments under different assumptions or conditions, which may have a material adverse effect on our financial condition or results of operations in subsequent periods.

From time to time, the FASB and the SEC change the financial accounting and reporting standards or the interpretation of those standards that govern the preparation of our external financial statements. These changes are beyond our control, can be difficult to predict and could materially impact how we report our financial condition and results of operations.

For example, the FASB has adopted a new accounting standard that will be effective for our first fiscal year after December 15, 2019. This standard, referred to as Current Expected Credit Loss, or CECL, will require financial institutions to determine periodic estimates of lifetime expected credit losses on loans, and recognize the expected credit losses as allowances. This will change the current method of providing allowances that are probable, which may require us to increase our allowance, and to greatly increase the types of data we will need to collect and review to determine the appropriate level of the allowance. Any increase in our allowance or expenses incurred to determine the appropriate level of the allowance may have a material adverse effect on our financial condition and results of operations.

Secondary mortgage, government guaranteed loan and interest rate swap market conditions could have a material impact on our financial condition and results of operations.

Currently, we sell a portion of the residential real estate and government guaranteed loans we originate. The profitability of these operations depends in large part upon our ability to make loans and to sell them in the secondary market at a gain. Thus, we are dependent upon the existence of an active secondary market and our ability to profitably sell loans into that market.

In addition to being affected by interest rates, the secondary markets are also subject to investor demand for residential mortgages and government guaranteed loans and investor yield requirements for those loans. These conditions may fluctuate or even worsen in the future. As a result, a prolonged period of secondary market illiquidity may reduce our loan production volumes and could have a material adverse effect on our financial condition and results of operations.

The interest rate swap market is dependent upon market conditions. If interest rates move, interest rate swap transactions may no longer make sense for the Company and/or its customers. Interest rate swaps are generally appropriate for commercial customers with a certain level of expertise and comfort with derivatives, so our success is dependent upon the ability to make loans to these types of commercial customers. Additionally, our ability to execute interest rate swaps is also dependent upon counterparties that are willing to enter into the interest rate swap that is equal and offsetting to the interest rate swap we enter into with the commercial customer.

Table of Contents

Consumers and businesses are increasingly using non-banks to complete their financial transactions, which could adversely affect our business and results of operations.

Technology and other changes are allowing consumers and businesses to complete financial transactions that historically have involved banks through alternative methods. For example, the wide acceptance of Internet-based commerce has resulted in a number of alternative payment processing systems and lending platforms in which banks play only minor roles. Customers can now maintain funds in prepaid debit cards or digital currencies, and pay bills and transfer funds directly without the direct assistance of banks. The diminishing role of banks as financial intermediaries has resulted and could continue to result in the loss of fee income, as well as the loss of customer deposits and the related income generated from those deposits. The loss of these revenue streams and the potential loss of lower cost deposits as a source of funds could have a material adverse effect on our business, financial condition and results of operations.

New lines of business or new products and services may subject us to additional risks.

From time to time, we may seek to implement new lines of business or offer new products and services within existing lines of business in our current markets or new markets. 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, we 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, which could in turn have a material negative effect on our operating results.

We have a substantial amount of debt outstanding and may incur additional indebtedness in the future, which could restrict our operations.

As of December 31, 2018, on an adjusted basis to give effect to the sale of our 5.375% Fixed-to-Floating Rate Subordinated Notes due February 15, 2029 (the “Notes”) and the application of the net proceeds to the repayment of our then existing indebtedness with First National Bank of Omaha, we had approximately $101.1 million of total indebtedness outstanding at the holding company level. In the future, it is possible that we may not generate sufficient revenues to service or repay our debt, and have sufficient funds left over to achieve or sustain profitability in our operations, meet our working capital and capital expenditure needs, and to pay dividends to our common stockholders.

Moreover, the degree to which we are leveraged could have important consequences for our stockholders, including:

- limiting our flexibility in planning for, or reacting to, changes in our business and the industry in which we operate;
- making it more difficult for us to satisfy our debt and other obligations;
- limiting our ability to borrow additional funds, or to sell assets to raise funds, if needed, for working capital, capital expenditures, acquisitions or other purposes;
- increasing our vulnerability to general adverse economic and industry conditions, including changes in interest rates; and
- placing us at a competitive disadvantage compared to our competitors that have less debt.

Item 1B. Unresolved Staff Comments

There are no unresolved staff comments.

Table of Contents

Item 2. Properties

The following table is a listing of the Company's operating facilities:

Facility Address	Facility Square Footage	Facility Owned or Leased
QCR Holdings, Inc.		
3551 7th Street in Moline, IL (1)	30,000	Owned
4550 N Brady Street in Davenport, IA	10,300	Owned
QCBT		
2118 Middle Road in Bettendorf, IA	6,700	Owned
4500 N Brady Street in Davenport, IA	36,000	Owned
5405 Utica Ridge Road in Davenport, IA	7,400	Leased
1700 Division Street in Davenport, IA	12,000	Owned
CRBT		
500 1st Avenue NE, in Cedar Rapids, IA	48,000	Owned
5400 Council Street in Cedar Rapids, IA	5,900	Owned
422 Commercial Street in Waterloo, IA (2)	25,000	Owned
11 Tower Park Drive in Waterloo, IA (2)	6,000	Owned
312 W 1st Street in Cedar Falls, IA (2)	4,800	Owned
2711 Bever Ave SE in Cedar Rapids, IA (3)	2,200	Owned
191 Jacolyn Dr NW in Cedar Rapids, IA (3) (4)	1,700	Owned
700 25th St in Marion, IA (3)	3,400	Owned
3406 F Ave NW in Cedar Rapids, IA (4)	4,100	Owned
CSB		
817 N Ankeny Boulevard, in Ankeny, IA	13,000	Owned
200 8th Street SE, in Altoona, IA	6,000	Owned
902 SE Oralabor Road, in Ankeny, IA	3,900	Owned
1640 SW White Birch Circle, in Ankeny, IA	15,700	Owned
3540 E 33rd Street, in Des Moines, IA	3,900	Owned
1401 E Euclid, in Des Moines, IA	4,500	Owned
6175 Merle Hay Road, in Johnston, IA	9,200	Owned
1025 N Hickory Boulevard, in Pleasant Hill, IA	4,500	Owned
4811 SE 14th Street, in Des Moines, IA	3,500	Owned
460 SE University Avenue, in Waukee, IA	6,000	Owned
RB&T		
4571 Guilford Road in Rockford, IL	20,000	Owned
308 West State Street in Rockford, IL	1,100	Leased
SFC Bank		
2006 S Glenstone Ave in Springfield, MO	14,500	Owned
1615-B East Primrose in Springfield, MO	1,400	Leased

m2		
175 North Patrick Boulevard in Brookfield, WI	6,500	Leased
Bates Companies		
8437 Northern Avenue in Rockford, IL	12,400	Leased

(1) This facility is utilized as a branch of QCBT in addition to housing the holding company.
(2) Branches of Community Bank & Trust, a division of CRBT.
(3) Branches acquired in 2018 through the purchase of Guaranty Bank.
(4) Branch at 3406 F Ave NW in Cedar Rapids, IA opened in February 2019 and replaced the branch at 191 Jacolyn Dr NW in Cedar Rapids, IA, which closed in February 2019.

The subsidiary banks intend to limit their investment in premises to no more than 50% of their capital. Management believes that the facilities are of sound construction, in good operating condition, are appropriately insured, and are adequately equipped for carrying on the business of the Company.

No individual real estate property amounts to 10% or more of consolidated assets.

Table of Contents

Item 3. Legal Proceedings

There are no material pending legal proceedings to which the Company or any of its subsidiaries is a party other than ordinary routine litigation incidental to their respective businesses.

Item 4. Mine Safety Disclosures

Not applicable.

Table of Contents

Part II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Market Information. The common stock, par value $1.00 per share, of the Company is listed on The Nasdaq Global Market under the symbol "QCRH". The stock began trading on Nasdaq on October 6, 1993. The Company transferred its listing from the Nasdaq Capital Market to the Nasdaq Global Market on March 1, 2010. As of February 28, 2019, there were 15,738,761 shares of common stock outstanding held by 782 holders of record. Additionally, there are an estimated 3,500 beneficial holders whose stock was held in the street name by brokerage houses and other nominees as of that date.

Dividends on Common Stock. The Company is heavily dependent on dividend payments from its subsidiary banks to provide cash flow for the operations of the holding company and dividend payments on the Company's common stock. Under applicable state laws, the banks are restricted as to the maximum amount of dividends that they may pay on their common stock. Iowa, Illinois and Missouri law provide that state-chartered banks in those states may not pay dividends in excess of their undivided profits.

The Company's ability to pay dividends to its stockholders may be affected by both general corporate law considerations and policies of the Federal Reserve applicable to bank holding companies. The payment of dividends by any financial institution or its holding company is affected by the requirement to maintain adequate capital pursuant to applicable capital adequacy guidelines and regulations, and a financial institution generally is prohibited from paying any dividends if, following payment thereof, the institution would be undercapitalized. See Appendix A for additional information regarding regulatory restrictions on the payment of dividends.

The Company also has certain contractual restrictions on its ability to pay dividends. The Company has issued junior subordinated debentures in private placements. Under the terms of the debentures, the Company may be prohibited, under certain circumstances, from paying dividends on shares of its common stock. None of these circumstances existed through the date of filing of this Form 10 K. See Note 16 to the Consolidated Financial Statements for additional information regarding dividend restrictions.

Purchase of Equity Securities by the Company. There were no purchases of common stock by the Company during the years ended December 31, 2018, 2017, and 2016.

26

Table of Contents

Stockholder Return Performance Graph. The following graph indicates, for the period commencing December 31, 2013 and ending December 31, 2018, a comparison of cumulative total returns for the Company, the Nasdaq Composite Index, and the SNL Bank Nasdaq Index prepared by S&P Global, Charlottesville, Virginia. The graph was prepared at the Company's request by S&P Global. The information assumes that $100 was invested at the closing price on December 31, 2013 in the common stock of the Company and in each index, and that all dividends were reinvested.

Index	12/31/13	12/31/14	12/31/15	12/31/16	12/31/17	12/31/18
QCR Holdings, Inc.	100.00	105.34	143.77	257.67	256.15	192.95
Nasdaq Composite Index	100.00	114.75	122.74	133.62	173.22	168.30
SNL Bank Nasdaq Index	100.00	103.57	111.80	155.02	163.20	137.56

Table of Contents

Item 6. Selected Financial Data

The following "Selected Financial Data" of the Company is derived in part from, and should be read in conjunction with, our Consolidated Financial Statements and the accompanying notes thereto. See Item 8. Financial Statements. Results for past periods are not necessarily indicative of results to be expected for any future period.

	Year Ended December 31,				
	2018	2017	2016	2015	2014
	(dollars in thousands, except per share data)				
STATEMENT OF INCOME DATA					
Interest income	$ 182,879	$ 135,517	$ 106,468	$ 90,003	$ 85,965
Interest expense	40,484	19,452	11,951	13,707	16,894
Net interest income	142,395	116,065	94,517	76,296	69,071
Provision for loan/lease losses	12,658	8,470	7,478	6,871	6,807
Non-interest income	41,541	30,482	31,037	24,364	21,282
Non-interest expense (1)	119,143	97,424	81,486	73,192	65,554
Income tax expense	9,015	4,946	8,903	3,669	3,039
Net income attributable to QCR Holdings, Inc.	43,120	35,707	27,687	16,928	14,953
Less: preferred stock dividends and discount accretion	—	—	—	—	1,082
Net income attributable to QCR Holdings, Inc. common stockholders	43,120	35,707	27,687	16,928	13,871
PER COMMON SHARE DATA					
Net income - Basic (2)	$ 2.92	$ 2.68	$ 2.20	$ 1.64	$ 1.75
Net income - Diluted (2)	2.86	2.61	2.17	1.61	1.72
Cash dividends declared	0.24	0.20	0.16	0.08	0.08
Dividend payout ratio	8.22 %	7.46 %	7.27 %	4.88 %	4.57 %
Closing stock price	$ 32.09	$ 42.85	$ 43.30	$ 24.29	$ 17.86
BALANCE SHEET DATA					
Total assets	$ 4,949,710	$ 3,982,665	$ 3,301,944	$ 2,593,198	$ 2,524,958
Securities	662,969	652,382	574,022	577,109	651,539
Total loans/leases	3,732,754	2,964,485	2,405,487	1,798,023	1,630,003
Allowance	39,847	34,356	30,757	26,141	23,074
Deposits	3,977,031	3,266,655	2,669,261	1,880,666	1,679,668
Borrowings	404,969	309,480	290,952	444,162	662,558
Stockholders' equity: common	473,138	353,287	286,041	225,886	144,079
KEY RATIOS					

ROAA (3)	0.98	%	1.01	%	0.97	%	0.66	%	0.61	%
ROACE (2)	10.62		11.51		10.56		8.79		10.49	
ROAE (3)	10.62		11.51		10.56		8.79		10.48	
NIM, tax equivalent yield (Non-GAAP) (4) (6)	3.62		3.78		3.75		3.37		3.15	
Efficiency ratio (Non-GAAP) (5) (6)	64.77		66.48		64.90		72.71		72.55	
Loans/leases to assets	75.41		74.43		72.85		69.34		64.56	
Loans/leases to deposits	93.86		90.75		90.12		95.61		97.04	
NPAs to total assets	0.56		0.81		0.82		0.74		1.31	
Allowance to total loans/leases	1.07		1.16		1.28		1.45		1.42	
Allowance to NPLs	214.80		184.28		144.85		223.33		114.78	
Net charge-offs to average loans/leases	0.21		0.19		0.14		0.22		0.34	
Average total stockholders' equity to average total assets	9.24		8.81		9.21		7.55		5.82	

(1) Non-interest expense includes several one-time expenses - most notably, $3.9 million, $5.4 million and $2.4 million of acquisition and post-acquisition compensation, transition and integration costs for 2018, 2017 and 2016, respectively. See Note 2 to the Consolidated Financial Statements for additional information regarding the merger with Springfield Bancshares, the Bates Companies, Guaranty Bank and CSB. Additionally, non-interest expense for 2016 and 2015, respectively, included $4.6 million and $7.2 million of losses on debt extinguishment related to the prepayment of certain borrowings.

(2) Numerator is net income attributable to QCR Holdings, Inc. common stockholders.

(3) Numerator is net income attributable to QCR Holdings, Inc.

(4) Interest earned and yields on nontaxable investments and nontaxable loans are determined on a tax equivalent basis using a 35% tax rate for years including and prior to December 31, 2017 and 21% for years after December 31, 2017.

(5) Non-interest expenses divided by the sum of net interest income before provision for loan/lease losses and non-interest income.

(6) See GAAP to Non-GAAP reconciliations.

Table of Contents

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion provides additional information regarding our operations for the years ending December 31, 2018, 2017, and 2016, and our financial condition at December 31, 2018 and 2017. This discussion should be read in conjunction with "Selected Financial Data" and our Consolidated Financial Statements and the accompanying notes thereto included or incorporated by reference elsewhere in this document.

Additionally, a comprehensive list of the acronyms and abbreviations used throughout this discussion is included in Note 1 to the Consolidated Financial Statements.

GENERAL

The Company was formed in February 1993 for the purpose of organizing QCBT. Over the past twenty-five years, the Company has grown to include four additional banking subsidiaries and a number of nonbanking subsidiaries. As of December 31, 2018, the Company had $4.9 billion in consolidated assets, including $3.7 billion in total loans/leases and $4.0 billion in deposits. The financial results of acquired/merged entities for the periods since their acquisition/merger are included in this report.

EXECUTIVE OVERVIEW

The Company reported net income of $43.1 million for the year ended December 31, 2018, and diluted EPS of $2.86. For the same period in 2017, the Company reported net income of $35.7 million, and diluted EPS of $2.61. By comparison, for 2016, the Company reported net income of $27.7 million, and diluted EPS of $2.17.

The year ended December 31, 2018 was highlighted by several significant items:

- The successful merger with Springfield Bancshares and the acquisition of the Bates Companies (described in Note 2 to the Consolidated Financial Statements);
- Record noninterest income of $41.5 million for the year;
- Organic deposit growth of 8.3% for the year;
- Organic loan and lease growth of 9.8% for the year; and
- Nonperforming assets to total assets down to 0.56% at December 31, 2018 from 0.81% at December 31, 2017.

Following is a table that represents the various net income measurements for the years ended December 31, 2018, 2017, and 2016.

	Year Ended December 31,		
	2018	2017	2016
Net income	$ 43,119,699	$ 35,706,507	$ 27,686,787
Diluted earnings per common share	$ 2.86	$ 2.61	$ 2.17
Weighted average common and common equivalent shares outstanding*	15,064,730	13,680,472	12,766,003

* The 2018 and 2017 increase in the weighted average common and common equivalent shares outstanding was primarily due to the common stock issued in connection with the merger with Springfield Bancshares and acquisition of Guaranty Bank discussed in Note 2 to the Consolidated Financial Statements.

The Company reported adjusted net income (non-GAAP) of $46.4 million, with diluted adjusted EPS of $3.08. See section titled “GAAP to Non-GAAP Reconciliations” for additional information. Adjusted net income for the year excludes a number of non-recurring items, most significantly $3.3 million of after-tax acquisition and post-acquisition related costs. The Tax Act was enacted in December 2017 and reduced the federal corporate tax rate from 35% to 21%. As a result, the Company revalued the deferred tax assets and liabilities to reflect the lower federal corporate tax rate, which resulted in the Company recognizing a benefit of $2.9 million in the fourth quarter of 2017. See Note 13 to the Consolidated Financial Statements for additional information regarding the impact of the Tax Act on deferred tax assets and income tax expense.

Table of Contents

Following is a table that represents the major income and expense categories.

	Year Ended December 31,		
	2018	2017	2016
Net interest income	$ 142,395,585	$ 116,065,281	$ 94,516,777
Provision expense	12,658,449	8,469,919	7,478,166
Noninterest income	41,541,094	30,482,292	31,036,875
Noninterest expense	119,143,419	97,424,697	81,485,912
Federal and state income tax expense	9,015,112	4,946,450	8,902,787
Net income	$ 43,119,699	$ 35,706,507	$ 27,686,787

The following are some noteworthy developments in the Company's financial results:

· Net interest income grew $26.3 million, or 23% in 2018, compared to the prior year. Net interest income for 2017 grew $21.5 million, or 23%, compared to 2016. The increase in 2018 was primarily due to strong organic loan and lease growth and recent acquisitions.

· Provision increased $4.2 million when comparing 2018 to 2017, while provision increased $992 thousand when comparing 2017 to 2016. The increase in 2018 was primarily attributable to loans to two unrelated borrowers as well as to strong loan growth and accounting for acquired loans (as acquired loans renew, the discount associated with those loans is eliminated and the Company must establish an allowance).

· Noninterest income increased $11.1 million, or 36%, when compared to the prior year. Noninterest income decreased $555 thousand, or 2%, when comparing 2017 to 2016. The increase in 2018 was primarily attributable to higher swap fee income as well as solid growth in wealth management fee income and recent acquisitions.

· Noninterest expense increased $21.7 million, or 22% in 2018, compared to the prior year, including:

oAcquisition and post-acquisition compensation, transition and integration costs totaling $3.9 million and $5.4 million in 2018 and 2017, respectively. The increase from 2016 primarily was due to legal and accounting costs and IT integration and conversion costs associated with recent acquisitions.

oOccupancy and equipment expense increased $1.9 million in 2018, due to renovations of existing facilities and to the additional facilities acquired in recent acquisitions.

oSalaries and benefits increased $13.3 million with the addition of personnel with recent acquisitions as well as new positions created to build scale.

oNet cost of operations and gains/losses on other real estate increased $2.5 million primarily due to the $2.0 million writedown of one large OREO property and the sale of a $1.3 million OREO property at a loss of $424 thousand.

LONG-TERM FINANCIAL GOALS

The Company has established certain financial goals by which it manages its business and measures its performance. The goals are periodically updated to reflect business developments. While the Company is determined to work prudently to achieve these goals, there is no assurance that they will be met. Moreover, the Company's ability to achieve these goals will be affected by the factors discussed under "Forward Looking Statements" as well as the factors detailed in the "Risk Factors" section included under Item 1A. of Part I of this Form 10 K. The Company's long-term financial goals are as follows:

· Strong organic loan and lease growth in order to maintain a gross loans and leases to total assets ratio in the range of 73 – 78%;

· Improve profitability (measured by NIM and ROAA);

· Improve asset quality by reducing NPAs to total assets to below 0.75% and maintain charge-offs as a percentage of average loans/leases of under 0.25% annually;

Table of Contents

- Grow core deposits to maintain reliance on wholesale funding at less than 15% of total assets;

- Continue to focus on generating gains on sales of government guaranteed portions of loans and swap fee income to more than $4 million annually; and

- Grow wealth management net income by 10% annually.

The following table shows the evaluation of the Company's long-term financial goals.

Goal	Key Metric (1)	Target (2)	For the Year Ending December 31, 2018	For the Year Ending December 31, 2017
Balance sheet efficiency	Gross loans and leases to total assets	73% - 78%	75 %	74 %
	NIM TEY (non-GAAP)	> 3.65%	3.62 %	3.78 %
Profitability	ROAA	> 1.10%	0.98 %	1.01 %
	Adjusted ROAA (non-GAAP)	> 1.10%	1.06 %	1.03 %
Asset quality	NPAs to total assets	< 0.75%	0.56 %	0.81 %
	Net charge-offs to average loans and leases	< 0.25% annually	0.21 %	0.19 %
Reliance on wholesale funding	Wholesale funding to total assets (3)	< 15%	14 %	10 %
Consistent, high quality noninterest income revenue streams	Gains on sales of government guaranteed portions of loans and swap fee income	> $4 million annually	11.2 $ million	$ 4.3 million
	Grow wealth management net income	> 10% annually	32 %	35 %

(1) Refer to GAAP to non-GAAP Reconciliation for detail concerning non-GAAP financial measures.
(2) Targets will be re-evaluated and adjusted as appropriate.
(3) Wholesale funding to total assets is calculated by dividing total borrowings and brokered deposits by total assets.

STRATEGIC DEVELOPMENTS

The Company took the following actions in 2018 to support our corporate strategy and further the long-term financial goals shown above.

- Organic loan and lease growth for the year was 9.8%. This was slightly below the Company's target organic growth rate of 10 12%. A portion of this growth was in the C&I category. As of December 31, 2018, this segment of the portfolio accounted for 38% of total loans and leases. The Company has also grown CRE loans, with that segment now representing 48% of the portfolio as of December 31, 2018. The strong organic loan and lease growth has continued to help move the loan and lease to total asset ratio upward to 75%, from 74% in the prior year and 73% two years ago. The Company has reached the targeted loan and lease to total asset ratio in the range of 73% - 78%. Going forward, the Company will strive to maintain the ratio in this range.

.

The Company intends to continue to participate in a prudent manner as an acquirer in the consolidation taking place in our markets to further boost ROAA and improve the Company's efficiency ratio. In the fourth quarter of 2018, the Company acquired the Bates Companies, headquartered in Rockford, Illinois. In the third quarter of 2018, the Company mergered with Springfield Bancshares, headquartered in Springfield, Missouri. See Note 2 of the Consolidated Financial Statements for additional detail concerning the acquisition and merger.

· The Company continues to focus on reducing the NPAs to total assets ratio. The ratio of NPAs to total assets decreased from 0.81% at December 31, 2017 to 0.56% at December 31, 2018. The Company remains committed to improving asset quality in 2019.

· Management continues to focus on reducing the Company's reliance on wholesale funding and continues to prioritize core deposit growth through a variety of strategies including growth in correspondent banking.

· Correspondent banking continues to be a core line of business for the Company. The Company is competitively positioned with experienced staff, software systems and processes to continue growing in the three states currently served – Iowa, Illinois and Wisconsin - and to expand into Missouri. The Company acts as the correspondent bank for 190 downstream banks with total average noninterest bearing deposits of $183.5 million and total average interest bearing deposits of $233.9 million as of December 31, 2018. This line of business provides a

Table of Contents

strong source of noninterest bearing and interest bearing deposits, fee income, high-quality loan participations and bank stock loans.

- As a result of the relatively low interest rate environment including a flat yield curve, the Company is focused on executing interest rate swaps on select commercial loans. The interest rate swaps allow the commercial borrowers to pay a fixed interest rate while the Company receives a variable interest rate as well as an upfront fee dependent on the pricing. Management believes that these swaps help position the Company more favorably for rising rate environments. The Company will continue to review opportunities to execute these swaps at all of its subsidiary banks, as the circumstances are appropriate for the borrower and the Company.

- Wealth management is another core line of business for the Company and includes a full range of products, including trust services, brokerage and investment advisory services, asset management, estate planning and financial planning. As of December 31, 2018, the Company had $2.8 billion of total financial assets in trust and related accounts and $1.6 billion of total financial assets in brokerage and related accounts. Continued growth in assets under management will help to drive trust and investment advisory fees. The Company offers trust and investment advisory services to the correspondent banks that it serves. As management focuses on growing fee income, expanding market share will continue to be a primary strategy both through organic growth as well as the acquisition of managed assets. On October 1, 2018, the Company acquired the Bates Companies, headquartered in Rockford, Illinois. The acquisition enhanced the wealth management services of the Company by adding approximately $704 million of assets under management as of October 1, 2018.

GAAP TO NON-GAAP RECONCILIATIONS

The following table presents certain non-GAAP financial measures related to the “TCE/TA ratio”, “adjusted net income”, “adjusted net income attributable to QCR Holdings, Inc. common stockholders”, “adjusted EPS”, “adjusted ROAA”, “NIM (TEY)”, “adjusted NIM” and “efficiency ratio”. In compliance with applicable rules of the SEC, all non-GAAP measures are reconciled to the most directly comparable GAAP measure, as follows:

- TCE/TA ratio (non-GAAP) is reconciled to stockholders’ equity and total assets;

- Adjusted net income, adjusted net income attributable to QCR Holdings, Inc. common stockholders, adjusted EPS and adjusted ROAA (all non-GAAP measures) are reconciled to net income;

- NIM (TEY) (non-GAAP) and adjusted NIM (non-GAAP) are reconciled to NIM; and

- Efficiency ratio (non-GAAP) is reconciled to noninterest expense, net interest income and noninterest income.

The TCE/TA non-GAAP ratio has been a focus for investors and management believes that this ratio may assist investors in analyzing the Company’s capital position without regard to the effects of intangible assets.

The table below also includes the following “adjusted” non-GAAP measurements of financial performance: adjusted net income, adjusted net income attributable to QCR Holdings, Inc. common stockholders, adjusted earnings per share and adjusted return on average assets. The Company’s management believes that these measures are important to investors as they exclude non-recurring income and expense items; therefore, they provide a better comparison for analysis and may provide a better indicator of future results.

NIM (TEY) is a financial measure that the Company's management utilizes to take into account the tax benefit associated with certain loans and securities. It is standard industry practice to measure net interest margin using tax-equivalent measures. In addition, the Company calculates NIM without the impact of acquisition accounting net accretion (adjusted NIM), as accretion amounts can fluctuate a great deal, making comparisons difficult.

The efficiency ratio is a ratio that management utilizes to compare the Company to peers. It is standard in the banking industry and widely utilized by investors.

Non-GAAP financial measures have inherent limitations, are not required to be uniformly applied, and are not audited. Although these non-GAAP financial measures are frequently used by investors to evaluate a company, they have

Table of Contents

limitations as analytical tools and should not be considered in isolation, or as a substitute for analyses of results as reported under GAAP.

GAAP TO NON-GAAP RECONCILIATIONS	As of December 31, 2018	December 31, 2017
	(dollars in thousands, except per share data)	
TCE/TA RATIO		
Stockholders' equity (GAAP)	$ 473,138	$ 353,287
Less: Intangible assets	95,282	37,413
TCE (non-GAAP)	$ 377,856	$ 315,874
Total assets (GAAP)	$ 4,949,710	$ 3,982,665
Less: Intangible assets	95,282	37,413
TA (non-GAAP)	$ 4,854,428	$ 3,945,252
TCE/TA ratio (non-GAAP)	7.78 %	8.01 %

	For the Year Ended December 31, 2018	December 31, 2017	December 31, 2016	December 31, 2015	December 31, 2014
ADJUSTED NET INCOME					
Net income (GAAP)	$ 43,120	$ 35,707	$ 27,687	$ 16,928	$ 14,953
Less nonrecurring items (post-tax) (*):					
Income:					
Securities gains, net	$ —	$ (57)	$ 2,985	$ 519	$ 60
Total nonrecurring income (non-GAAP)	$ —	$ (57)	$ 2,985	$ 519	$ 60
Expense:					
Losses on debt extinguishment	$ —	$ —	$ 2,975	$ 4,671	$ —
Acquisition costs	1,645	695	1,086	—	—
Post-acquisition compensation, transition and integration costs	1,647	2,802	677	(487)	—
Accrual adjustments	—	—	—	513	—
Total nonrecurring expense (non-GAAP)	$ 3,292	$ 3,497	$ 4,738	$ 4,697	$ 60
Adjustment of tax expense related to the	$ —	$ 2,919	$ —	$ —	$ —

Tax Act					
Adjusted net income (non-GAAP)	$ 46,412	$ 36,342	$ 29,440	$ 20,854	$ 14,893
Less: Preferred Stock Dividends	—	—	—	—	1,082
Adjusted net income attributalbe to QCR Holdings, Inc common stochholders (non-GAAP)	$ 46,412	$ 36,342	$ 29,440	$ 20,854	$ 13,811
ADJUSTED EPS					
Adjusted net income (non-GAAP) (from above)	$ 46,412	$ 36,342	$ 29,440	$ 20,854	$ 13,811
Weighted average common shares outstanding	14,768,687	13,325,128	12,570,767	10,345,286	7,925,220
Weighted average common and common equivalent shares outstanding	15,064,730	13,680,472	12,766,003	10,499,841	8,048,661
Adjusted EPS (non-GAAP):					
Basic	$ 3.14	$ 2.73	$ 2.34	$ 2.02	$ 1.74
Diluted	$ 3.08	$ 2.66	$ 2.31	$ 1.99	$ 1.72
ADJUSTED ROAA					
Adjusted net income (non-GAAP) (from above)	$ 46,412	$ 36,342	$ 29,440	$ 20,854	$ 14,893
Average Assets	$ 4,392,121	$ 3,519,848	$ 2,846,699	$ 2,549,921	$ 2,453,678
Adjusted ROAA (annualized) (non-GAAP)	1.06 %	1.03 %	1.03 %	0.82 %	0.61 %
ADJUSTED NIM (TEY)*					
Net interest income (GAAP)	$ 142,395	$ 116,065	$ 94,517	$ 76,296	$ 69,071
Plus: Taxequivalent adjustment	6,637	9,215	6,021	4,881	3,977
Net interest income - taxequivalent	$ 149,032	$ 125,280	$ 100,538	$ 81,177	$ 73,048

(non-GAAP)										
Less: Accquisition accounting net accretion	5,527		4,774		3,718		367		675	
Adjusted net interest income	$ 143,505		$ 120,506		$ 96,820		$ 80,810		$ 72,373	
Average earning assets	$ 4,120,144		$ 3,314,836		$ 2,678,359		$ 2,406,213		$ 2,319,441	
NIM (GAAP)	3.46	%	3.50	%	3.53	%	3.17	%	2.98	%
NIM (TEY) (non-GAAP)	3.62	%	3.78	%	3.75	%	3.37	%	3.15	%
Adjusted NIM (TEY) (non-GAAP)	3.48	%	3.64	%	3.61	%	3.36	%	3.12	%
EFFICIENCY RATIO										
Noninterest expense (GAAP)	$ 119,143		$ 97,424		$ 81,486		$ 73,192		$ 65,554	
Net interest income (GAAP)	$ 142,395		$ 116,065		$ 94,517		$ 76,296		$ 69,071	
Noninterest income (GAAP)	41,541		30,482		31,037		24,363		21,282	
Total income	$ 183,936		$ 146,547		$ 125,554		$ 100,659		$ 90,353	
Efficiency ratio (noninterest expense/total income) (non-GAAP)	64.77	%	66.48	%	64.90	%	72.71	%	72.55	%

* Nonrecurring items (after-tax) are calculated using an estimated effective tax rate of 35% for each year including and prior to December 31, 2017 and 21% for each period after December 31, 2017.

Table of Contents

NET INTEREST INCOME AND MARGIN (TAX EQUIVALENT BASIS) (Non-GAAP)

As part of the Tax Act, the Company's federal income tax rate was reduced from 35% down to 21% effective January 1, 2018. In order to compare periods before and after the effective date of the Tax Act, it's important to note the difference in the federal income tax rate and the impact on the Company's tax exempt earning assets (loans and securities) and the related tax equivalent yield reporting.

Net interest income, on a tax equivalent basis, increased 19% to $149.0 million for the year ended December 31, 2018, compared to the prior year. Excluding the tax equivalent adjustments, net interest income increased 23% for the year ended December 31, 2018 compared to the prior year. Net interest income improved due to several factors:

- The merger with Springfield Bancshares in the third quarter of 2018 and the acquisition of Guaranty Bank in the fourth quarter of 2017;
- Organic loan growth has been strong over the past 12 months pushing loans/leases up to 75.4% of total assets; and
- The Company's continued strategy to redeploy funds from cash and lower yielding taxable securities portfolio into higher yielding loans and municipal bonds, especially with the Company's most recent acquisitions of SFC Bank and Guaranty Bank.

A comparison of yields, spread and margin on a tax equivalent and GAAP basis is as follows:

	Tax Equivalent Basis For the Year Ended			GAAP For the Year Ended		
	December 31, 2018	December 31, 2017	December 31, 2016	December 31, 2018	December 31, 2017	December 31, 2016
Average Yield on Interest-Earning Assets	4.60 %	4.37 %	4.20 %	4.44 %	4.09 %	3.98 %
Average Cost of Interest-Bearing Liabilities	1.29 %	0.81 %	0.65 %	1.29 %	0.81 %	0.65 %
Net Interest Spread	3.31 %	3.56 %	3.55 %	3.15 %	3.28 %	3.33 %
NIM	3.62 %	3.78 %	3.75 %	3.46 %	3.50 %	3,53 %
NIM Excluding Acquisition Accounting Net Accretion	3.48 %	3.63 %	3.61 %	3.32 %	3.35 %	3.39 %

Acquisition accounting net accretion can fluctuate mostly depending on the payoff activity of the acquired loans. In evaluating net interest income and NIM, it's important to understand the impact of acquisition accounting net accretion when comparing periods. The above table reports NIM with and without the acquisition accounting net accretion to allow for more appropriate comparisons. A comparison of acquisition accounting net accretion included in NIM is as follows:

For the Year Ended

	December 31, 2018	December 31, 2017	December 31, 2016
	dollars in thousands		
Acquisition Accounting Net Accretion in NIM	5,527	$ 4,941	$ 3,718

Excluding acquisition accounting net accretion, NIM was down four basis points on a linked-year basis. This margin compression was primarily due to the following:

- Increases in the cost of funds due to both mix and rate as the Company continues to grow larger commercial and public deposit relationships which tend to have higher interest rate sensitivity;
- With the flat yield curve and continued competition in our markets, loan pricing continues to be pressured. The Company has had success in widening spreads as core loan yields increased over the year; however, the pace and magnitude of the widening has been offset by the increasing cost of funds; and
- The addition of SFC Bank and its NIM was expansive to the Company's NIM, though only for half of 2018.

Table of Contents

The Company's management closely monitors and manages NIM. From a profitability standpoint, an important challenge for the Company's subsidiary banks and leasing company is focusing on quality growth in conjunction with the improvement of their NIMs. Management continually addresses this issue with pricing and other balance sheet management strategies which included better loan pricing, reducing reliance on very rate-sensitive funding, closely managing deposit rate increases and finding additional ways to manage cost of funds through derivatives.

The Company’s average balances, interest income/expense, and rates earned/paid on major balance sheet categories are presented in the following table:

	Year Ended December 31,								
	2018			2017			2016		
	Average Balance	Interest Earned or Paid	Average Yield or Cost	Average Balance	Interest Earned or Paid	Average Yield or Cost	Average Balance	Interest Earned or Paid	A Yi Co
	(dollars in thousands)								
rning									
nds sold	$ 20,472	$ 338	1.65 %	$ 17,577	$ 149	0.85 %	$ 15,142	$ 45	0.
aring									
financial									
s	66,275	1,267	1.91	78,842	874	1.11	70,757	393	0.
t									
(1)	659,017	23,621	3.58	590,761	22,460	3.80	535,912	19,054	3.
t									
	22,023	1,093	4.96	15,768	631	4.00	13,993	522	3.
s/leases									
(1) (2) (3)	3,352,357	163,197	4.87	2,611,888	120,618	4.62	2,042,555	92,475	4.
est									
sets	$ 4,120,144	189,516	4.60	$ 3,314,836	144,732	4.37	$ 2,678,359	112,489	4.
st-earning									
due from									
	$ 72,920			$ 67,559			$ 53,650		
nd									
	68,602			62,719			44,773		
ance	(38,200)			(33,193)			(28,686)		
	168,655			107,927			98,603		
ts	$ 4,392,121			$ 3,519,848			$ 2,846,699		
IES AND									
OLDERS'									
aring									
	$ 2,043,314	18,651	0.91 %	$ 1,622,723	7,992	0.49 %	$ 1,092,687	3,843	0.

aring									
sits	766,020	12,024	1.57	528,834	5,020	0.95	436,070	2,175	0.
n									
s	19,458	271	1.39	22,596	114	0.50	50,899	94	0.
ances	202,715	4,193	2.07	120,206	1,981	1.65	114,797	1,284	1.
owings	69,623	3,346	4.81	73,394	2,879	3.92	98,105	3,318	3.
ordinated	37,578	1,999	5.32	34,030	1,466	4.31	33,735	1,237	3.
aring	$ 3,138,708	40,484	1.29	$ 2,401,783	19,452	0.81	$ 1,826,293	11,951	0.
st-bearing eposits	$ 792,885			$ 765,019			$ 714,867		
t-bearing	54,555			42,836			43,464		
lities	$ 3,986,148			$ 3,209,638			$ 2,584,624		
ers' equity	405,973			310,210			262,075		
lities and ers' equity	$ 4,392,121			$ 3,519,848			$ 2,846,699		
st income		$ 149,032			$ 125,280			$ 100,538	
st spread			3.31 %			3.56 %			3.
st margin			3.46 %			3.50 %			3.
st margin n-GAAP)			3.62 %			3.78 %			3.
et interest n-GAAP)			3.48 %			3.64 %			3.
verage rning verage aring	131.27 %			138.02 %			146.66 %		

(1) Interest earned and yields on nontaxable investment securities and loans are determined on a tax equivalent basis using a 35% tax rate in each years including and prior to December 31, 2017 and using a 21% tax rate for each year after December 31, 2017.

(2) Loan/lease fees are not material and are included in interest income from loans/leases receivable in accordance with accounting and regulatory guidance.

(3) Non-accrual loans/leases are included in the average balance for gross loans/leases receivable in accordance with accounting and regulatory guidance.

Table of Contents

The Company's components of change in net interest income are presented in the following table:

	For the years ended December 31, 2018, 2017 and 2016					
	Inc./(Dec.) from Prior Year	Components of Change (1)		Inc./(Dec.) from Prior Year	Components of Change (1)	
	2018 vs. 2017 (dollars in thousands)	Rate	Volume	2017 vs. 2016 (dollars in thousands)	Rate	Volume
INTEREST INCOME						
Federal funds sold	$ 189	$ 161	$ 28	$ 104	$ 96	$ 8
Interest-bearing deposits at financial institutions	393	550	(157)	481	431	50
Investment securities (2)	1,161	(1,334)	2,495	3,406	1,376	2,030
Restricted investment securities	462	175	287	109	40	69
Gross loans/leases receivable (2) (3)	42,579	6,829	35,750	28,143	1,886	26,257
Total change in interest income	$ 44,784	$ 6,381	$ 38,403	$ 32,243	$ 3,829	$ 28,414
INTEREST EXPENSE						
Interest-bearing deposits	$ 10,659	$ 8,176	$ 2,483	$ 4,149	$ 1,876	$ 2,273
Time deposits	7,004	4,153	2,851	2,845	2,302	543
Short-term borrowings	157	175	(18)	20	94	(74)
Federal Home Loan Bank advances	2,212	599	1,613	697	634	63
Other borrowings	467	621	(154)	(439)	478	(917)
Junior subordinated debentures	533	369	164	229	218	11
Total change in interest expense	$ 21,032	$ 14,093	$ 6,939	$ 7,501	$ 5,602	$ 1,899
Total change in net interest income	$ 23,752	$ (7,712)	$ 31,464	$ 24,742	$ (1,773)	$ 26,515

(1) The column "Inc/(Dec) from Prior Year" is segmented into the changes attributable to variations in volume and the changes attributable to changes in interest rates. The variations attributable to simultaneous volume and rate changes have been proportionately allocated to rate and volume.

(2) Interest earned and yields on nontaxable investment securities and loans are determined on a tax equivalent basis using a 35% tax rate in each year including and prior to December 31, 2017 and using a 21% tax rate in each year after December 31, 2017.

(3) Loan/lease fees are not material and are included in interest income from loans/leases receivable in accordance with accounting and regulatory guidance.

The Company's operating results are also impacted by various sources of noninterest income, including trust department fees, investment advisory and management fees, deposit service fees, gains from the sales of residential real estate loans and government guaranteed loans, earnings on BOLI, and other income. Offsetting these items, the Company incurs noninterest expenses, which include salaries and employee benefits, occupancy and equipment expense, professional and data processing fees, FDIC and other insurance expense, loan/lease expense, and other administrative expenses.

The Company's operating results are also affected by economic and competitive conditions, particularly changes in interest rates, income tax rates, government policies, and actions of regulatory authorities.

CRITICAL ACCOUNTING POLICIES

The Company's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America. The financial information contained within these statements is, to a significant extent, financial information that is based on approximate measures of the financial effects of transactions and events that have already occurred.

Based on its consideration of accounting policies that involve the most complex and subjective decisions and assessments, management has identified the following as critical accounting policies:

GOODWILL

The Company records all assets and liabilities purchased in an acquisition, including intangibles, at fair value. Goodwill is not amortized but is subject, at a minimum, to annual tests for impairment. In certain situations, interim impairment tests may be required if events occur or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount.

The initial recognition of goodwill and subsequent impairment analysis requires us to make subjective judgments concerning estimates of how the acquired assets will perform in the future using valuation methods, which may include using the current market price of stock or discounted cash flow analyses. Additionally, estimated cash flows may extend

Table of Contents

beyond five years and, by their nature, are difficult to determine over an extended timeframe. Events and factors that may significantly affect the estimates include, among others, competitive forces, customer behaviors, changes in revenue growth trends, cost structures, technology, changes in discount rates and market conditions. In determining the reasonableness of cash flow estimates, the Company reviews historical performance of the underlying assets or similar assets in an effort to assess and validate assumptions utilized in its estimates.

In assessing the fair value of reporting units, we may consider the stage of the current business cycle and potential changes in market conditions. We may also utilize other information to validate the reasonableness of our valuations, including public market comparables and multiples of recent mergers and acquisitions of similar businesses. Valuation multiples may be based on tangible capital ratios of comparable companies and business segments. These multiples may be adjusted to consider competitive differences, including size, operating leverage and other factors. The carrying amount of a reporting unit is determined based on the capital required to support the reporting unit's activities, including its tangible and intangible assets. The determination of a reporting unit's capital allocation requires judgment and considers many factors, including the regulatory capital regulations and capital characteristics of comparable companies in relevant industry sectors. In certain circumstances, the Company will engage a third-party to independently validate our assessment of the fair value of our reporting units.

The Company assesses the impairment of goodwill whenever events or changes in circumstances indicate the carrying value may not be recoverable. Factors considered important, which could trigger an impairment review, include the following:

- Significant under-performance relative to expected historical or projected future operating results;
- Significant changes in the manner of use of the acquired asets or the strategy for the overall business;
- Significant negative industry or economic trends; or
- Significant decline in the market price for our common stock over a sustained period; and market capitalization relative to net book value.

The Company conducted an internal assessment of the goodwill, both collectively and at its subsidiaries, in both 2018 and 2017 and determined no goodwill impairment charges were required.

ALLOWANCE FOR LOAN AND LEASE LOSSES

The Company's allowance methodology incorporates a variety of risk considerations, both quantitative and qualitative, in establishing an allowance that management believes is appropriate at each reporting date. Quantitative factors include the Company's historical loss experience, delinquency and charge-off trends, collateral values, governmental guarantees, payment status, changes in nonperforming loans/leases, and other factors. Quantitative factors also incorporate known information about individual loans/leases, including borrowers' sensitivity to interest rate movements.

Qualitative factors include the general economic environment in the Company's markets, including economic conditions both locally and nationally, and in particular, the economic health of certain industries. Size and complexity of individual credits in relation to loan/lease structure, existing loan/lease policies and pace of portfolio growth are other qualitative factors that are considered in the methodology. As the Company adds new products and increases the complexity of its loan/lease portfolio, it enhances its methodology accordingly.

Management may report a materially different amount for the provision in the statement of operations to change the allowance if its assessment of the above factors were different. The discussion regarding the Company's allowance should be read in conjunction with the Company's financial statements and the accompanying notes presented elsewhere in this Form 10 K, as well as the portion of this MD&A section entitled "Financial Condition – Allowance for Estimated Losses on Loans/Leases."

Although management believes the level of the allowance as of December 31, 2018 was adequate to absorb losses inherent in the loan/lease portfolio, a decline in local economic conditions, or other factors, could result in increasing losses that cannot be reasonably predicted at this time.

Table of Contents

RESULTS OF OPERATIONS FOR THE YEARS ENDED DECEMBER 31, 2018, 2017, and 2016

INTEREST INCOME

For 2018, interest income grew $47.4 million, or 35%. In total, the Company's average interest-earning assets increased $805.3 million, or 24%, year-over-year. Average loans/leases grew 28%, while average securities grew 12%. The acquisition of Guaranty Bank occurred in the fourth quarter of 2017, therefore 2018 was the first full year that Guaranty Bank was included in the Company's financial results. The merger with Springfield Bancshares in the third quarter of 2018 also contributed to the increase in interest income and average interest-earning assets.

For 2017, interest income grew $29.0 million, or 27%. In total, the Company's average interest-earning assets increased $636.5 million, or 24%, year-over-year. Average loans/leases grew 28%, while average securities grew 10%. The acquisition of CSB occurred in the third quarter of 2016, therefore 2017 was the first full year that CSB was included in the Company's financial results. The acquisition of Guaranty Bank in the fourth quarter of 2017 also contributed to the increase in interest income and average interest-earning assets.

Additionally, the Company continued to diversify its securities portfolio, including increasing its portfolio of tax exempt municipal securities. The large majority of these are privately placed debt issuances by municipalities located in the Midwest and require a thorough underwriting process before investment. Execution of this strategy has led to increased interest income on a tax equivalent basis over the past several years. Management understands that this strategy has extended the duration of its securities portfolio and continually evaluates the combined benefit of increased interest income and reduced effective income tax rate and the impact on interest rate risk.

The Company intends to continue to grow quality loans and leases as well as diversify the securities portfolio to maximize yield while minimizing credit and interest rate risk.

INTEREST EXPENSE

Comparing 2018 to 2017, interest expense increased $21.0 million, or 108%, year-over-year. Average interest-bearing liabilities increased 31% in 2018. The acquisition of Guaranty Bank occurred in the fourth quarter of 2017, therefore 2018 was the first full year that Guaranty Bank was included in the Company's financial results. SFC Bank, acquired at the beginning of the third quarter of 2018, also contributed to the increase in interest expense and average interest-bearing liabilities. Additionally, as the Company has grown organically at a significant pace over the past several years, the loan growth has been funded in larger part by bigger depositor relationships with higher rate sensitivity, many of which have pricing tied to a certain index. As a result, the cost of these funds is higher than the rest of the Company's core deposit portfolio, and the cost rises at a higher rate (beta) as market interest rates rise (which has been the case over the past year). The beta on the balance of the Company's core deposit portfolio has performed well and is much lower than the beta on relationships with pricing tied to a certain index. Additionally, loan growth has outpaced deposit growth, therefore, short-term borrowings have increased to temporarily fill in the funding gap and the cost of these funds has increased with the rising rate environment.

Comparing 2017 to 2016, interest expense increased $7.5 million, or 63%, year-over-year. Average interest-bearing liabilities increased 32% in 2017. The acquisition of CSB occurred in the third quarter of 2016, therefore 2017 was the first full year that CSB was included in the Company's financial results. Guaranty Bank, acquired in the fourth quarter of 2017, also contributed to the increase in interest expense and average interest-bearing liabilities. The Company's cost of funds increased because the Company has rate sensitive deposits that have repriced with the increase in certain market rates.

The Company's management intends to continue to shift the mix of funding from wholesale funds to core deposits, including noninterest-bearing deposits. Continuing this trend is expected to strengthen the Company's franchise value, reduce funding costs, and increase fee income opportunities through deposit service charges.

PROVISION FOR LOAN/LEASE LOSSES

The provision is established based on a number of factors, including the Company's historical loss experience, delinquencies and charge-off trends, the local and national economy and the risk associated with the loans/leases in the portfolio as described in more detail in the "Critical Accounting Policies" section.

Table of Contents

The Company's provision totaled $12.7 million for 2018, an increase of $4.2 million from 2017. Notably, RB&T's provision expense increased $3.9 million when comparing 2018 to the prior year, primarily attributable to loans to two unrelated borrowers. Additionally, the Company had strong loan growth. SFC Bank incurred $990 thousand of provision expense in 2018. As acquired loans renew, the discount associated with those loans is eliminated and the Company must establish a loan loss reserve. When comparing 2017 to 2016, the Company's provision increased by $992 thousand. In 2017, CSB incurred $2.8 million of provision expense for the full year.

The Company had an allowance of 1.07% of total gross loans/leases at December 31, 2018, compared to 1.16% of total gross loans/leases at December 31, 2017, and compared to 1.28% of total gross loans/leases at December 31, 2016. Management evaluates the allowance needed on the acquired loans factoring in the remaining discount, which was $11.6 million, $8.1 million and $10.1 million at December 31, 2018, 2017 and 2016, respectively.

The Company's allowance to total NPLs was 214.80% at December 31, 2018, which was up from 184.28% at December 31, 2017, and up from 144.85% at December 31, 2016.

The fluctuations in these ratios were the result of recent acquisitions. In accordance with GAAP for acquisition accounting, acquired loans must be recorded at fair value; therefore, no allowance was associated with these loans. As acquired loans renew, the discount associated with those loans is eliminated and the Company must establish an allowance.

NONINTEREST INCOME

The following tables set forth the various categories of noninterest income for the years ended December 31, 2018, 2017, and 2016.

	Year Ended December 31, 2018	December 31, 2017	$ Change	% Change	
Trust department fees	$ 8,707,406	$ 7,187,820	$ 1,519,586	21.1	%
Investment advisory and management fees	4,725,557	3,869,699	855,858	22.1	
Deposit service fees	6,420,237	5,919,317	500,920	8.5	
Gains on sales of residential real estate loans, net	900,744	408,655	492,089	120.4	
Gains on sales of government guaranteed portions of loans, net	404,852	1,163,741	(758,889)	(65.2)	
Swap fee income	10,787,234	3,094,939	7,692,295	248.5	
Securities gains (losses), net	—	(87,885)	87,885	(100.0)	
Earnings on bank-owned life insurance	1,631,749	1,802,443	(170,694)	(9.5)	
Debit card fees	3,262,645	2,941,703	320,942	10.9	
Correspondent banking fees	851,514	915,647	(64,133)	(7.0)	
Other	3,849,156	3,266,213	582,943	17.8	
Total noninterest income	$ 41,541,094	$ 30,482,292	$ 11,058,802	36.3	%

	Year Ended December 31, 2017	December 31, 2016	$ Change	% Change

Trust department fees	$ 7,187,820	$ 6,164,137	$ 1,023,683	16.6	%
Investment advisory and management fees	3,869,699	2,992,811	876,888	29.3	
Deposit service fees	5,919,317	4,439,455	1,479,862	33.3	
Gains on sales of residential real estate loans, net	408,655	431,313	(22,658)	(5.3)	
Gains on sales of government guaranteed portions of loans, net	1,163,741	3,159,073	(1,995,332)	(63.2)	
Swap fee income	3,094,939	1,708,204	1,386,735	81.2	
Securities gains (losses), net	(87,885)	4,592,398	(4,680,283)	(101.9)	
Earnings on bank-owned life insurance	1,802,443	1,771,396	31,047	1.8	
Debit card fees	2,941,703	1,814,488	1,127,215	62.1	
Correspondent banking fees	915,647	1,050,142	(134,495)	(12.8)	
Other	3,266,213	2,913,458	352,755	12.1	
Total noninterest income	$ 30,482,292	$ 31,036,875	$ (554,583)	(1.8)	%

In recent years, the Company has been successful in expanding its wealth management customer base. Trust department fees continue to be a significant contributor to noninterest income. With strong growth in assets under management, trust department fees increased 21% in the current year. Comparatively, trust fee income increased 17% when comparing 2017 to 2016. Income is generated primarily from fees charged based on assets under administration for corporate and personal trusts and for custodial services. The majority of the trust department fees are determined based on the value of the investments within the fully managed trusts.

Table of Contents

Management has placed a stronger emphasis on growing its investment advisory and management services. Part of this initiative has been to restructure the Company's Wealth Management Division to allow for more efficient delivery of products and services through selective additions of talent as well as leverage of and collaboration among existing resources (including the aforementioned trust department). Similar to trust department fees, fees from these services are largely determined based on the value of the investments managed. On October 1, 2018 the Company acquired the Bates Companies, headquartered in Rockford, Illinois. The acquisition enhanced the wealth management services of the Company by adding approximately $704 million of assets under management. Investment advisory and management fees increased 22% in 2018. Comparatively, investment advisory and management fees increased 29% in 2017.

Deposit service fees expanded 9% in 2018 and 33% in 2017. The increases in both years were the result of the recent acquistions. Additionally, the Company continues its emphasis on shifting the mix of deposits from brokered and retail time deposits to non-maturity demand deposits across all its markets. With this continuing shift in mix, the Company has increased the number of demand deposit accounts, which tend to be lower in interest cost and higher in service fees. The Company plans to continue this shift in mix and to further focus on growing deposit service fees.

Gains on sales of residential real estate loans, net, increased 120% in 2018, while decreasing 5% in 2017. The increase in 2018 was due to the addition of SFC Bank which recognized $532 thousand of gains on sales of residential real estate, net since it was acquired via merger on July 1, 2018. Overall, refinancing activity has slowed, as many of the Company's existing and prospective customers have already executed a refinancing. Therefore, this area has become a much smaller contributor to overall noninterest income.

The Company's gains on the sale of government-guaranteed portions of loans for 2018 decreased 65%, while decreasing 63% in the prior year. Given the nature of these gains, large fluctuations can happen from quarter-to-quarter and year-to-year. As one of its strategies, the Company continues to leverage its expertise by taking advantage of programs offered by the SBA and the USDA. In some cases, it is more beneficial for the Company to sell the government-guaranteed portion on the secondary market for a premium rather than retain the loans in the Company's portfolio. Sales activity for government-guaranteed portions of loans tends to fluctuate depending on the demand for loans that fit the criteria for the government guarantee. Further, the size of the transactions can vary and, as the gain is determined as a percentage of the guaranteed amount, the resulting gain on sale can vary. Recently, competitors have been offering SBA loan candidates traditional financing without the guarantee and the Company is not willing to relax its structure for those lending opportunities.

As a result of the interest rate environment, the Company was able to execute numerous interest rate swaps on select commercial loans, including tax credit project loans. The interest rate swaps allow the commercial borrowers to pay a fixed interest rate while the Company receives a variable interest rate as well as an upfront fee dependent upon the pricing. Management believes that these swaps help position the Company more favorably for rising rate environments. Management will continue to review opportunities to execute these swaps at all of its subsidiary banks, as the circumstances are appropriate for the borrower and the Company. An optimal interest rate swap candidate must be of a certain size and sophistication which can lead to volatility in activity from year to year. Swap fee income totaled $10.8 million in 2018, compared to $3.1 million in 2017 and $1.7 million in 2016. Future levels of swap fee income are dependent upon prevailing interest rates.

There were no securities gains or losses in the current year as compared to securities losses (net) of $88 thousand for the prior year and securities gains (net) of $4.6 million in 2016. In 2016, the Company took advantage of market opportunities by selling approximately $130.2 million of investments that were low-yielding. Proceeds were then used to purchase higher-yielding tax-exempt municipal bonds and to fund loan and lease growth. Additionally, in the third quarter of 2016, the Company sold an equity investment and recognized a gain of $4.0 million, which was then used to reduce wholesale borrowings and further de-lever the balance sheet.

Earnings on BOLI decreased 10% in 2018 and increased 2% in 2017. There were no purchases of BOLI in 2018 or 2017. Yields on BOLI (based on a simple average and excluding the impact of the federal income tax exemption) were 2.57% for 2018, 3.05% for 2017, and 3.09% for 2016. Notably, a small portion of the Company's BOLI is variable rate whereby the returns are determined by the performance of the equity market. Management intends to continue to review its BOLI investments to be consistent with policy and regulatory limits in conjunction with the rest of its earning assets in an effort to maximize returns while minimizing risk.

Debit card fees are the interchange fees paid on certain debit card customer transactions. Debit card fees increased 11% in 2018, compared to a 62% increase in the prior year. The primary reason for the increase in both years was the recent

Table of Contents

acquisitions. These fees can vary based on customer debit card usage, so fluctuations from period to period may occur. As an opportunity to maximize fees, the Company offers a deposit product with a higher interest rate that incentivizes debit card activity.

Correspondent banking fees decreased 7% in 2018 and decreased 13% in 2017. Management will continue to evaluate earnings credit rates and the resulting impact on deposit balances and fees while balancing the ability to grow market share. Correspondent banking continues to be a core strategy for the Company, as this line of business provides a high level of noninterest bearing deposits that can be used to fund loan growth as well as a steady source of fee income. The Company now serves 190 banks in Iowa, Illinois and Wisconsin.

Other noninterest income increased 18% in 2018 and 12% in 2017. The primary reason for the increase was driven by fluctuations in net gains recognized on the disposal of leased assets.

NONINTEREST EXPENSES

The following tables set forth the various categories of noninterest expenses for the years ended December 31, 2018, 2017, and 2016.

	Year Ended December 31, 2018	December 31, 2017	$ Change	% Change	
Salaries and employee benefits	$ 68,994,218	$ 55,722,288	$ 13,271,930	23.8	%
Occupancy and equipment expense	12,883,632	10,938,037	1,945,595	17.8	
Professional and data processing fees	11,452,084	10,757,057	695,027	6.5	
Acquisition costs	1,795,119	1,068,918	726,201	67.9	
Post-acquisition compensation, transition and integration costs	2,086,386	4,309,565	(2,223,179)	(51.6)	
FDIC insurance, other insurance and regulatory fees	3,594,480	2,752,270	842,210	30.6	
Loan/lease expense	1,543,343	1,163,708	379,635	32.6	
Net cost and gains/losses on operations of other real estate	2,488,730	1,599	2,487,131	155,542.9	
Advertising and marketing	3,551,822	2,624,951	926,871	35.3	
Bank service charges	1,837,626	1,770,942	66,684	3.8	
Correspondent banking expense	820,905	807,077	13,828	1.7	
CDI amortization expense	1,692,431	1,000,561	691,870	69.1	
Other	6,402,643	4,507,724	1,894,919	42.0	
Total noninterest expense	$ 119,143,419	$ 97,424,697	$ 21,718,722	22.3	%

	Year Ended December 31, 2017	December 31, 2016	$ Change	% Change	
Salaries and employee benefits	$ 55,722,288	$ 46,317,060	$ 9,405,228	20.3	%
Occupancy and equipment expense	10,938,037	8,404,605	2,533,432	30.1	
Professional and data processing fees	10,757,057	7,113,443	3,643,614	51.2	
Acquisition costs	1,068,918	1,400,004	(331,086)	(23.6)	

Post-acquisition compensation, transition and integration costs	4,309,565	1,041,169	3,268,396	313.9	
FDIC insurance, other insurance and regulatory fees	2,752,270	2,549,314	202,956	8.0	
Loan/lease expense	1,163,708	662,299	501,409	75.7	
Net cost and gains/losses on operations of other real estate	1,599	591,303	(589,704)	(99.7)	
Advertising and marketing	2,624,951	2,127,566	497,385	23.4	
Bank service charges	1,770,942	1,692,957	77,985	4.6	
Losses on debt extinguishment, net	—	4,577,668	(4,577,668)	(100.0)	
Correspondent banking expense	807,077	750,646	56,431	7.5	
CDI amortization	1,000,561	442,850	557,711	125.9	
Other	4,507,724	3,815,028	692,696	18.2	
Total noninterest expense	$ 97,424,697	$ 81,485,912	$ 15,938,785	19.6	%

Management places strong emphasis on overall cost containment and is committed to improving the Company's general efficiency. One-time charges relating to acquisitions impacted expense in 2018, 2017 and 2016.

Salaries and employee benefits, which is the largest component of noninterest expense, increased 24% and 20% in 2018 and 2017, respectively. This increase was primarily related to the recent acquisitions, new hires and merit increases. To help support recent and expected growth the Company is adding to its operational infrastructure and investing in additional staffing both at the corporate level and at some of its bank charters. Some of these hires are opportunistic, as the Company

Table of Contents

takes advantages of talent availability in the marketplace as a result of ongoing industry consolidation. Incentives and commissions increased, driven by higher swap fee income in 2018.

Occupancy and equipment expense increased 18% in 2018 and increased 30% in 2017. These increases were largely due to the addition of Guaranty Bank late in 2017 and the addition of SFC Bank in the third quarter of 2018.

Professional and data processing fees increased 7% in 2018 and increased 51% in 2017. This increased expense was mostly due to the additions of the Bates Companies, SFC Bank and Guaranty Bank. Legal expense was elevated due to a legal matter at RBT where two employees have been charged with wrongdoing in connection with an SBA loan application. The Company anticipates these legal expenses will continue until the court proceedings are completed, which the Company expects to be sometime in late 2019. Neither RB&T, nor the Company, have been charged in the case. Generally, professional and data processing fees can fluctuate depending on certain one-time project costs. Management will continue to focus on minimizing such one-time costs and driving recurring costs down through contract negotiation or managed reduction in activity where costs are determined on a usage basis.

Acquisition costs totaled $1.8 million and $1.1 million for 2018 and 2017, respectively. These costs were comprised primarily of legal, accounting and investment banking costs related to the acquisitions described in Note 2 to the Consolidated Financial Statements.

Post-acquisition compensation, transition and integration costs totaled $2.1 million and $4.3 million for 2018 and 2017, respectively. These costs were comprised primarily of personnel costs, IT integration, and conversion costs related to the acquisitions described in Note 2 to the Consolidated Financial Statements. There was a one-time contract termination fee related to a data processing software conversion at CSB that accounted for the increased cost in 2017.

FDIC insurance, other insurance and regulatory fee expense increased 31% in 2018 and increased 8% in 2017. The increase in expense was due to recent acquisitions.

Loan/lease expense increased 33% in 2018 and increased 76% in 2017. Generally, loan/lease expense has a direct relationship with the level of NPLs; however, it may deviate depending upon the individual NPLs.

Net cost and gains/losses on operations of other real estate includes gains/losses on the sale of OREO, write-downs of OREO and all income/expenses associated with OREO. Net costs of operations totaled $2.5 million for 2018 and $2 thousand for 2017. The increase in 2018 is due primarily to a $2.0 million write-down of one OREO property and the loss on sale of another OREO property totaling $424 thousand.

Advertising and marketing expense increased 35% in 2018 and increased 23% in 2017. The increase in expense was primarily due to the additions of SFC Bank and Guaranty Bank.

Bank service charges, a large portion of which include indirect costs incurred to provide services to QCBT’s correspondent banking customer portfolio, increased over the past two years (4% in 2018 and 5% in 2017). As transaction volumes continue to increase and the number of correspondent banking clients increases, the associated expenses will also increase.

In 2016, the Company incurred $4.6 million in losses on debt extinguishment (net). These losses relate to the prepayment of certain FHLB advances and wholesale structured repurchase agreements. Additionally, the Company recognized gains on extinguishment related to the repurchase of junior subordinated debentures that were acquired at a discount through auction.

Correspondent banking expense increased 2% in 2018 and 8% in 2017. These are direct costs incurred to provide services to QCBT's correspondent banking customer portfolio, including safekeeping and cash management services. The increases in both years were due, in large part, to the success QCBT has had in growing its correspondent banking customer portfolio.

Core deposit intangible amortization expense increased 69% in 2018 and 126% in 2017. Increases were due to the additions of SFC Bank and Guaranty Bank.

Other noninterest expense increased 42% in 2018 and 18% in 2017. Included in other noninterest expense are items such as subscriptions, sales and use tax and expenses related to wealth management. The majority of this increase is also related to the additions of SFC Bank and Guaranty Bank.

Table of Contents

INCOME TAX EXPENSE

The provision for income taxes was $9.0 million for 2018, or an effective tax rate of 17.3%, compared to $4.9 million for 2017, or an effective tax rate of 12.2%, and compared to $8.9 million for 2016, or an effective tax rate of 24.3%. The effective tax rate for 2017 was significantly impacted by a $2.9 million income tax benefit for the re-valuation of deferred taxes at the lower federal income tax rate as a result of the Tax Act. See Note 13 to the Consolidated Financial Statements for additional information regarding the impact of Tax Act on deferred tax assets and income tax.

Refer to the reconciliation of the expected income tax rate to the effective tax rate that is included in Note 13 to the Consolidated Financial Statements for additional details.

FINANCIAL CONDITION, AS OF THE YEARS ENDED DECEMBER 31, 2018 AND 2017

OVERVIEW

Following is a table that represents the major categories of the Company’s balance sheet.

	As of December 31, 2018 (dollars in thousands)		2017	
	Amount	%	Amount	%
Cash , federal funds sold, and interest-bearing deposits	$ 245,119	5 %	$ 161,684	4 %
Securities	662,969	13 %	652,382	16 %
Net loans/leases	3,692,907	75 %	2,930,130	74 %
Other assets	348,715	7 %	238,469	6 %
Total assets	$ 4,949,710	100 %	$ 3,982,665	100 %
Total deposits	$ 3,977,031	80 %	$ 3,266,655	82 %
Total borrowings	404,969	8 %	309,480	8 %
Other liabilities	94,572	2 %	53,243	1 %
Total stockholders' equity	473,138	10 %	353,287	9 %
Total liabilities and stockholders' equity	$ 4,949,710	100 %	$ 3,982,665	100 %

In 2018, total assets grew $967.0 million, or 24%. This included $578.9 million in assets acquired and new goodwill of $49.7 million as part of the Bates Companies acquisition and merger with Springfield Bancshares (further described in Note 2 to the Consolidated Financial Statements). The Company organically grew its net loan/lease portfolio $285.4 million, which was primarily funded by deposit growth. Deposits grew $270.8 million, or 8% during 2018, excluding the $439.6 million of deposits assumed in the Springfield Bancshares merger. Borrowings increased $10.3 million, or 3% during 2018, excluding the $85.2 million of borrowings assumed in the Springfield Bancshares merger.

In 2017, total assets grew $680.7 million, or 21%. This included $259.6 million in assets acquired and new goodwill of $15.2 million as part of the Guaranty Bank acquisition (further described in Note 2 to the Consolidated Financial Statements). The Company organically grew its net loan/lease portfolio $362.9 million, which was primarily funded by deposit growth. Deposits grew $384.9 million, or 14% during 2017, excluding the $212.5 million of deposits acquired. Borrowings decreased $2.5 million, or 1% during 2017, excluding the $21.1 million of borrowings acquired.

INVESTMENT SECURITIES

The composition of the Company’s securities portfolio is managed to meet liquidity needs while prioritizing the impact on interest rate risk and maximizing return, while minimizing credit risk. The Company has further diversified the portfolio by decreasing U.S government sponsored agency securities, while increasing residential mortgage-backed and related securities and tax-exempt municipal securities. Of the latter, the large majority are privately placed tax-exempt debt issuances by municipalities located in the Midwest (with some in or near the Company’s existing markets) and require a thorough underwriting process before investment.

Following is a breakdown of the Company’s securities portfolio by type, the percentage of net unrealized losses to carrying value on the total portfolio, and the portfolio duration as of December 31, 2018, 2017, and 2016.

Table of Contents

	2018		2017		2016	
	Amount	%	Amount	%	Amount	%
	(dollars in thousands)					
U.S. govt. sponsored agency securities	$ 36,411	5 %	$ 38,097	6 %	$ 46,084	8 %
Municipal securities	459,409	70 %	445,049	68 %	374,463	65 %
Residential mortgage-backed and related securities	159,249	24 %	163,301	25 %	147,702	26 %
Other securities	7,900	1 %	5,935	1 %	5,773	1 %
	$ 662,969	100 %	$ 652,382	100 %	$ 574,022	100 %
Securities as a % of Total Assets	13.39 %		16.38 %		17.38 %	
Net Unrealized Losses as a % of Amortized Cost	(1.01) %		(0.13) %		(0.87) %	
Duration (in years)	6.8		7.0		6.0	
Yield on investment securities (tax equivalent)	3.58 %		3.80 %		3.56 %	
Yield on investment securities (GAAP)	2.85 %		2.47 %		2.31 %	

Management monitors the level of unrealized gains/losses including performing quarterly reviews of individual securities for evidence of OTTI. Management identified no OTTI in 2018, 2017 or 2016.

In 2017, the duration of the securities portfolio increased due, in large part, to the continued shift in mix. Duration was extended from the strong growth in longer term fixed rate municipal securities.

The Company has not invested in non-agency commercial or residential mortgage-backed securities or pooled trust preferred securities.

See Note 3 to the Consolidated Financial Statements for additional information regarding the Company’s investment securities.

LOANS/LEASES

The Company’s loan/lease portfolio grew organically $290.9 million, or 9.8%, during 2018. The remaining growth in the loan/lease portfolio was related to the merger with Springfield Bancshares (further described in Note 2 to the Consolidated Financial Statements). Notably, C&I loans increased $294.9 million, or 26% and CRE loans grew $462.6 million, or 35%.

The Company’s loan/lease portfolio grew organically $366.5 million, or 15%, during 2017. The remaining growth in the loan/lease portfolio was related to the acquisition of Guaranty Bank (further described in Note 2 to the Consolidated Financial Statements). Notably, C&I loans increased $306.9 million, or 37% and CRE loans grew $210.0 million, or 19%.

The mix of loan/lease types within the Company's loan/lease portfolio is presented in the following table.

	As of December 31,									
	2018		2017		2016		2015		2014	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
	(dollars in thousands)									
oans	$ 1,429,410	38 %	$ 1,134,516	38 %	$ 827,637	34 %	$ 648,160	36 %	$ 523,927	3
oans	1,766,111	48 %	1,303,492	44 %	1,093,459	46 %	724,369	41 %	702,140	4
ng	117,969	3 %	141,448	5 %	165,419	7 %	173,656	10 %	166,032	1
ntial tate	290,759	8 %	258,646	9 %	229,233	10 %	170,433	9 %	158,633	1
ment ner ner	119,381	3 %	118,611	4 %	81,666	3 %	73,669	4 %	72,607	
eases	$ 3,723,630	100 %	$ 2,956,713	100 %	$ 2,397,414	100 %	$ 1,790,287	100 %	$ 1,623,339	1
ed ase tion net of	9,124		7,773		8,073		7,736		6,664	
nce	(39,847)		(34,356)		(30,757)		(26,141)		(23,074)	
eases	$ 3,692,907		$ 2,930,130		$ 2,374,730		$ 1,771,882		$ 1,606,929	

Historically, the Company structures most residential real estate loans to conform to the underwriting requirements of Freddie Mac and Fannie Mae to allow the subsidiary banks to resell the loans on the secondary market to avoid the interest rate risk associated with longer term fixed rate loans and recognizing noninterest income from the gain on sale. Loans originated for this purpose were classified as held for sale and are included in the residential real estate loans in the table above. Historically, the subsidiary banks structure most loans that will not conform to those underwriting requirements as

Table of Contents

adjustable rate mortgages that mature or adjust in one to five years, and then retain these loans in their portfolios. The Company holds a limited amount of 15 year fixed rate residential real estate loans originated in prior years that met certain credit guidelines. In addition, the Company has not originated any subprime, Alt-A, no documentation, or stated income residential real estate loans throughout its history.

The following tables set forth the remaining maturities by loan/lease type as of December 31, 2018 and 2017. Maturities are based on contractual dates.

	As of December 31, 2018				
				Maturities After One Year	
	Due in one year or less	Due after one through 5 years	Due after 5 years	Predetermined interest rates	Adjustable interest rates
	(dollars in thousands)				
C&I loans	$ 567,593	$ 465,514	$ 396,303	$ 583,819	277,998
CRE loans	275,540	1,010,093	480,478	1,054,286	436,285
Direct financing leases	7,897	104,318	5,753	110,071	—
Residential real estate loans	10,430	23,373	256,956	207,344	72,985
Installment and other consumer loans	21,652	59,760	37,970	47,067	50,663
	$ 883,112	$ 1,663,058	$ 1,177,460	$ 2,002,587	$ 837,931
Percentage of total loans/leases	24 %	45 %	31 %	71 %	29 %

	As of December 31, 2017				
				Maturities After One Year	
	Due in one year or less	Due after one through 5 years	Due after 5 years	Predetermined interest rates	Adjustable interest rates
	(dollars in thousands)				
C&I loans	$ 378,849	$ 427,347	$ 328,320	$ 505,345	$ 250,322
CRE loans	225,712	715,661	362,119	734,844	342,936
Direct financing leases	8,504	127,853	5,091	132,944	—
Residential real estate loans	6,793	7,546	244,307	184,284	67,569
Installment and other consumer loans	28,908	54,565	35,138	43,817	45,886
	$ 648,766	$ 1,332,972	$ 974,975	$ 1,601,234	$ 706,713
Percentage of total loans/leases	22 %	45 %	33 %	69 %	31 %

As CRE loans have historically been the Company's largest portfolio segment, management places a strong emphasis on monitoring the composition of the Company's CRE loan portfolio. For example, management tracks the level of owner-occupied CRE loans relative to non owner-occupied loans. Owner-occupied loans are generally considered to have less risk. As of December 31, 2018 and 2017, respectively, approximately 28% and 26% of the CRE loan

portfolio was owner-occupied. The increase in this percentage in 2018 was mostly due to the addition of SFC Bank, which had a slightly higher owner-occupied percentage as compared to the legacy charters. SFC Bank's percentage of owner-occupied loans was 30% of their CRE portfolio.

Over the past several years, the Company has been successful in shifting the mix of its commercial loan portfolio by adding more C&I loans. C&I loans grew $294.9 million, or 26% over the past twelve months. A portion of this growth was attributable to the merger with Springfield Bancshares and the acquisition of Guaranty Bank, which had $95.8 million and $44.7 million of C&I loans at acquisition, respectively.

A syndicated loan is a commercial loan provided by a group of lenders and is structured, arranged and administered by one or several commercial or investment banks known as arrangers. The nationally syndicated loans invested in by the Company consist of fully funded, highly liquid term loans for which there is a liquid secondary market. The amount of nationally syndicated loans totaled $40.8 million and $51.2 million as of December 31, 2018 and 2017, respectively.

The Company also has several loans that are syndicated to borrowers in our existing markets or purchased from peer banks that we have a relationship with. These loans were immaterial as of December 31, 2018 and 2017.

See Note 4 to the Consolidated Financial Statements for additional information on the Company's loan/lease portfolio.

Table of Contents

ALLOWANCE FOR ESTIMATED LOSSES ON LOANS/LEASES

The allowance totaled $39.8 million at December 31, 2018, which was an increase of $5.5 million, or 16%, from $34.4 million at December 31, 2017. Provision totaled $12.7 million for 2018 and outpaced net charge-offs of $7.2 million (or 21 basis points of average loans/leases outstanding).

The allowance totaled $34.4 million at December 31, 2017, which was an increase of $3.6 million, or 12%, from $30.8 million at December 31, 2016. Provision totaled $8.5 million for 2017 and outpaced net charge-offs of $4.9 million (or 19 basis points of average loans/leases outstanding).

The increase in allowance in both 2018 and 2017 was primarily due to a combination of general allocations related to loan growth, as well as changes in qualitative and quantitative factors. Additionally, a portion of the increase in both years was due to the recent acquisitions. Although purchase accounting eliminates the allowance at acquisition, as acquired loans refinance and new loans are originated, an allowance must be established.

The following table summarizes the activity in the allowance.

	Year ended December 31,				
	2018	2017	2016	2015	2014
	(dollars in thousands)				
Average amount of loans/leases outstanding, before allowance	$ 3,352,357	$ 2,611,888	$ 2,042,555	$ 1,707,523	$ 1,540,382
Allowance:					
Balance, beginning of fiscal year	$ 34,356	$ 30,757	$ 26,141	$ 23,074	$ 21,448
Charge-offs:					
C&I	(5,359)	(1,150)	(527)	(454)	(1,476)
CRE	(387)	(1,795)	(24)	(2,560)	(2,756)
Direct financing leases	(2,002)	(2,285)	(2,503)	(1,789)	(1,504)
Residential real estate	(127)	(102)	(77)	(170)	(131)
Installment and other consumer	(44)	(41)	(113)	(252)	(269)
Subtotal charge-offs	(7,919)	(5,373)	(3,244)	(5,225)	(6,136)
Recoveries:					
C&I	295	191	109	634	363
CRE	50	43	33	502	418
Direct financing leases	344	186	93	136	68
Residential real estate	23	29	1	4	10
Installment and other consumer	40	53	146	145	96
Subtotal recoveries	752	502	382	1,421	955
Net charge-offs	(7,167)	(4,871)	(2,862)	(3,804)	(5,181)
	12,658	8,470	7,478	6,871	6,807

Provision charged to expense										
Balance, end of fiscal year	$ 39,847		$ 34,356		$ 30,757		$ 26,141		$ 23,074	
Net charge-offs to average loans/leases outstanding	0.21	%	0.19	%	0.14	%	0.22	%	0.34	%

The adequacy of the allowance was determined by management based on factors that included the overall composition of the loan/lease portfolio, types of loans/leases, historical loss experience, loan/lease delinquencies, potential substandard and doubtful credits, economic conditions, collateral positions, government guarantees and other factors that, in management's judgment, deserved evaluation. To ensure that an adequate allowance was maintained, provisions were made based on the increase/decrease in loans/leases and a detailed analysis of the loan/lease portfolio. The loan/lease portfolio was reviewed and analyzed quarterly with specific detailed reviews completed on all credits risk-rated less than "fair quality" and carrying aggregate exposure in excess of $250 thousand. The adequacy of the allowance was monitored by the credit administration staff and reported to management and the board of directors.

Table of Contents

The following is a table that reports the historical trends of criticized and classified loan totals as of December 31, 2018, 2017 and 2016.

Internally Assigned Risk Rating *	As of December 31, 2018	2017	2016
	(dollars in thousands)		
Special Mention (Rating 6)	$ 42,058	$ 31,024	$ 20,082
Substandard (Rating 7)	28,593	43,435	49,035
Doubtful (Rating 8)	—	271	—
	$ 70,651	$ 74,730	$ 69,117
Criticized Loans **	$ 70,651	$ 74,730	$ 69,117
Classified Loans ***	$ 28,593	$ 43,706	$ 49,035

* Amounts above exclude the government guaranteed portion, if any. The Company assigns internal risk ratings of Pass (Rating 2) for the government guaranteed portion.

** Criticized loans are defined as C&I and CRE loans with internally assigned risk ratings of 6, 7, or 8, regardless of performance.

*** Classified loans are defined as C&I and CRE loans with internally assigned risk ratings of 7 or 8, regardless of performance.

Criticized loans decreased 5% in 2018 and increased 8% in 2017. Classified loans decreased 35% in 2018 and 11% in 2017. Notably, the Company merged SFC Bank in the third quarter of 2018 and SFC Bank had no criticized or classified loans.

NPLs (consisting of nonaccrual loans/leases, accruing loans/leases past due 90 days or more, and accruing TDRs) decreased $92 thousand, or 1%, during 2018. NPLs decreased $2.6 million, or 12%, during 2017. See the table in the following section for further detail on NPLs and NPAs.

In 2018 and 2017, allowance as a percentage of gross loans/leases decreased due to the acquisitions of SFC Bank and Guaranty Bank. In accordance with GAAP for acquisition accounting, acquired loans were recorded at fair value; therefore, there was no allowance associated with these loans at acquisition. Management continues to evaluate the allowance needed on the acquired loans factoring in the net remaining discount ($11.6 million, $8.1 million and $10.1 million at December 31, 2018, 2017 and 2016, respectively).

The following table summarizes the trend in allowance as a percentage of gross loans/leases and as a percentage of NPLs as of December 31, 2018, 2017, and 2016.

	As of December 31, 2018	2017	2016
Allowance / Gross Loans/Leases	1.07 %	1.16 %	1.28 %
Allowance / NPLs	214.80 %	184.28 %	144.85 %

The following table presents the allowance by type and the percentage of loan/lease type to total loans/leases.

	As of December 31, 2018		2017		2016		2015		2014	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
	(dollars in thousands)									
C&I loans	16,420	38 %	14,323	38 %	12,545	34 %	10,484	36 %	8,834	32 %
CRE loans	17,719	48 %	13,963	44 %	11,671	46 %	9,375	41 %	8,353	43 %
Direct financing leases	1,792	3 %	2,382	5 %	3,112	7 %	3,395	10 %	3,359	10 %
Residential real estate loans	2,557	8 %	2,466	9 %	2,342	10 %	1,790	9 %	1,526	10 %
Installment and other consumer loans	1,359	3 %	1,222	4 %	1,087	3 %	1,097	4 %	1,002	5 %
	$ 39,847	100 %	$ 34,356	100 %	$ 30,757	100 %	$ 26,141	100 %	$ 23,074	100 %

%Represents the percentage of the certain type of loan/lease to total loans/leases

Table of Contents

Although management believes that the allowance at December 31, 2018 is at a level adequate to absorb probable losses on existing loans/leases, there can be no assurance that such losses will not exceed the estimated amounts or that the Company will not be required to make additional provisions for loan/lease losses in the future. Unpredictable future events could adversely affect cash flows for both commercial and individual borrowers, which could cause the Company to experience increases in problem assets, delinquencies and losses on loans/leases, and require additional increases in the provision. Asset quality is a priority for the Company and its subsidiaries. The ability to grow profitably is in part dependent upon the ability to maintain that quality. The Company continually focuses efforts at its subsidiary banks and its leasing company with the intention to improve the overall quality of the Company's loan/lease portfolio.

See Note 4 to the Consolidated Financial Statements for additional information on the Company's allowance.

NONPERFORMING ASSETS

The table below presents the amounts of NPAs.

	As of December 31,				
	2018	2017	2016	2015	2014
	(dollars in thousands)				
Nonaccrual loans/leases (1) (2)	$ 14,260	$ 11,441	$ 13,919	$ 10,648	$ 18,588
Accruing loans/leases past due 90 days or more (3)	632	89	967	3	93
TDRs - accruing	3,659	7,113	6,347	1,054	1,421
Total NPLs	18,551	18,643	21,233	11,705	20,102
OREO	9,378	13,558	5,523	7,151	12,768
Other repossessed assets	8	80	202	246	155
Total NPAs	$ 27,937	$ 32,281	$ 26,958	$ 19,102	$ 33,025
NPLs to total loans/leases	0.50 %	0.63 %	0.88 %	0.65 %	1.23 %
NPAs to total loans/leases plus repossessed property	0.75 %	1.08 %	1.12 %	1.06 %	2.01 %
NPAs to total assets	0.56 %	0.81 %	0.82 %	0.74 %	1.31 %

(1) Includes government guaranteed portions of loans, if applicable.
(2) Includes TDRs of $2.3 million at December 31, 2018, $2.3 million at December 31, 2017, $2.3 million at December 31, 2016, $1.5 million at December 31, 2015, and $5.0 million at December 31, 2014.
(3) Includes TDRs of $496 thousand at December 31, 2018.

The large majority of the Company's NPAs consists of nonaccrual loans/leases, accruing TDRs and OREO. For nonaccrual loans/leases, management thoroughly reviewed these loans/leases and provided specific allowances as appropriate. OREO is carried at the lower of carrying amount or fair value less costs to sell.

The policy of the Company is to place a loan/lease on nonaccrual status if: (a) payment in full of interest or principal is not expected; or (b) principal or interest has been in default for a period of 90 days or more unless the obligation is both in the process of collection and well secured. A loan/lease is well secured if it is secured by collateral with sufficient market value to repay principal and all accrued interest. A debt is in the process of collection if collection of the debt is proceeding in due course either through legal action, including judgment enforcement procedures, or in appropriate circumstances, through collection efforts not involving legal action which are reasonably expected to

result in repayment of the debt or in its restoration to current status.

In 2018, the Company's NPAs decreased $4.3 million, or 13%. OREO decreased $4.2 million primarily due to the $2.0 million writedown of one large OREO property and the sale of a $1.3 million OREO property (including a loss on sale of $424 thousand). In the fourth quarter of 2018, there was a $3.5 million paydown on a large nonaccrual loan.

In 2017, the Company's NPAs increased $5.3 million, or 20%. OREO increased $8.0 million primarily due to the addition of one large non owner-occupied CRE relationship.

The Company's lending/leasing practices remain unchanged and asset quality remains a top priority for management.

Table of Contents

DEPOSITS

Deposits grew $710.4 million during 2018 (including $270.8 million of organic growth and $439.6 million of deposits assumed through the merger with Springfield Bancshares). For 2017, deposits grew $597.3 million (including $384.9 million of organic growth and $212.5 million of deposits acquired through the purchase of Guaranty Bank). The table below presents the composition of the Company's deposit portfolio.

	As of December 31,								
	2018			2017			2016		
	Amount	%		Amount	%		Amount	%	
	(dollars in thousands)								
Noninterest bearing demand deposits	$ 791,101	20	%	$ 789,548	24	%	$ 797,415	30	%
Interest bearing demand deposits*	2,204,206	55	%	1,855,893	57	%	1,369,226	51	%
Time deposits	704,903	18	%	516,058	16	%	439,169	17	%
Brokered deposits	276,821	7	%	105,156	3	%	63,451	2	%
	$ 3,977,031	100	%	$ 3,266,655	100	%	$ 2,669,261	100	%

* Includes brokered money market balances of $7.0 million, $25.1 million and $22.0 million as of December 31, 2018, 2017 and 2016, respectively.

The Company has been successful in growing its noninterest-bearing deposit portfolio over the past several years, growing average balances 4% in 2018 and 7% in 2017. Year-end balances can fluctuate a great deal due to large customer and correspondent bank activity. Trends have shown that this fluctuation is generally temporary.

Management will continue to focus on growing its core deposit portfolio, including its correspondent banking business at QCBT, as well as shifting the mix from brokered and other higher cost deposits to lower cost core deposits. With the significant success achieved by QCBT in growing its correspondent banking business, QCBT has developed procedures to proactively monitor this industry concentration of deposits and loans. Other deposit-related industry concentrations and large accounts are monitored by the internal asset liability management committee. See discussion regarding policy limits on bank stock loans in the Lending/Leasing section under Item 1 – Business in Part I of this Form 10 K.

SHORT-TERM BORROWINGS

The subsidiary banks purchase federal funds for short-term funding needs from the FRB, or from their correspondent banks. The table below presents the composition of the Company's short-term borrowings.

	As of, December 31,		
	2018	2017	2016
	(dollars in thousands)		
Overnight repurchase agreements	$ 2,084	$ 7,003	$ 8,131
Federal funds purchased	26,690	6,990	31,840
	$ 28,774	$ 13,993	$ 39,971

In 2016, the Company shifted overnight customer repurchase agreement funds to insured deposit products which do not require collateral, helping to free up additional liquidity for the Company. This also allowed the Company to further execute on the strategy of rotating out of investment securities into loans and leases.

Regarding the Company's federal funds purchased, this fluctuates based on the short-term funding needs of the Company's subsidiary banks. See Note 9 to the Consolidated Financial Statements for additional information on the Company's short-term borrowings.

FHLB ADVANCES AND OTHER BORROWINGS

As a result of their memberships in the FHLB of Des Moines and Chicago, the subsidiary banks have the ability to borrow funds for short-term or long-term purposes under a variety of programs. The subsidiary banks can utilize FHLB advances for loan matching as a hedge against the possibility of rising interest rates or when these advances provide a less costly source of funds than customer deposits. For 2018, FHLB advances increased $74.5 million, or 39%, due to the merger with Springfield Bancshares and strong loan and lease growth, which outpaced the Company's deposit growth. See Note 10 of the Consolidated Financial Statements for additional details. For 2017, FHLB advances increased $54.5 million, or 40%, due to the timing of strong loan and lease growth which temporarily outpaced the Company's deposit growth. The

Table of Contents

FHLB advance increases were overnight advances. There were no increases in term advances. See Note 10 of the Consolidated Financial Statements for additional details.

	As of December 31,		
	2018	2017	2016
	(dollars in thousands)		
Amount Due	$ 266,492	$ 192,000	$ 137,500
Weighted Average Interest Rate at Year-End	2.55 %	1.82 %	1.25 %

Other borrowings consist largely of wholesale structured repurchase agreements which the subsidiary banks historically utilized as an alternative funding source to FHLB advances and customer deposits. The table below presents the composition of the Company's other borrowings.

	As of, December 31,		
	2018	2017	2016
	(dollars in thousands)		
Wholesale structured repurchase agreements	$ 35,000	$ 35,000	$ 45,000
Term notes	23,250	31,000	30,000
Subordinated debentures	4,782	—	—
Revolving line of credit	9,000	—	5,000
	$ 72,032	$ 66,000	$ 80,000

During 2018 the Company assumed $9.5 million of other borrowings in the Springfield Bancshares merger. Excluding the merger impact, other borrowings decreased $3.5 million. The term notes and revolving line of credit have been used to fund acquisitions as described in Note 2 to the Consolidated Financial Statements. In 2017, other borrowings decreased $14 million with the paydown of $5.0 million revolving line of credit and the maturity of $9.0 million wholesale structured repurchase agreement.

See Notes 10 and 11 to the Consolidated Financial Statements for additional information regarding FHLB advances, and other borrowings.

It is management's intention to continue to reduce its reliance on wholesale funding, including FHLB advances, wholesale structured repurchase agreements, and brokered deposits. Replacement of this funding with core deposits helps to reduce interest expense as the wholesale funding tends to be higher cost. However, the Company may choose to utilize wholesale funding sources to supplement funding needs, as this is a way for the Company to effectively and efficiently manage interest rate risk.

STOCKHOLDERS' EQUITY

The table below presents the composition of the Company's stockholders' equity.

	As of December 31,		
	2018	2017	2016
	(dollars in thousands)		
Common stock	$ 15,718	$ 13,918	$ 13,107
Additional paid in capital	270,761	189,078	156,777
Retained earnings	192,203	151,962	118,617
AOCI (loss)	(5,544)	(1,671)	(2,460)
Total stockholders' equity	$ 473,138	$ 353,287	$ 286,041
TCE / TA ratio (non-GAAP)	7.78 %	8.01 %	8.04 %

* TCE/TA ratio is a non-GAAP measure. Refer to the GAAP to Non-GAAP Reconciliations section of this report for more information.

Table of Contents

As of December 31, 2018, 2017 and 2016, no preferred stock was outstanding.

In connection with the merger with Springfield Bancshares in the third quarter of 2018, the Company issued 1,699,414 shares of its common stock at a price of $47.45 per share. This issuance modestly increased common stock and additional paid in capital in comparison to the prior year. Refer to Note 2 of the Consolidated Financial Statements for additional information.

In connection with the acquisition of Guaranty Bank in the fourth quarter of 2017, the Company issued 678,670 shares of its common stock at a price of $45.50 per share. This issuance significantly increased common stock and additional paid in capital in comparison to the prior year. Refer to Note 2 of the Consolidated Financial Statements for additional information.

In the third quarter of 2016, the Company sold 1,215,000 shares of its common stock at a price of $24.75 per share, for net proceeds of $29.8 million, after deducting expenses, to help fund the acquisition of CSB. This offering significantly increased common stock and additional paid in capital in comparison to the prior year. Refer to Note 2 of the Consolidated Financial Statements for additional information.

The following table presents the rollforward of stockholders' equity for the years ended December 31, 2018 and 2017, respectively.

	For the Year Ended December 31,	
	2018	2017
	(dollars in thousands)	
Beginning balance	$ 353,287	$ 286,041
Net income	43,120	35,707
Other comprehensive income (loss), net of tax	(3,205)	1,093
Common cash dividends declared	(3,546)	(2,665)
Proceeds from issuance of 678,670 shares of common stock, net of costs	—	30,741
Proceeds from issuance of 23,501 shares of common stock	1,000	—
Proceeds from issuance of 1,699,414 shares of common stock, net of costs	80,531	—
Other *	1,951	2,370
Ending balance	$ 473,138	$ 353,287

* Includes mostly common stock issued for options exercised and the employee stock purchase plans, as well as stock-based compensation.

LIQUIDITY AND CAPITAL RESOURCES

Liquidity measures the ability of the Company to meet maturing obligations and its existing commitments, to withstand fluctuations in deposit levels, to fund its operations, and to provide for customers' credit needs. The Company monitors liquidity risk through contingency planning stress testing on a regular basis. The Company seeks to avoid over concentration of funding sources and to establish and maintain contingent funding facilities that can be drawn upon if normal funding sources become unavailable. One source of liquidity is cash and short-term assets, such as interest-bearing deposits in other banks and federal funds sold, which averaged $159.7 million during 2018, $164.0 million during 2017 and $139.5 million during 2016. The Company's on balance sheet liquidity position can fluctuate

based on short-term activity in deposits and loans.

The subsidiary banks have a variety of sources of short-term liquidity available to them, including federal funds purchased from correspondent banks, FHLB advances, structured repos, brokered deposits, lines of credit, borrowing at the Federal Reserve Discount Window, sales of securities available for sale, and loan/lease participations or sales. The Company also generates liquidity from the regular principal payments and prepayments made on its loan/lease portfolio, and on the regular principal payments on its securities portfolio.

At December 31, 2018, the subsidiary banks had 33 lines of credit totaling $363.7 million, of which $1.7 million was secured and $362.0 million was unsecured. At December 31, 2018, $343.7 million of the $363.7 million was available.

At December 31, 2017, the subsidiary banks had 34 lines of credit totaling $375.0 million, of which $3.0 million was secured and $372.0 million was unsecured. At December 31, 2017, the full $375.0 million was available.

Table of Contents

The Company maintains a $10.0 million secured revolving credit note with a variable interest rate and a maturity of June 30, 2019. At December 31, 2018, $1.0 million was available. See Note 11 to the Consolidated Financial Statements for additional information.

Investing activities used cash of $333.7 million during 2018 compared to $410.5 million during 2017, and $169.0 million during 2016. Proceeds from calls, maturities, pay downs, and sales of securities were $70.2 million for 2018 compared to $152.6 million for 2017, and $285.2 million for 2016. Purchases of securities used cash of $84.0 million for 2018 compared to $179.8 million for 2017, and $179.6 million for 2016. The net increase in loans/leases used cash of $292.7 million for 2018 compared to $375.2 million for 2017, and $187.5 million for 2016. The Company paid net cash of $5.2 million related to the acquisition of the Bates Companies and merger with Springfield Bancshares for 2018 and paid net cash of and $3.4 million related to the acquisition of Guaranty Bank for 2017.

Financing activities provided cash of $279.2 million for 2018 compared to $382.0 million for 2017, and $154.4 million for 2016. Net increases in deposits totaled $271.3 million, $385.1 million, and $302.4 million for 2018, 2017, and 2016, respectively. Net short-term borrowings increased $13.6 million, $39.1 million and $104.7 million in 2018 and 2017 and 2016, respectively. In 2018 the Company did not prepay any FHLB advances and other borrowings. In 2017, and 2016, respectively, the Company used $4.1 million, and $31.0 million to prepay select FHLB advances and other borrowings. Short-term FHLB advances increased $24.8 million, $60.9 million. and $20.5 million in 2018, 2017, and 2016, respectively.

Total cash provided by operating activities was $64.3 million for 2018, compared to $33.7 million for 2017, and $43.4 million for 2016.

Throughout its history, the Company has secured additional capital through various resources, including common and preferred stock and the issuance of trust preferred securities.

As of December 31, 2018 and 2017, the subsidiary banks remained “well-capitalized” in accordance with regulatory capital requirements administered by the federal banking authorities. See Note 16 to the Consolidated Financial Statements for detail of the capital amounts and ratios for the Company and subsidiary banks.

The Company filed a universal shelf registration statement on Form S 3 with the SEC on October 27, 2016, as amended on January 11, 2017. Declared effective by the SEC on January 31, 2017, the registration statement allows the Company to offer and sell various types of securities, including common stock, preferred stock, debt securities and/or warrants, from time to time up to an aggregate amount of $100 million. The specific terms and prices of any securities offered pursuant to the registration statement will be determined at the time of any future offering and described in a separate prospectus supplement, which would be filed with the SEC at the time of the particular offering, if any. There were no securities issued under this shelf registration statement during 2017 or 2018. In February 2019, the Company utilized a portion of the $100.0 million by completing an underwritten public offering of $65.0 million in aggregate principal amount of its 5.375% Fixed-to-Floating Rate Subordinated Notes. Net proceeds, after deducting the underwriting discount and expenses, were approximately $63.5 million. Refer to Note 23 of the Consolidated Financial Statements for additional information.

The subordinated notes qualify for regulatory capital treatment, therefore Tier 2 Capital will increase by the net proceeds amount of $63.5 million. The following table compares actual regulatory capital ratios to pro forma capital ratios, reflecting the issuance of the subordinated notes:

	For the Year Ended December 31, 2018			
	Actual		Pro forma	
	Amount	Ratio	Amount	Ratio
Total Risk-Based Capital	$ 460,416	10.69%	$ 523,889	12.34
Tier 1 Risk-Based Capital	420,569	9.77	420,569	9.77
Tier 1 Leverage Ratio	420,569	8.87	420,569	8.87
Common Equity Tier 1 Capital	382,899	8.89	382,899	8.89

Table of Contents

COMMITMENTS, CONTINGENCIES, CONTRACTUAL OBLIGATIONS, AND OFF-BALANCE SHEET ARRANGEMENTS

In the normal course of business, the subsidiary banks make various commitments and incur certain contingent liabilities that are not presented in the accompanying Consolidated Financial Statements. The commitments and contingent liabilities include various guarantees, commitments to extend credit, and standby letters of credit.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The subsidiary banks evaluate each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the banks upon extension of credit, is based upon management's credit evaluation of the counter-party. Collateral held varies but may include accounts receivable, marketable securities, inventory, property, plant and equipment, and income-producing commercial properties.

Standby letters of credit are conditional commitments issued by the subsidiary banks to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support public and private borrowing arrangements and, generally, have terms of one year, or less. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The banks hold collateral, as described above, supporting those commitments if deemed necessary. In the event the customer does not perform in accordance with the terms of the agreement with the third party, the banks would be required to fund the commitments. The maximum potential amount of future payments the banks could be required to make is represented by the contractual amount. If the commitment is funded, the banks would be entitled to seek recovery from the customer. At December 31, 2018 and 2017, no amounts had been recorded as liabilities for the banks' potential obligations under these guarantees.

As of December 31, 2018 and 2017, commitments to extend credit aggregated $1.17 billion and $791.6 million, respectively. As of December 31, 2018 and 2017, standby letters of credit aggregated $20.3 million and $17.3 million, respectively. Management does not expect that all of these commitments will be funded.

Additional information regarding commitments, contingencies, and off-balance sheet arrangements is described in Note 18 to the Consolidated Financial Statements.

The Company has various financial obligations, including contractual obligations and commitments, which may require future cash payments. The following table presents, as of December 31, 2018, significant fixed and determinable contractual obligations to third parties by payment date. Further discussion of the nature of each obligation is included in the referenced note to the Consolidated Financial Statements.

	Financial Statement Note	Payments Due by Period				
Description	Reference	Total	One Year or Less	2 - 3 Years	4 - 5 Years	After 5 Years
	(dollars in thousands)					
Deposits without a stated maturity	N/A	$ 3,002,327	$ 3,002,327	$ —	$ —	$ —
Certificates of deposit	8	974,704	796,333	148,019	30,094	258

Short-term borrowings	9	28,774	28,774	—	—	—
FHLB advances	10	266,492	239,958	26,534	—	—
Other borrowings	11	72,032	26,750	40,500	—	4,782
Junior subordinated debentures	12	37,670	—	—	—	37,670
Rental commitments	5	1,414	576	619	203	16
Operating contracts	N/A	39,497	11,752	16,557	5,892	5,296
Total contractual cash obligations		$ 4,422,910	$ 4,106,470	$ 232,229	$ 36,189	$ 48,022

The Company’s operating contract obligations represent short and long-term contractual payments for data processing equipment and services, software, and other equipment and professional services.

Table of Contents

IMPACT OF INFLATION AND CHANGING PRICES

The Consolidated Financial Statements of the Company and the accompanying notes have been prepared in accordance with U.S. GAAP, which require the measurement of financial position and operating results in terms of historical dollar amounts without considering the changes in the relative purchasing power of money over time due to inflation. The impact of inflation is reflected in the increased cost of the Company's operations. Unlike industrial companies, nearly all of the assets and liabilities of the Company are monetary in nature. As a result, interest rates have a greater impact on the Company's performance than do the effects of general levels of inflation. Interest rates do not necessarily move in the same direction or to the same extent as the price of goods and services.

FORWARD LOOKING STATEMENTS

This document (including information incorporated by reference) contains, and future oral and written statements of the Company and its management may contain, forward-looking statements, within the meaning of such term in the Private Securities Litigation Reform Act of 1995, with respect to the financial condition, results of operations, plans, objectives, future performance and business of the Company. Forward-looking statements, which may be based upon beliefs, expectations and assumptions of the Company's management and on information currently available to management, are generally identifiable by the use of words such as "believe," "expect," "anticipate," "bode," "predict," "suggest," "project," "appear," "plan," "intend," "estimate," "may," "will," "would," "could," "should," "likely," or other simi Additionally, all statements in this document, including forward-looking statements, speak only as of the date they are made, and the Company undertakes no obligation to update any statement in light of new information or future events.

The Company's ability to predict results or the actual effect of future plans or strategies is inherently uncertain. The factors that could have a material adverse effect on the operations and future prospects of the Company and its subsidiaries are detailed in the "Risk Factors" section included under Item 1A. of Part I of this Form 10 K. In addition to the risk factors described in that section, there are other factors that could have a material adverse effect on the operations and future prospects of the Company and its subsidiaries. These additional factors include, but are not limited to, the following:

- The strength of the local, state, and national economy (including the impact of tariffs, a U.S. withdrawal from or significant renegotiation of trade agreements, trade wars and other changes in trade regulation).

- Changes in the interest rate environment.

- The economic impact of past and any future terrorist attacks, acts of war or threats thereof and the response of the United States to any such threats and attacks.

- The impact of cybersecurity risks.

- The costs, effects and outcomes of existing or future litigation.

- Changes in accounting policies and practices, as may be adopted by state and federal regulatory agencies, the FASB, the SEC or the PCAOB.

- Unexpected results of acquisitions which may include failure to realize the anticipated benefits of the acquisition.

- The economic impact of exceptional weather occurrences such as tornadoes, floods and blizzards.

- The ability of the Company to manage the risks associated with the foregoing as well as anticipated.

- The imposition of tariffs or other governmental policies impacting the value of the agricultural or other products of our borrowers.

These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements.

Table of Contents

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

The Company, like other financial institutions, is subject to direct and indirect market risk. Direct market risk exists from changes in interest rates. The Company's net income is dependent on its net interest income. Net interest income is susceptible to interest rate risk to the degree that interest-bearing liabilities mature or reprice on a different basis than interest-earning assets. When interest-bearing liabilities mature or reprice more quickly than interest-earning assets in a given period, a significant increase in market rates of interest could adversely affect net interest income. Similarly, when interest-earning assets mature or reprice more quickly than interest-bearing liabilities, falling interest rates could result in a decrease in net interest income.

In an attempt to manage the Company's exposure to changes in interest rates, management monitors the Company's interest rate risk. Each subsidiary bank has an asset/liability management committee of the board of directors that meets quarterly to review the bank's interest rate risk position and profitability, and to make or recommend adjustments, as necessary, for consideration by the full board of each bank.

Internal asset/liability management teams consisting of members of the subsidiary banks' management meet weekly to manage the mix of assets and liabilities to maximize earnings and liquidity and minimize interest rate and other risks. Management also reviews the subsidiary banks' securities portfolios, formulates investment strategies, and oversees the timing and implementation of transactions to assure attainment of the board's objectives in the most effective manner. Notwithstanding the Company's interest rate risk management activities, the potential for changing interest rates is an uncertainty that can have an adverse effect on net income.

In adjusting the Company's asset/liability position, the board of directors and management attempt to manage the Company's interest rate risk while maintaining or enhancing net interest margins. At times, depending on the level of general interest rates, the relationship between long-term and short-term interest rates, market conditions and competitive factors, the board of directors and management may decide to increase the Company's interest rate risk position somewhat in order to increase its net interest margin. The Company's results of operations and net portfolio values remain vulnerable to increases in interest rates and to fluctuations in the difference between long-term and short-term interest rates.

One method used to quantify interest rate risk is a short-term earnings at risk summary, which is a detailed and dynamic simulation model used to quantify the estimated exposure of net interest income to sustained interest rate changes. This simulation model captures the impact of changing interest rates on the interest income received and interest expense paid on all interest sensitive assets and liabilities reflected on the Company's consolidated balance sheet. This sensitivity analysis demonstrates net interest income exposure annually over a five-year horizon, assuming no balance sheet growth, no balance sheet mix change, and various interest rate scenarios including no change in rates; 100, 200, 300 and 400 basis point upward shifts; and 100 and 200 basis point downward shifts in interest rates, where interest-bearing assets and liabilities reprice at their earliest possible repricing date.

The model assumes parallel and pro rata shifts in interest rates over a twelve-month period for the 200 basis point upward shift and 100 and 200 basis point downward shifts. For the 400 basis point upward shift, the model assumes a parallel and pro rata shift in interest rates over a twenty-four month period.

Further, in recent years, the Company added additional interest rate scenarios where interest rates experience a parallel and instantaneous shift ("shock") upward of 100, 200, 300, and 400 basis points and a parallel and instantaneous shock downward of 100 and 200 basis points. The Company will run additional interest rate scenarios on an as-needed basis.

The asset/liability management committees of the subsidiary bank boards of directors have established policy limits of a 10% decline in net interest income for the 200 basis point upward parallel shift and the 100 basis point downward

parallel shift. For the 300 basis point upward shock, the established policy limit is a 25% decline in net interest income. The increased policy limit is appropriate as the shock scenario is extreme and unlikely and warrants a higher limit than the more realistic and traditional parallel/pro-rata shift scenarios.

Table of Contents

Application of the simulation model analysis for select interest rate scenarios at December 31, 2018, 2017 and 2016 demonstrated the following:

	NET INTEREST INCOME EXPOSURE in YEAR 1							
			As of December 31,		As of December 31,		As of December 31,	
INTEREST RATE SCENARIO	POLICY LIMIT		2018		2017		2016	
100 basis point downward shift	(10.0)	%	0.7	%	0.3	%	(1.7)	%
200 basis point upward shift	(10.0)	%	(2.7)	%	(3.7)	%	(1.2)	%
300 basis point upward shock	(25.0)	%	(9.0)	%	(8.4)	%	(1.4)	%

The simulation is within the board-established policy limits for all three scenarios. Additionally, for all of the various interest rate scenarios modeled and measured by management (as described above), the results at December 31, 2018 were well within established risk tolerances as established by policy or by best practice (if the interest rate scenario didn’t have a specific policy limit).

Interest rate risk is considered to be one of the most significant market risks affecting the Company. For that reason, the Company engages the assistance of a national consulting firm and its risk management system to monitor and control the Company’s interest rate risk exposure. Other types of market risk, such as foreign currency exchange rate risk and commodity price risk, do not arise in the normal course of the Company’s business activities.

Table of Contents

Item 8. Financial Statements

QCR HOLDINGS, INC.

Index to Consolidated Financial Statements

Report of Independent Registered Public Accounting Firm

Financial Statements

Consolidated Balance Sheets as of December 31, 2018 and 2017

Consolidated Statements of Income for the years ended December 31, 2018, 2017, and 2016

Consolidated Statements of Comprehensive Income for the years ended December 31, 2018, 2017, and 2016

Consolidated Statements of Changes in Stockholders' Equity for the years ended December 31, 2018, 2017, and 2016

Consolidated Statements of Cash Flows for the years ended December 31, 2018, 2017, and 2016

Notes to Consolidated Financial Statements:

Note 1: Nature of Business and Significant Accounting Policies
Note 2: Mergers/Acquisitions
Note 3: Investment Securities
Note 4: Loans/Leases Receivable
Note 5: Premises and Equipment
Note 6: Goodwill and Intangibles
Note 7: Derivatives and Hedging Activities
Note 8: Deposits
Note 9: Short-Term Borrowings
Note 10: FHLB Advances
Note 11: Other Borrowings and Unused Lines of Credit
Note 12: Junior Subordinated Debentures
Note 13: Federal and State Income Taxes
Note 14: Employee Benefit Plans
Note 15: Stock-Based Compensation
Note 16: Regulatory Capital Requirements and Restrictions on Dividends
Note 17: Earnings Per Share
Note 18: Commitments and Contingencies
Note 19: Quarterly Results of Operations (Unaudited)
Note 20: Parent Company Only Financial Statements
Note 21: Fair Value
Note 22: Business Segment Information
Note 23: Subsequent Event: Subordinated Notes

57

Table of Contents

Report of Independent Registered Public Accounting Firm

To the Stockholders and the Board of Directors of QCR Holdings, Inc.

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of QCR Holdings, Inc. and subsidiaries (the Company) as of December 31, 2018 and 2017, the related consolidated statements of income, comprehensive income, changes in stockholders' equity and cash flows for each of the three years in the period ended December 31, 2018, and the related notes to the consolidated financial statements (collectively, the financial statements). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2018 and 2017, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2018, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company's internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013, and our report dated March 15, 2019 expressed an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

Basis for Opinion

These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on the Company’s financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates

made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

We have served as the Company's auditor since 1993.

Davenport, Iowa

March 15, 2019

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Consolidated Balance Sheets

December 31, 2018 and 2017

	December 31, 2018	December 31, 2017
Assets		
Cash and due from banks	$ 85,522,685	$ 75,721,663
Federal funds sold	26,398,000	30,197,000
Interest-bearing deposits at financial institutions	133,198,095	55,765,012
Securities held to maturity, at amortized cost	401,912,885	379,474,205
Securities available for sale, at fair value	261,056,448	272,907,907
Total securities	662,969,333	652,382,112
Loans receivable held for sale	1,295,400	645,001
Loans/leases receivable held for investment	3,731,458,642	2,963,840,399
Gross loans/leases receivable	3,732,754,042	2,964,485,400
Less allowance for estimated losses on loans/leases	(39,847,108)	(34,355,728)
Net loans/leases receivable	3,692,906,934	2,930,129,672
Bank-owned life insurance	67,783,126	59,059,494
Premises and equipment, net	75,582,118	62,838,255
Restricted investment securities	25,688,775	19,782,525
Other real estate owned, net	9,377,735	13,558,308
Goodwill	77,831,902	28,334,092
Intangibles	17,450,182	9,078,953
Other assets	75,001,310	45,817,687
Total assets	$ 4,949,710,195	$ 3,982,664,773
Liabilities and Stockholders' Equity		
Liabilities:		
Deposits:		
Noninterest-bearing	$ 791,101,467	$ 789,547,696
Interest-bearing	3,185,929,107	2,477,107,360
Total deposits	3,977,030,574	3,266,655,056
Short-term borrowings	28,774,157	13,993,122
Federal Home Loan Bank advances	266,492,039	192,000,000
Other borrowings	72,032,318	66,000,000
Junior subordinated debentures	37,670,043	37,486,487
Other liabilities	94,572,661	53,242,979
Total liabilities	4,476,571,792	3,629,377,644
Stockholders' Equity:		

Preferred stock, $1 par value; shares authorized 250,000 December 2018 and December 2017- No shares issued or outstanding	—	—
Common stock, $1 par value; shares authorized 20,000,000 December 2018 - 15,718,208 shares issued and outstanding December 2017 - 13,918,168 shares issued and outstanding	15,718,208	13,918,168
Additional paid-in capital	270,760,511	189,077,550
Retained earnings	192,203,333	151,962,661
Accumulated other comprehensive loss:		
Securities available for sale	(4,267,461)	(866,223)
Derivatives	(1,276,188)	(805,027)
Total stockholders' equity	473,138,403	353,287,129
Total liabilities and stockholders' equity	$ 4,949,710,195	$ 3,982,664,773

See Notes to Consolidated Financial Statements.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Consolidated Statements of Income

Years Ended December 31, 2018, 2017, and 2016

	2018	2017	2016
Interest and dividend income:			
Loans/leases, including fees	$ 160,160,173	$ 117,465,275	$ 91,235,049
Securities:			
Taxable	6,353,413	5,144,336	4,585,300
Nontaxable	13,668,283	11,253,351	9,686,844
Interest-bearing deposits at financial institutions	1,266,530	873,988	393,048
Restricted investment securities	1,092,807	631,049	522,047
Federal funds sold	338,036	149,319	45,447
Total interest and dividend income	182,879,242	135,517,318	106,467,735
Interest expense:			
Deposits	30,674,621	13,011,906	6,018,366
Short-term borrowings	271,243	113,981	93,934
Federal Home Loan Bank advances	4,192,510	1,981,593	1,284,212
Other borrowings	3,346,225	2,878,879	3,317,513
Junior subordinated debentures	1,999,058	1,465,678	1,236,933
Total interest expense	40,483,657	19,452,037	11,950,958
Net interest income	142,395,585	116,065,281	94,516,777
Provision for loan/lease losses	12,658,449	8,469,919	7,478,166
Net interest income after provision for loan/lease losses	129,737,136	107,595,362	87,038,611
Noninterest income:			
Trust department fees	8,707,406	7,187,820	6,164,137
Investment advisory and management fees	4,725,557	3,869,699	2,992,811
Deposit service fees	6,420,237	5,919,317	4,439,455
Gains on sales of residential real estate loans, net	900,744	408,655	431,313
Gains on sales of government guaranteed portions of loans, net	404,852	1,163,741	3,159,073
Swap fee income	10,787,234	3,094,939	1,708,204
Securities gains (losses), net	—	(87,885)	4,592,398
Earnings on bank-owned life insurance	1,631,749	1,802,443	1,771,396
Debit card fees	3,262,645	2,941,703	1,814,488
Correspondent banking fees	851,514	915,647	1,050,142
Other	3,849,156	3,266,213	2,913,458
Total noninterest income	41,541,094	30,482,292	31,036,875
Noninterest expense:			
Salaries and employee benefits	68,994,218	55,722,288	46,317,060
Occupancy and equipment expense	12,883,632	10,938,037	8,404,605
Professional and data processing fees	11,452,084	10,757,057	7,113,443
Acquisition costs	1,795,119	1,068,918	1,400,004

Post-acquisition compensation, transition and integration costs	2,086,386	4,309,565	1,041,169
FDIC insurance, other insurance and regulatory fees	3,594,480	2,752,270	2,549,314
Loan/lease expense	1,543,343	1,163,708	662,299
Net cost and gains/losses on operations of other real estate	2,488,730	1,599	591,303
Advertising and marketing	3,551,822	2,624,951	2,127,566
Bank service charges	1,837,626	1,770,942	1,692,957
Losses on debt extinguishment, net	—	—	4,577,668
Correspondent banking expense	820,905	807,077	750,646
CDI amortization	1,692,431	1,000,561	442,850
Other	6,402,643	4,507,724	3,815,028
Total noninterest expense	119,143,419	97,424,697	81,485,912
Net income before income taxes	52,134,811	40,652,957	36,589,574
Federal and state income tax expense	9,015,112	4,946,450	8,902,787
Net income	$ 43,119,699	$ 35,706,507	$ 27,686,787
Basic earnings per common share	$ 2.92	$ 2.68	$ 2.20
Diluted earnings per common share	$ 2.86	$ 2.61	$ 2.17
Weighted average common shares outstanding	14,768,687	13,325,128	12,570,767
Weighted average common and common equivalent shares outstanding	15,064,730	13,680,472	12,766,003
Cash dividends declared per common share	$ 0.24	$ 0.20	$ 0.16

See Notes to Consolidated Financial Statements.

Table of Contents

QCR HOLDINGS, INC. AND SUBSIDIARIES

Consolidated Statements of Comprehensive Income

Years Ended December 31, 2018, 2017, and 2016

	2018	2017	2016
Net income	$ 43,119,699	$ 35,706,507	$ 27,686,787
Other comprehensive income (loss):			
Unrealized gains (losses) on securities available for sale:			
Unrealized holding gains (losses) arising during the period before tax	(4,464,294)	1,257,289	4,258,154
Less reclassification adjustment for gains (losses) included in net income before tax	—	(87,885)	4,592,398
Less reclassification adjustment for adoption of ASU 2016-01	855,039	—	—
	(3,609,255)	1,345,174	(334,244)
Unrealized gains (losses) on derivatives:			
Unrealized holding gains (losses) arising during the period before tax	(1,199,062)	(69,827)	(279,497)
Less reclassification adjustment for ineffectiveness and caplet amortization before tax	(602,654)	(484,891)	(75,290)
	(596,408)	415,064	(204,207)
Other comprehensive income (loss), before tax	(4,205,663)	1,760,238	(538,451)
Tax expense (benefit)	(1,000,164)	668,085	(202,691)
Other comprehensive income (loss), net of tax	(3,205,499)	1,092,153	(335,760)
Comprehensive income	$ 39,914,200	$ 36,798,660	$ 27,351,027

See Notes to Consolidated Financial Statements.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Consolidated Statements of Changes in Stockholders' Equity

Years Ended December 31, 2018, 2017, and 2016

	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive (Loss)	Total
Balance December 31, 2015	$ 11,761,083	$ 123,282,851	$ 92,965,645	$ (2,123,829)	$ 225,885,750
Net income	—	—	27,686,787	—	27,686,787
Other comprehensive loss, net of tax	—	—	—	(335,760)	(335,760)
Common cash dividends declared, $0.16 per share	—	—	(2,035,531)	—	(2,035,531)
Issuance of 1,215,000 shares of common stock, net of issuance costs of $242,334	1,215,000	28,613,916	—	—	29,828,916
Issuance of 20,192 shares of common stock as a result of stock purchased under the Employee Stock Purchase Plan	20,192	417,336	—	—	437,528
Issuance of 111,423 shares of common stock as a result of stock options exercised	111,423	1,556,823	—	—	1,668,246
Tax basis adjustment related to the acquisition of noncontrolling interest in m2 Lease Funds	—	2,132,415	—	—	2,132,415
Stock-based compensation expense	—	947,174	—	—	947,174
Tax benefit of nonqualified stock options exercised	—	394,149	—	—	394,149
Restricted stock awards - 21,882 shares of common stock	21,882	(21,882)	—	—	—

Exchange of 22,735 shares of common stock in connection with payroll taxes for restricted stock and in connection with stock options exercised	(22,735)	(546,140)	—	—	(568,875)
Balance, December 31, 2016	$ 13,106,845	$ 156,776,642	$ 118,616,901	$ (2,459,589)	$ 286,040,799
Net income	—	—	35,706,507	—	35,706,507
Other comprehensive loss, net of tax	—	—	—	1,092,153	1,092,153
Reclassification of certain tax effects from accumulated other comprehensive income	—	—	303,814	(303,814)	—
Common cash dividends declared, $0.20 per share	—	—	(2,664,561)	—	(2,664,561)
Issuance of 678,670 shares of common stock as a result of the acquisition of Guaranty Bank & Trust, net of issuance costs of $138,071	678,670	30,062,744	—	—	30,741,414
Issuance of 13,318 shares of common stock as a result of stock purchased under the Employee Stock Purchase Plan	13,318	454,822	—	—	468,140
Issuance of 114,100 shares of common stock as a result of stock options exercised	114,100	1,611,338	—	—	1,725,438
Stock-based compensation expense	—	1,187,036	—	—	1,187,036
Restricted stock awards - 28,289 shares of common stock	28,289	(28,289)	—	—	—
Exchange of 23,054 shares of common stock in connection with payroll taxes for restricted stock and in connection					

with stock options exercised	(23,054)	(986,743)	—	—	(1,009,797)
Balance, December 31, 2017	$ 13,918,168	$ 189,077,550	$ 151,962,661	$ (1,671,250)	$ 353,287,129
Net income	—	—	43,119,699	—	43,119,699
Other comprehensive loss, net of tax	—	—	—	(3,205,499)	(3,205,499)
Impact of adoption of ASU 2016-01	—	—	666,900	(666,900)	—
Common cash dividends declared, $0.24 per share	—	—	(3,545,927)	—	(3,545,927)
Issuance of 1,699,414 shares of common stock as a result of merger with Springfield Bancshares, net of issuance costs of $106,237	1,699,414	78,831,543	—	—	80,530,957
Issuance of 23,501 shares of common stock as a result of acquisition of Bates Companies	23,501	976,471	—	—	999,972
Issuance of 15,528 shares of common stock as a result of stock purchased under the Employee Stock Purchase Plan	15,528	576,245	—	—	591,773
Issuance of 60,127 shares of common stock as a result of stock options exercised	60,127	733,491	—	—	793,618
Stock-based compensation expense	—	1,443,346	—	—	1,443,346
Restricted stock awards - 22,660 shares of common stock	22,660	(22,660)	—	—	—
Exchange of 21,190 shares of common stock in connection with payroll taxes for restricted stock and in connection with stock options exercised	(21,190)	(855,475)	—	—	(876,665)
Balance December 31, 2018	$ 15,718,208	$ 270,760,511	$ 192,203,333	$ (5,543,649)	$ 473,138,403

See Notes to Consolidated Financial Statements.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Consolidated Statements of Cash Flows

Years Ended December 31, 2018, 2017, and 2016

	2018	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income	$ 43,119,699	$ 35,706,507	$ 27,686,787
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation	4,450,758	3,948,934	3,424,140
Provision for loan/lease losses	12,658,449	8,469,919	7,478,166
Deferred income taxes	6,292,477	(6,029,555)	(3,066,407)
Stock-based compensation expense	1,443,346	1,187,036	947,174
Deferred compensation expense accrued	1,826,055	1,425,717	1,171,406
Losses (gains) on other real estate owned, net	2,584,890	(151,211)	243,858
Amortization of premiums on securities, net	1,614,426	1,839,196	1,302,962
Securities (gains) losses, net	—	87,885	(4,592,398)
Loans originated for sale	(57,697,515)	(49,578,773)	(74,329,667)
Proceeds on sales of loans	58,352,712	51,641,668	77,850,553
Gains on sales of residential real estate loans	(900,744)	(408,655)	(431,313)
Gains on sales of government guaranteed portions of loans	(404,852)	(1,163,741)	(3,159,073)
Losses on debt extinguishment, net	—	—	4,577,668
Amortization of core deposit intangible	1,692,431	1,000,561	442,850
Accretion of acquisition fair value adjustments, net	(5,527,105)	(4,940,760)	(3,718,160)
Increase in cash value of bank-owned life insurance	(1,631,749)	(1,802,443)	(1,771,396)
Decrease (increase) in other assets	(11,140,958)	726,336	(943,892)
Increase (decrease) in other liabilities	7,538,428	(8,245,340)	10,269,563
Net cash provided by operating activities	64,270,748	33,713,281	43,382,821
CASH FLOWS FROM INVESTING ACTIVITIES			
Net decrease (increase) in federal funds sold	3,799,000	(7,940,000)	(1,709,000)
Net decrease (increase) in interest-bearing deposits at financial institutions	(14,508,687)	12,137,820	(12,904,803)
Proceeds from sales of other real estate owned	2,538,865	1,138,520	2,084,696
Activity in securities portfolio:			
Purchases	(84,044,869)	(179,785,944)	(179,598,630)
Calls, maturities and redemptions	23,931,014	43,010,478	117,876,284
Paydowns	44,287,054	38,495,801	33,169,638
Sales	1,938,043	71,091,580	134,188,737
Activity in restricted investment securities:			
Purchases	(5,409,075)	(4,824,000)	(1,098,200)
Redemptions	3,157,025	515,000	2,450,000
Net increase in loans/leases originated and held for investment	(292,696,750)	(375,226,301)	(187,496,180)
Purchase of premises and equipment	(11,457,086)	(5,760,802)	(6,032,416)

Net cash paid for acquisitions	(5,182,804)	(3,368,909)	(69,905,355)
Net cash used in investing activities	(333,648,270)	(410,516,757)	(168,975,229)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Net increase in deposit accounts	271,266,725	385,082,234	302,390,928
Net increase (decrease) in short-term borrowings	13,637,557	(39,080,308)	(104,691,329)
Activity in Federal Home Loan Bank advances:			
Term advances	15,080,200	1,600,000	—
Calls and maturities	(40,000,000)	(8,000,000)	(24,000,000)
Net change in short-term and overnight advances	24,765,000	60,900,000	20,500,000
Prepayments	—	(4,108,027)	(31,008,668)
Activity in other borrowings:			
Proceeds from other borrowings	9,000,000	7,000,000	35,000,000
Calls, maturities and scheduled principal payments	(12,550,000)	(21,000,000)	—
Prepayments	—	—	(69,769,000)
Retirement of junior subordinated debentures	—	—	(3,955,000)
Payment of cash dividends on common stock	(3,300,091)	(2,494,260)	(1,981,541)
Proceeds from issuance of common stock, net	1,279,153	2,055,507	31,934,690
Net cash provided by financing activities	279,178,544	381,955,146	154,420,080
Net decrease in cash and due from banks	9,801,022	5,151,670	28,827,672
Cash and due from banks, beginning	75,721,663	70,569,993	41,742,321
Cash and due from banks, ending	$ 85,522,685	$ 75,721,663	$ 70,569,993

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Consolidated Statements of Cash Flows - Continued

Years Ended December 31, 2018, 2017, and 2016

	2018	2017	2016
Supplemental disclosure of cash flow information, cash payments (receipts) for:			
Interest	$ 38,781,813	$ 19,053,645	$ 11,926,012
Income/franchise taxes	29,583	13,039,516	10,758,611
Supplemental schedule of noncash investing activities:			
Change in accumulated other comprehensive income, unrealized gains on securities available for sale and derivative instruments, net	(3,205,499)	1,092,153	(335,760)
Exchange of shares of common stock in connection with payroll taxes for restricted stock and in connection with stock options exercised	(876,665)	(1,009,797)	(568,875)
Tax benefit of nonqualified stock options exercised	—	—	394,149
Transfers of loans to other real estate owned	943,183	9,022,514	51,000
Due to broker for purchases of securities	—	—	2,655,492
Tax basis adjustment related to the acquisition of noncontrolling interest in m2 Lease Funds	—	—	2,132,415
Increase (decrease) in the fair value of back to back interest rate swap assets and liabilities	17,798,475	2,058,957	(706,244)
Dividends payable	938,710	692,874	522,573
Transfer of equity securities from securities available for sale to other assets at fair value	2,614,260	—	—
Supplemental disclosure of cash flow information for acquisitions:			
Fair value of assets acquired:			
Cash and due from banks	$ 4,650,731	$ 4,434,511	$ 10,094,645
Federal funds sold	—	—	698,000
Interest-bearing deposits at financial institutions	62,924,396	3,953,907	14,730,157
Securities	4,845,441	49,703,419	102,640,029
Loans receivable, net	477,336,699	192,517,677	419,029,277
Bank-owned life insurance	7,091,883	—	—
Premises and equipment, net	6,091,978	4,808,343	20,684,880
Restricted investment securities	3,654,200	476,500	1,512,900
Other real estate owned	—	—	650,000
Intangibles	10,063,660	2,698,301	6,352,653
Other assets	2,254,778	997,810	5,283,937
Total assets acquired	$ 578,913,766	$ 259,590,468	$ 581,676,478
Fair value of liabilities assumed:			

Deposits	$ 439,579,328	$ 212,467,514	$ 486,298,262
Short-term borrowings	1,143,478	13,102,043	—
FHLB advances	74,539,463	4,108,027	20,368,877
Other borrowings	9,543,810	—	—
Junior subordinated debentures	—	3,857,275	—
Other liabilities	8,877,991	2,595,883	4,897,564
Total liabilities assumed	533,684,070	236,130,742	511,564,703
Net assets acquired	$ 45,229,696	$ 23,459,726	$ 70,111,775
Consideration paid:			
Cash paid *	$ 9,833,535	$ 7,803,420	$ 80,000,000
Promissory note	1,500,000	—	—
Contingent consideration	2,000,000	—	—
Common stock	81,637,166	30,879,485	—
Total consideration paid	94,970,701	38,682,905	80,000,000
Goodwill	$ 49,741,005	$ 15,223,179	$ 9,888,225

* Net cash paid at closing totaled $1,435,595 for acquisition of the Bates Companies in 2018.

Net cash paid at closing totaled $3,747,209 for merger with Springfield Bancshares in 2018.

Net cash paid at closing totaled $3,368,909 for acquisition of Guaranty Bank in 2017.

Net cash paid at closing totaled $69,905,355 for acquisition of CSB in 2016.

See Notes to Consolidated Financial Statements.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Nature of Business and Significant Accounting Policies

Basis of presentation:

The acronyms and abbreviations identified below are used in the Notes to the Consolidated Financial Statements, as well as in the other sections of this Form 10 K (including appendices). It may be helpful to refer back to this page as you read this report.

Allowance: Allowance for estimated losses on loans/leases
AOCI: Accumulated other comprehensive income (loss)
AFS: Available for sale
ASC: Accounting Standards Codification
ASC 805: Business Combination Standard
ASU: Accounting Standards Update

Bates Companies: Bates Financial Advisors, Inc., Bates Financial Services, Inc., Bates Securities, Inc. and Batess Financial Group, Inc.
BBA: British Bankers' Association.
BHCA: Bank Holding Company Act of 1956
BOLI: Bank-owned life insurance
Caps: Interest rate cap derivatives

CBRL: Community Bank Leverage Ratio
CFPB: Bureau of Consumer Financial Protection
CDI: Core deposit intangible
Community National: Community National Bancorporation
CNB: Community National Bank
CRA: Community Reinvestment Act
CRBT: Cedar Rapids Bank & Trust Company
CRE: Commercial real estate
CRE Guidance: Interagency Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices guidance
CSB: Community State Bank
C&I: Commercial and industrial
Dodd-Frank Act: Dodd-Frank Wall Street Reform and Consumer Protection Act
DGCL: Delaware General Corporation Law
DIF: Deposit Insurance Fund
EPS: Earnings per share DIF: Deposit Insurance Fund
Exchange Act: Securities Exchange Act of 1934, as amended

Goldman Sachs: Goldman Sachs and Company
HTM: Held to maturity
IDFPR: Illinois Department of Financial & Professional Regulation
Iowa Superintendent: Iowa Superintendent of Banking
LCR: Liquidity Coverage Ratio

LIBOR: London Inter-Bank Offered Rate
m2: m2 Lease Funds, LLC
MD&A: Management's Discussion & Analysis
MSA: Metropolitan Statistical Area
NIM: Net interest margin
NPA: Nonperforming asset
NPL: Nonperforming loan

NSFR: Net Stable Funding Ratio
OREO: Other real estate owned
OTTI: Other-than-temporary impairment
PCAOB: Public Company Accounting Oversight Board
PCI: Purchased credit impaired
Provision: Provision for loan/lease losses
PUD LOC: Public Unit Deposit Letter of Credit
QCBT: Quad City Bank & Trust Company
QCIA: Quad Cities Investment Advisors
RB&T: Rockford Bank & Trust Company
ROAA: Return on Average Assets
ROACE: Return on Average Common Equity
ROAE: Return on Average Equity
SBA: U.S. Small Business Administration
SEC: Securities and Exchange Commission
SFC Bank: Springfield First Community Bank
SERPs: Supplemental Executive Retirement Plans
Springfield Bancshares: Springfield Bancshares, Inc.
TA: Tangible assets
Tax Act: Tax Cuts and Jobs Act

FASB: Financial Accounting Standards Board
FDIC: Federal Deposit Insurance Corporation
Federal Reserve: Board of Governors of the Federal Reserve System
FHLB: Federal Home Loan Bank
FICO: Financing Corporation
FRB: Federal Reserve Bank of Chicago
FTEs: Full-time equivalents
GAAP: Generally Accepted Accounting Principles
Guaranty: Guaranty Bankshares, Ltd.
Guaranty Bank: Guaranty Bank and Trust Company
TCE: Tangible common equity
TDRs: Troubled debt restructurings
TEY: Tax equivalent yield
The Company: QCR Holdings, Inc.
Treasury: U.S. Department of the Treasury
USA Patriot Act: Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001
USDA: U.S. Department of Agriculture

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Nature of Business and Significant Account Policies (continued)

Nature of business:

QCR Holdings, Inc. is a bank holding company that has elected to operate as a financial holding company under the BHCA. The Company provides bank and bank-related services through its banking subsidiaries, QCBT, CRBT, CSB, RB&T and SFC Bank. The Company also engages in direct financing lease contracts through its wholly-owned equity investment by QCBT in m2, headquartered in Milwaukee, Wisconsin. The Company also engages in wealth management services through its banking subsidiaries and its subsidiary, the Bates Companies, headquartered in Rockford, Illinois.

On October 1, 2018, the Company acquired the Bates Companies, headquartered in Rockford, Illinois. On July 1, 2018, the Company merged with Springfield Bancshares, the holding company of SFC Bank, headquartered in Springfield, Missouri. On October 1, 2017 the Company acquired Guaranty Bank, headquartered in Cedar Rapids, Iowa, from Guaranty. On December 2, 2017, the Company merged Guaranty Bank with and into CRBT, with CRBT as the surviving bank. On August 31, 2016, the Company acquired Community State Bank in Ankeny, Iowa (Des Moines MSA). The financial results of acquired/merged entities for the periods since acquisition/merger are included in this report. See Note 2 to the Consolidated Financial Statements for additional information.

QCBT is a commercial bank that serves the Iowa and Illinois Quad Cities and adjacent communities. CRBT is a commercial bank that serves Cedar Rapids, Iowa, and adjacent communities including Cedar Falls and Waterloo, Iowa. CSB is a commercial bank that serves Des Moines, Iowa, and adjacent communities. RB&T is a commercial bank that serves Rockford, Illinois, and adjacent communities. SFC is a commercial bank that serves Springfield, Missouri.

QCBT, CRBT, and CSB are chartered and regulated by the state of Iowa. RB&T is chartered and regulated by the state of Illinois. SFC Bank is chartered and regulated by the state of Missouri. All five subsidiary banks are insured and subject to regulation by the FDIC. All five subsidiary bank are members of and regulated by the Federal Reserve System.

The remaining subsidiaries of the Company consist of six non-consolidated subsidiaries formed for the issuance of trust preferred securities. See Note 12 for a listing of these subsidiaries and additional information.

Significant accounting policies:

Accounting estimates: The preparation of financial statements, in conformity with GAAP, requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance, OTTI of securities, impairment of goodwill, the fair value of financial instruments, and the fair value of assets acquired/liabilities assumed in a business combination.

Principles of consolidation: The accompanying Consolidated Financial Statements include the accounts of the Company and its subsidiaries, except those six subsidiaries formed for the issuance of trust preferred securities which do not meet the criteria for consolidation. See Note 12 for a detailed listing of these subsidiaries. All material intercompany accounts and transactions have been eliminated in consolidation.

Presentation of cash flows: For purposes of reporting cash flows, cash and due from banks include cash on hand and noninterest bearing amounts due from banks. Cash flows from federal funds sold, interest bearing deposits at financial institutions, loans/leases, deposits, and short-term borrowings are treated as net increases or decreases.

Cash and due from banks: The subsidiary banks are required by federal banking regulations to maintain certain cash and due from bank reserves. The reserve requirement was approximately $33,372,000 and $41,803,000 as of December 31, 2018 and 2017, respectively.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Nature of Business and Significant Account Policies (continued)

Investment securities: Investment securities held to maturity are those debt securities that the Company has the ability and intent to hold until maturity regardless of changes in market conditions, liquidity needs, or changes in general economic conditions. Such securities are carried at cost adjusted for amortization of premiums and accretion of discounts. If the ability or intent to hold to maturity is not present for certain specified securities, such securities are considered AFS as the Company intends to hold them for an indefinite period of time but not necessarily to maturity. Any decision to sell a security classified as AFS would be based on various factors, including movements in interest rates, changes in the maturity mix of the Company's assets and liabilities, liquidity needs, regulatory capital considerations, and other factors. Securities AFS are carried at fair value. Unrealized gains or losses, net of taxes, are reported as increases or decreases in AOCI. Realized gains or losses, determined on the basis of the cost of specific securities sold, are included in earnings.

All securities are evaluated to determine whether declines in fair value below their amortized cost are other-than-temporary.

In estimating OTTI losses on debt securities, management considers a number of factors including, but not limited to, (1) the length of time and extent to which the fair value has been less than amortized cost, (2) the financial condition and near-term prospects of the issuer, (3) the current market conditions, and (4) the lack of intent of the Company to sell the security prior to recovery and whether it is not more-likely-than-not that it will be required to sell the security prior to recovery.

If the Company lacks the intent to sell the security, and it is not more-likely-than-not the entity will be required to sell the security before recovery of its amortized cost basis, the Company will recognize the credit component of an OTTI of a debt security in earnings and the remaining portion in other comprehensive income. For held to maturity debt securities, the amount of an OTTI recorded in other comprehensive income for the noncredit portion would be amortized prospectively over the remaining life of the security on the basis of the timing of future estimated cash flows of the security.

Loans receivable, held for sale: Residential real estate loans which are originated and intended for resale in the secondary market in the foreseeable future are classified as held for sale. These loans are carried at the lower of cost or estimated market value in the aggregate. As assets specifically acquired for resale, the origination of, disposition of, and gain/loss on these loans are classified as operating activities in the statement of cash flows.

Loans receivable, held for investment: Loans that management has the intent and ability to hold for the foreseeable future, or until pay-off or maturity occurs, are classified as held for investment. These loans are stated at the amount of unpaid principal adjusted for charge-offs, the allowance, and any deferred fees and/or costs on originated loans. Interest is credited to earnings as earned based on the principal amount outstanding. Deferred direct loan origination fees and/or costs are amortized as an adjustment of the related loan's yield. As assets held for and used in the production of services, the origination and collection of these loans are classified as investing activities in the statement of cash flows.

The Company discloses the allowance for credit losses (also known as the allowance) by portfolio segment, and credit quality information, impaired financing receivables, nonaccrual status, and TDRs by class of financing receivable. A portfolio segment is the level at which the Company develops and documents a systematic methodology to determine its allowance for credit losses. A class of financing receivable is a further disaggregation of a portfolio segment based on risk characteristics and the Company's method for monitoring and assessing credit risk. See the following information and Note 4.

The Company's portfolio segments are as follows:

- C&I
- CRE
- Residential real estate
- Installment and other consumer

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Nature of Business and Significant Account Policies (continued)

Direct financing leases are considered a segment within the overall loan/lease portfolio.

The Company's classes of loans receivable are as follows:

- C&I
- Owner-occupied CRE
- Commercial construction, land development, and other land loans that are not owner-occupied CRE
- Other non-owner-occupied CRE
- Residential real estate
- Installment and other consumer

Direct financing leases are considered a class of financing receivable within the overall loan/lease portfolio. The accounting policies for direct financing leases are disclosed below.

Generally, for all classes of loans receivable, loans are considered past due when contractual payments are delinquent for 31 days or greater.

For all classes of loans receivable, loans will generally be placed on nonaccrual status when the loan has become 90 days past due (unless the loan is well secured and in the process of collection); or if any of the following conditions exist:

- It becomes evident that the borrower will not make payments, or will not or cannot meet the terms for renewal of a matured loan;
- When full repayment of principal and interest is not expected;
- When the loan is graded "doubtful";
- When the borrower files bankruptcy and an approved plan of reorganization or liquidation is not anticipated in the near future; or
- When foreclosure action is initiated.

When a loan is placed on nonaccrual status, income recognition is ceased. Previously recorded but uncollected amounts of interest on nonaccrual loans are reversed at the time the loan is placed on nonaccrual status. Generally, cash collected on nonaccrual loans is applied to principal. Should full collection of principal be expected, cash collected on nonaccrual loans can be recognized as interest income.

For all classes of loans receivable, nonaccrual loans may be restored to accrual status provided the following criteria are met:

- The loan is current, and all principal and interest amounts contractually due have been made;
- All principal and interest amounts contractually due, including past due payments, are reasonably assured of repayment within a reasonable period; and
- There is a period of minimum repayment performance, as follows, by the borrower in accordance with contractual terms:

oSix months of repayment performance for contractual monthly payments, or

oOne year of repayment performance for contractual quarterly or semi-annual payments.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Nature of Business and Significant Account Policies (continued)

Direct finance leases receivable, held for investment: The Company leases machinery and equipment to customers under leases that qualify as direct financing leases for financial reporting and as operating leases for income tax purposes. Under the direct financing method of accounting, the minimum lease payments to be received under the lease contract, together with the estimated unguaranteed residual values (approximately 3% to 25% of the cost of the related equipment), are recorded as lease receivables when the lease is signed and the lease property delivered to the customer. The excess of the minimum lease payments and residual values over the cost of the equipment is recorded as unearned lease income. Unearned lease income is recognized over the term of the lease on a basis that results in an approximate level rate of return on the unrecovered lease investment.

Lease income is recognized on the interest method. Residual value is the estimated fair market value of the equipment on lease at lease termination. In estimating the equipment's fair value at lease termination, the Company relies on historical experience by equipment type and manufacturer and, where available, valuations by independent appraisers, adjusted for known trends.

The Company's estimates are reviewed continuously to ensure reasonableness; however, the amounts the Company will ultimately realize could differ from the estimated amounts. If the review results in a lower estimate than had been previously established, a determination is made as to whether the decline in estimated residual value is other-than-temporary. If the decline in estimated unguaranteed residual value is judged to be other-than-temporary, the accounting for the transaction is revised using the changed estimate. The resulting reduction in the investment is recognized as a loss in the period in which the estimate is changed. An upward adjustment of the estimated residual value is not recorded.

The policies for delinquency and nonaccrual for direct financing leases are materially consistent with those described above for all classes of loan receivables.

The Company defers and amortizes fees and certain incremental direct costs over the contractual term of the lease as an adjustment to the yield. In periods prior to and including December 31, 2018, these initial direct leasing costs approximated 5.5% of the leased asset's cost. With the adoption of ASU 2016-02 on January 1, 2019, a portion of these costs will now be expensed instead of deferred. Accordingly, initial direct leasing costs are expected to approximate only 4.9% of the leased asset's cost in 2019. The unamortized direct costs are recorded as a reduction of unearned lease income.

TDRs: TDRs exist when the Company, for economic or legal reasons related to the borrower's/lessee's financial difficulties, grants a concession (either imposed by court order, law, or agreement between the borrower/lessee and the Company) to the borrower/lessee that it would not otherwise consider. The Company attempts to maximize its recovery of the balances of the loans/leases through these various concessionary restructurings.

The following criteria, related to granting a concession, together or separately, create a TDR:

· A modification of terms of a debt such as one or a combination of:
oThe reduction of the stated interest rate to a rate lower than the current market rate for new debt with similar risk.

oThe extension of the maturity date or dates at a stated interest rate lower than the current market rate for new debt with similar risk.

oThe reduction of the face amount or maturity amount of the debt as stated in the instrument or other agreement.

oThe reduction of accrued interest.

- A transfer from the borrower/lessee to the Company of receivables from third parties, real estate, other assets, or an equity position in the borrower to fully or partially satisfy a loan.
- The issuance or other granting of an equity position to the Company to fully or partially satisfy a debt unless the equity position is granted pursuant to existing terms for converting the debt into an equity position.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Nature of Business and Significant Account Policies (continued)

Allowance: For all portfolio segments, the allowance is established as losses are estimated to have occurred through a provision that is charged to earnings. Loan/lease losses, for all portfolio segments, are charged against the allowance when management believes the uncollectability of a loan/lease balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

For all portfolio segments, the allowance is evaluated on a regular basis by management and is based upon management's periodic review of the collectability of the loans/leases in light of historical experience, the nature and volume of the loan/lease portfolio, adverse situations that may affect the borrower's/lessee's ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

A discussion of the risk characteristics and the allowance by each portfolio segment follows:

For C&I loans, the Company focuses on small and mid-sized businesses with primary operations as wholesalers, manufacturers, building contractors, business services companies, other banks, and retailers. The Company provides a wide range of C&I loans, including lines of credit for working capital and operational purposes, and term loans for the acquisition of facilities, equipment and other purposes. 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.

Collateral for C&I 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.

The Company's lending policy specifies maximum term limits for C&I loans. For term loans, the maximum term is generally 7 years with average terms ranging from 3 to 5 years. For low-income housing tax credit permanent loans, the maximum term is generally up to 20 years. For lines of credit, the maximum term is generally 365 days.

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

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 CRE 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 (CRE loans on improved property, raw land, land development, and commercial construction). These limits are the same limits established by regulatory authorities.

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

In addition, management tracks the level of owner-occupied CRE loans versus non-owner occupied loans. Owner-occupied loans are generally considered to have less risk. As of December 31, 2018 and 2017, approximately 28% and 26%, respectively, of the CRE loan portfolio was owner-occupied.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Nature of Business and Significant Account Policies (continued)

The Company's lending policy incorporates regulatory guidelines which stipulate that non-owner occupied CRE lending in excess of 300% of total risk-based capital, and construction, land development, and other land loans in excess of 100% of total risk-based capital warrant the use of heightened risk management practices. As of December 31, 2018 and 2017, QCBT, CRBT and RB&T were in compliance with these limits. Although CSB's and SFC Bank's loan portfolio have historically been real estate dominated and the real estate portfolio levels at each bank exceed these policy limits, a Credit Risk Committee has been established to routinely monitor its real estate loan portfolio. CSB's real estate levels, while still elevated at December 31, 2018, have declined since December 31, 2017.

In some instances for all loans/leases, it may be appropriate to originate or purchase loans/leases that are exceptions to the guidelines and limits established within the Company's lending policy described above and below. In general, exceptions to the lending policy do not significantly deviate from the guidelines and limits established within the Company's lending policy and, if there are exceptions, they are clearly noted as such and specifically identified in loan/lease approval documents.

For C&I and CRE loans, the allowance consists of specific and general components.

The specific component relates to loans that are classified as impaired, as defined below. For those loans that are classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan are lower than the carrying value of that loan.

For C&I loans and all classes of CRE loans, a loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal and interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a case-by-case basis by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

The general component consists of quantitative and qualitative factors and covers non-impaired loans. The quantitative factors are based on historical charge-off experience and expected loss given default derived from the Company's internal risk rating process. See below for a detailed description of the Company's internal risk rating scale. The qualitative factors are determined based on an assessment of internal and/or external influences on credit quality that are not fully reflected in the historical loss or risk rating data.

For C&I and CRE loans, the Company utilizes the following internal risk rating scale:

1.

Highest Quality (Pass) – loans of the highest quality with no credit risk, including those fully secured by subsidiary bank certificates of deposit and U.S. government securities.

2. Superior Quality (Pass) – loans with very strong credit quality. Borrowers have exceptionally strong earnings, liquidity, capital, cash flow coverage, and management ability. Includes loans secured by high quality marketable securities, certificates of deposit from other institutions, and cash value of life insurance. Also includes loans supported by U.S. government, state, or municipal guarantees.
3. Satisfactory Quality (Pass) – loans with satisfactory credit quality. Established borrowers with satisfactory financial condition, including credit quality, earnings, liquidity, capital and cash flow coverage. Management is capable and

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Nature of Business and Significant Account Policies (continued)

experienced. Collateral coverage and guarantor support, if applicable, are more than adequate. Includes loans secured by personal assets and business assets, including equipment, accounts receivable, inventory, and real estate.

4. Fair Quality (Pass) – loans with moderate but still acceptable credit quality. The primary repayment source remains adequate; however, management's ability to maintain consistent profitability is unproven or uncertain. Borrowers exhibit acceptable leverage and liquidity. May include new businesses with inexperienced management or unproven performance records in relation to peer, or borrowers operating in highly cyclical or declining industries.
5. Early Warning (Pass) – loans where the borrowers have generally performed as agreed, however unfavorable financial trends exist or are anticipated. Earnings may be erratic, with marginal cash flow or declining sales. Borrowers reflect leveraged financial condition and/or marginal liquidity. Management may be new and a track record of performance has yet to be developed. Financial information may be incomplete, and reliance on secondary repayment sources may be increasing.
6. Special Mention – loans where the borrowers exhibit credit weaknesses or unfavorable financial trends requiring close monitoring. Weaknesses and adverse trends are more pronounced than Early Warning loans, and if left uncorrected, may jeopardize repayment according to the contractual terms. Currently, no loss of principal or interest is expected. Borrowers in this category have deteriorated to the point that it would be difficult to refinance with another lender. Special Mention should be assigned to borrowers in turnaround situations. This rating is intended as a transitional rating, therefore, it is generally not assigned to a borrower for a period of more than one year.
7. Substandard – loans which are inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if applicable. These loans have a well-defined weakness or weaknesses which jeopardize repayment according to the contractual terms. There is distinct loss potential if the weaknesses are not corrected. Includes loans with insufficient cash flow coverage which are collateral dependent, other real estate owned, and repossessed assets.
8. Doubtful – loans which have all the weaknesses inherent in a Substandard loan, with the added characteristic that existing weaknesses make full principal collection, on the basis of current facts, conditions and values, highly doubtful. The possibility of loss is extremely high, but because of pending factors, recognition of a loss is deferred until a more exact status can be determined. All doubtful loans will be placed on non-accrual, with all payments, including principal and interest, applied to principal reduction

The Company has certain loans risk-rated 7 (substandard), which are not classified as impaired based on the facts of the credit. For these non-impaired and risk-rated 7 loans, the Company does not follow the same allowance methodology as it does for all other non-impaired, collectively evaluated loans. Rather, the Company performs a more detailed analysis including evaluation of the cash flow and collateral valuations. Based upon this evaluation, an estimate of the probable loss in this portfolio is collectively evaluated under ASC 450 20. These non-impaired risk-rated 7 loans exist primarily in the C&I and CRE segments.

For term C&I and CRE loans greater than $1,000,000, a loan review is required within 15 months of the most recent credit review. The review is completed in enough detail to, at a minimum, validate the risk rating. Additionally, the review shall include an analysis of debt service requirements, covenant compliance, if applicable, and collateral adequacy. The frequency of the review is generally accelerated for loans with poor risk ratings.

The Company's Loan Quality area performs a documentation review of a sampling of C&I and CRE loans, the primary purpose of which is to ensure the credit is properly documented and closed in accordance with approval authorities and conditions. A review is also performed by the Company's Internal Audit Department of a sampling of C&I and CRE loans for proper documentation, according to an approved schedule. Validation of the risk rating is also part of Internal Audit's review (performed by Internal Loan Review). Additionally, over the past several years, the Company has contracted an

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Nature of Business and Significant Account Policies (continued)

independent outside third party to review a sampling of C&I and CRE loans. Validation of the risk rating is part of this review as well.

The Company leases machinery and equipment to C&I customers under direct financing leases. All lease requests are subject to the credit requirements and criteria as set forth in the lending/leasing policy. In all cases, a formal independent credit analysis of the lessee is performed.

For direct financing leases, the allowance consists of specific and general components.

The specific component relates to leases that are classified as impaired, as defined for commercial loans above. For those leases that are classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired lease is lower than the carrying value of that lease.

The general component consists of quantitative and qualitative factors and covers nonimpaired leases. The quantitative factors are based on historical charge-off experience for the entire lease portfolio. The qualitative factors are determined based on an assessment of internal and/or external influences on credit quality that are not fully reflected in the historical loss data.

Generally, the Company’s residential real estate loans conform to the underwriting requirements of Freddie Mac and Fannie Mae to allow the subsidiary banks to resell loans in the secondary market. The subsidiary banks structure most loans that will not conform to those underwriting requirements as adjustable rate mortgages that mature or adjust in one to five years or fixed rate mortgages that mature in 15 years, and then retain these loans in their portfolios. Servicing rights are not presently retained on the loans sold in the secondary market. The Company’s lending policy establishes minimum appraisal and other credit guidelines.

The Company provides many types of installment and other consumer loans including motor vehicle, home improvement, home equity, signature loans and small personal credit lines. The Company’s lending policy addresses specific credit guidelines by consumer loan type.

For residential real estate loans, and installment and other consumer loans, these large groups of smaller balance homogenous loans are collectively evaluated for impairment. The Company applies a quantitative factor based on historical charge-off experience in total for each of these segments. Accordingly, the Company generally does not separately identify individual residential real estate loans, and/or installment or other consumer loans for impairment disclosures, unless such loans are the subject of a restructuring agreement due to financial difficulties of the borrower.

TDRs are considered impaired loans/leases and are subject to the same allowance methodology as described above for impaired loans/leases by portfolio segment. Once a loan is classified as a TDR, it will remain a TDR until the loan is paid off, charged off, moved to OREO or restructured into a new note without a concession. TDR status may also be removed if the TDR was restructured in a prior calendar year, is current, accruing interest and shows sustained performance.

Credit related financial instruments: In the ordinary course of business, the Company has entered into commitments to extend credit and standby letters of credit. Such financial instruments are recorded when they are funded.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Nature of Business and Significant Account Policies (continued)

Transfers of financial assets: Transfers of financial assets are accounted for as sales only when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when: (1) the assets have been isolated from the Company, (2) the transferee obtains the right to pledge or exchange the assets it received, and no condition both constrains the transferee from taking advantage of its right to pledge or exchange and provides more than a modest benefit to the transferor, and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity or the ability to unilaterally cause the holder to return specific assets. In addition, for transfers of a portion of financial assets (for example, participations of loan receivables), the transfer must meet the definition of a “participating interest” in order to account for the transfer as a sale. Following are the characteristics of a “participating interest”:

- Pro-rata ownership in an entire financial asset.
- From the date of the transfer, all cash flows received from entire financial assets are divided proportionately among the participating interest holders in an amount equal to their share of ownership.
- The rights of each participating interest holder have the same priority, and no participating interest holder’s interest is subordinated to the interest of another participating interest holder. That is, no participating interest holder is entitled to receive cash before any other participating interest holder under its contractual rights as a participating interest holder.
- No party has the right to pledge or exchange the entire financial asset unless all participating interest holders agree to pledge or exchange the entire financial asset.

BOLI: BOLI is carried at cash surrender value with increases/decreases reflected as income/expense in the statement of income.

Premises and equipment: Premises and equipment are stated at cost less accumulated depreciation. Depreciation is computed primarily by the straight-line method over the estimated useful lives of the assets.

Restricted investment securities: Restricted investment securities represent FHLB and FRB common stock. The stock is carried at cost. These equity securities are “restricted” in that they can only be sold back to the respective institution or another member institution at par. Therefore, they are less liquid than other tradable equity securities. The Company views its investment in restricted stock as a long-term investment. Accordingly, when evaluating for impairment, the value is determined based on the ultimate recovery of the par value, rather than recognizing temporary declines in value. There have been no other-than-temporary write-downs recorded on these securities.

OREO: Real estate acquired through, or in lieu of, loan foreclosures, is held for sale and initially recorded at fair value less costs to sell, establishing a new cost basis. Any writedown to fair value taken at the time of foreclosure is charged to the allowance. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less costs to sell. Subsequent write-downs to fair value are charged to earnings.

Repossessed assets: Equipment or other non-real estate property acquired through, or in lieu of foreclosure, is held for sale and initially recorded at fair value less costs to sell. Repossessed assets are included in other assets on the consolidated balance sheets.

Goodwill: The Company has recorded goodwill from various business combinations. The goodwill is not being amortized, but is evaluated at least annually for impairment. An impairment charge is recognized when the calculated fair value of the reporting unit, including goodwill, is less than its carrying amount. Based on the annual analysis completed as of September 30, 2018, which used a quantitative approach, the Company determined that the goodwill was not impaired. See Note 2 to the Consolidated Financial Statements for additional information.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Nature of Business and Significant Account Policies (continued)

Core deposit intangible: The Company has recorded a core deposit intangible from historical acquisitions including CNB, CSB and Guaranty Bank, and from its merger with Springfield Banchshares. The core deposit intangible was the portion of the acquisition purchase price which represented the value assigned to the existing deposit base at acquisition. See Notes 2 and 6 to the Consolidated Financial Statements for additional information. The core deposit intangibles have a finite life and are amortized over the estimated useful life of the deposits (estimated to be ten years).

Customer list intangible: The Company has recorded a customer list intangible from the Bates Companies acquisition. The customer list intangible was the portion of the acquisition purchase price which represented the value assigned to the existing customer base at acquisition. See Notes 2 and 6 to the Consolidated Financial Statements for addition information. The customer list intangible has a finite life and will be amortized over the estimated useful life (estimated to be fifteen years).

Swap transactions: The Company offers a loan swap program to certain commercial loan customers. Through this program, the Company originates a variable rate loan with the customer. The Company and the swap customer will then enter into a fixed interest rate swap. Lastly, an identical offsetting swap is entered into by the Company with a counterparty. These “back-to-back” swap arrangements are intended to offset each other and allow the Company to book a variable rate loan, while providing the customer with a contract for fixed interest payments. In these arrangements, the Company’s net cash flow is equal to the interest income received from the variable rate loan originated with the customer. These customer swaps are not designated as hedging instruments and are recorded at fair value in other assets and other liabilities. Additionally, the Company receives an upfront fee from the counterparty, dependent upon the pricing that is recognized upon receipt from the counterparty. Swap fee income totaled $10.8 million, $3.1 million and $1.7 million for the years ending December 31, 2018, 2017 and 2016, respectively.

Derivatives and hedging activities: The Company enters into derivative financial instruments as part of its strategy to manage its exposure to changes in interest rates.

Derivative instruments represent contracts between parties that result in one party delivering cash to the other party based on a notional amount and an underlying index (such as a rate, security price or price index) as specified in the contract. The amount of cash delivered from one party to the other is determined based on the interaction of the notional amount of the contract with the underlying index.

The derivative financial instruments currently used by the Company to manage its exposure to interest rate risk include: (1) interest rate lock commitments provided to customers to fund certain mortgage loans to be sold into the secondary market (although this type of derivative is negligible); (2) interest rate caps to manage the interest rate risk of certain short-term fixed rate liabilities; and (3) interest rate swaps on variable rate trust preferred securities.

Interest rate caps and interest rate swaps are valued by the transaction counterparty on a monthly basis and corroborated by a third party annually. The company uses the hypothetical derivative method to assess and measure effectiveness in accordance with ASC 815, Derivatives and Hedging.

Preferred stock: The Company currently has 250,000 shares of preferred stock authorized, but none outstanding as of December 31, 2018 and 2017. Should the Company have preferred stock outstanding in the future, dividends declared on those shares would be deducted from net income to arrive at net income available to common stockholders. Net income available to common stockholders would then be used in the earnings per share computation

Stock-based compensation plans: The Company accounts for stock-based compensation with measurement of compensation cost for all stock-based awards at fair value on the grant date and recognition of compensation over the requisite service period for awards expected to vest.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Nature of Business and Significant Account Policies (continued)

As discussed in Note 15, during the years ended December 31, 2018, 2017, and 2016, the Company recognized stock-based compensation expense for the grant-date fair value of stock based awards that are expected to vest over the requisite service period of $1,443,346, $1,187,036 and $947,174, respectively. As required, management made an estimate of expected forfeitures and is recognizing compensation costs only for those equity awards expected to vest.

The Company uses the Black-Scholes option pricing model to estimate the fair value of stock option grants with the following assumptions for the indicated periods:

	2018	2017	2016
Dividend yield	0.45% to 0.48%	0.36% to 0.47%	0.35% to 0.51%
Expected volatility	29.51% to 29.59%	29.64% to 29.95%	29.32% to 29.37%
Risk-free interest rate	2.60% to 2.94%	2.50% to 2.81%	1.73% to 2.18%
Expected life of option grants (in years)	6 years	6 years	6 years
Weighted-average grant date fair value	$ 14.68	$ 14.75	$ 7.31

The Company also uses the Black-Scholes option pricing model to estimate the fair value of stock purchase grants with the following assumptions for the indicated periods:

	2018	2017	2016
Dividend yield	0.37% to 0.51%	0.37% to 0.42%	0.33% to 0.59%
Expected volatility	20.90% to 21.40%	19.80% to 19.86%	12.70% to 15.60%
Risk-free interest rate	1.59% to 2.22%	0.67% to 1.18%	0.39% to 0.57%
Expected life of purchase grants (in months)	3 to 6 months	3 to 6 months	3 to 6 months
Weighted-average grant date fair value	$ 6.63	$ 6.42	$ 3.28

The fair value is amortized on a straight-line basis over the vesting periods of the grants and will be adjusted for subsequent changes in estimated forfeitures. The expected dividend yield assumption is based on the Company's current expectations about its anticipated dividend policy. Expected volatility is based on historical volatility of the Company's common stock price. The risk-free interest rate for periods within the contractual life of the option or purchase is based on the U.S. Treasury yield curve in effect at the time of the grant. The expected life of the option and purchase grants is derived using the "simplified" method and represents the period of time that options and purchases are expected to be outstanding. Historical data is used to estimate forfeitures used in the model. Two separate groups of employees (employees subject to broad based grants, and executive employees and directors) are used.

As of December 31, 2018, there was $704,659 of unrecognized compensation cost related to stock options granted, which is expected to be recognized over a weighted average period of 1.66 years.

The aggregate intrinsic value is calculated as the difference between the exercise price of the underlying awards and the quoted price of the Company's common stock for the 411,030 options that were in-the-money at December 31, 2018. The aggregate intrinsic value at December 31, 2018 was $7.1 million on options outstanding and $6.3 million on options exercisable. During the years ended December 31, 2018, 2017 and 2016, the aggregate intrinsic value of options exercised under the Company's stock option plans was $365,107, $1,005,193, and $1,525,902, respectively, and determined as of the date of the option exercise.

Restricted stock awards granted may not be sold or otherwise transferred until the service periods have lapsed. During the vesting periods, participants have voting rights and receive dividends. Upon termination of employment, common shares upon which the service periods have not lapsed must be returned to the Company.

All restricted share awards are classified as equity awards. The grant-date fair value of equity-classified restricted stock awards is amortized as compensation expense on a straight-line basis over the period restrictions lapse.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Nature of Business and Significant Account Policies (continued)

As of December 31, 2018, there was $1,976,929 of unrecognized compensation cost related to nonvested restricted stock awards expected to be recognized over a period of 1.51 years.

Income taxes: The Company files its tax return on a consolidated basis with its subsidiaries. The entities follow the direct reimbursement method of accounting for income taxes under which income taxes or credits which result from the inclusion of the subsidiaries in the consolidated tax return are paid to or received from the parent company.

Deferred income taxes are provided under the liability method whereby deferred tax assets are recognized for deductible temporary differences and net operating loss and tax credit carryforwards and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax basis. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some or all of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

When tax returns are filed, it is highly certain that some positions taken would be sustained upon examination by the taxing authorities, while others are subject to uncertainty about the merits of the position taken or the amount of the position that would be ultimately sustained. The benefit of a tax position is recognized in the financial statements in the period during which, based on all available evidence, management believes it is more likely than not that the position will be sustained upon examination, including the resolution of appeals or litigation processes, if any. Tax positions taken are not offset or aggregated with other positions. Tax positions that meet the more likely than not recognition threshold are measured as the largest amount of tax benefit that is more than 50 percent likely of being realized upon settlement with the applicable taxing authority. The portion of the benefits associated with tax positions taken that exceeds the amount measured as described above is reflected as a liability for unrecognized tax benefits in the accompanying balance sheet along with any associated interest and penalties that would be payable to the taxing authorities upon examination.

Interest and penalties associated with unrecognized tax benefits are classified as additional income taxes in the statements of income.

Trust assets: Trust assets held by the subsidiary banks in a fiduciary, agency, or custodial capacity for their customers, other than cash on deposit at the subsidiary banks, are not included in the accompanying Consolidated Financial Statements since such items are not assets of the subsidiary banks.

Earnings per share: See Note 17 for a complete description and calculation of basic and diluted earnings per share.

Revenue Recognition: As of January 1, 2018, the Company adopted ASU 2014 09 using the modified retrospective approach. The adoption of the guidance had no material impact on the measurement or recognition of revenue as approximately 89% of the Company's revenue (based on 2017 audited financial results) is outside the scope of this guidance; however, additional disclosures have been added in accordance with the ASU.

Descriptions of our revenue-generating contracts with customers that are within the scope of ASU 2014 09, which are presented in our income statements as components of non-interest income are as follows:

Trust department and Investment advisory and management fees: This is a contract between the Company and its customers for fiduciary and/or investment administration services on trust and brokerage accounts. Trust services and brokerage fee income is determined as a percentage of assets under management and is recognized over the period the underlying trust account is serviced. Such contracts are generally cancellable at any time, with the customer subject to a pro-rated fee in the month of termination.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Nature of Business and Significant Account Policies (continued)

Deposit service fees: The deposit contract obligates the Company to serve as a custodian of the customer's deposited funds and is generally terminable at will by either party. The contract permits the customer to access the funds on deposit and request additional services related to the deposit account. Deposit account related fees, including analysis charges, overdraft/nonsufficient fund charges, service charges, debit card usage fees, overdraft fees and wire transfer fees are within the scope of the guidance; however, revenue recognition practices did not change under the guidance, as deposit agreements are considered day-to-day contracts. Income for deposit accounts is recognized over the statement cycle period (typically on a monthly basis) or at the time the service is provided, if additional services are requested.

Correspondent banking fees: A contract between the Company and its correspondent banks for corresponding banking services. This line of business provides a strong source of noninterest bearing and interest bearing deposits, fee income, high-quality loan participations and bank stock loans. Correspondent banking fee income is tied to transaction activity and revenue is recognized monthly as earned for services provided.

Reclassifications: Certain amounts in the prior year’s Consolidated Financial Statements have been reclassified, with no effect on net income or stockholders’ equity, to conform with the current period presentation.

New Accounting Prounouncement: In May 2014, FASB issued ASU 2014 09, Revenue from Contracts with Customers. ASU 2014 09 implements a common revenue standard that clarifies the principles for recognizing revenue. The core principle of ASU 2014 09 is that an entity should recognize 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. To achieve that core principle, 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. ASU 2014 09 was originally effective for the Company on January 1, 2018, however, FASB issued ASU 2015 14 which deferred the effective date in order to provide additional time for both public and private entities to evaluate the impact. ASU 2014 09 was adopted by the Company on January 1, 2018 and had no significant impact on the Company’s Consolidated Financial Statements.

In January 2016, FASB issued ASU 2016 01, Financial Instruments – Overall. ASU 2016 01 makes targeted adjustments to GAAP by eliminating the available for sale classification for equity securities and requiring equity investments to be measured at fair value with changes in fair value recognized in net income. The standard also requires public business entities to use the exit price notion when measuring fair value of financial instruments for disclosure purposes. The standard clarifies that an 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. It also requires an entity to present separately (within 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. Additionally, the standard eliminates the requirement for public business 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. ASU 2016-01 was adopted by the Company on January 1, 2018 and had no significant impact on the

Company’s Consolidated Financial Statements.

In February 2016, the FASB issued ASU 2016 02, Leases. Under ASU 2016 02, lessees will be required to recognize a lease liability measured on a discounted basis and a right-of-use asset for all leases (with the exception of short-term leases). Lessor accounting is largely unchanged under ASU 2016 02. However, the definition of initial direct costs was updated to include only initial direct costs that are considered incremental. This change in definition will change the manner in which the Company recognizes the costs associated with originating leases. ASU 2016 02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted for all entities. The standard was adopted on January 1, 2019 and is expected to have no significant impact on the Company’s Consolidated Financial Statements.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Nature of Business and Significant Account Policies (continued)

In June 2016, the FASB issued ASU 2016 13, Financial Instruments – Credit Losses. Under the standard, assets measured at amortized cost (including loans, leases and AFS securities) will be presented at the net amount expected to be collected. Rather than the "incurred" model that is currently being utilized, the standard will require the use of a forward-looking approach to recognizing all expected credit losses at the beginning of an asset's life. For public companies, ASU 2016 13 is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Companies may choose to early adopt for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. The Company is in the process of analyzing the impact of adoption on the Company's Consolidated Financial Statements.

In January 2017, the FASB issued ASU 2017-04, Intangibles - Goodwill and Other (Topic 350). ASU 2017-04 is intended to simplify goodwill impairment testing by eliminating the second step of the analysis. ASU 2017-04 requires entities to compare the fair value of a reporting unit with its carrying amount and recognize an impairment charge for any amount by which the carrying amount exceeds the reporting unit's fair value, to the extent that the loss recognized does not exceed the amount of goodwill allocated to that reporting unit. This guidance is effective for annual and interim periods beginning after December 15, 2019, with early adoption permitted. The Company does not expect this guidance to have a significant impact on its Consolidated Financial Statements.

In February 2018, the FASB issued ASU 2018 02, Income Statement – Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income. Under the standard, entities are allowed to make a one-time reclassification from AOCI to retained earnings for the effect of remeasuring deferred tax liabilities and assets originally recorded in other comprehensive income as a result of the change in the federal tax rate as defined by the Tax Act. ASU 2018 02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those years. Companies may choose to early adopt for fiscal years or interim periods that have not been issued or made available for issuance as of February 14, 2018. The Company chose to early adopt ASU 2018 02 and apply the guidance to the Consolidated Financial Statements for the year ended December 31, 2017. The reclassification from AOCI to retained earnings for 2017 totaled $304 thousand and is presented in the Consolidated Statements of changes in Stockholders' Equity.

Note 2. Mergers/Acquisitions

General

The narrative in this subsection applies to all mergers and acquisitions detailed throughout this footnote.

Loans acquired in a business combination are recorded and initially measured at their estimated fair value as of the acquisition date. Credit discounts are included in the determination of fair value. A third party valuation consultant assisted with the determination of fair value.

Purchased loans are segregated into two categories: PCI loans and non-PCI (performing) loans. PCI loans are accounted for in accordance with ASC 310 30, as they display significant credit deterioration since origination and it is probable, as of the acquisition date, that the Company will be unable to collect all contractually required payments from the borrower. Performing loans are accounted for in accordance with ASC 310 20, as these loans do not have evidence of significant credit deterioration since origination and it is probable that the contractually required payments will be received from the borrower.

For PCI loans, the difference between the contractually required payments at acquisition and the cash flows expected to be collected is referred to as the non-accretable discount. Further, any excess cash flows expected at acquisition over the estimated fair value is referred to as the accretable yield and is recognized in interest income over the expected remaining life of the loan. Subsequent to the purchase date, increases in cash flows over those expected at the purchase date are recognized as interest income prospectively. The present value of any decreases in expected cash flows after the purchase date is recognized by recording an allowance for loan and lease losses and provision for loan losses.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 2. Mergers/Acquisitions (continued)

For performing loans, the difference between the estimated fair value of the loans and the principal balance outstanding is accreted over the remaining life of the loans.

Bates Companies

On October 1, 2018, the Company acquired the Bates Companies, headquartered in Rockford, Illinois. The acquisition enhanced the wealth management services of the Company by adding approximately $704 million of assets under management at acquisition. In the acquisition, the Company acquired 100% of the Bates Companies' outstanding common stock for aggregate consideration of $3.0 million cash and up to $3.0 million of the Company's common stock. Of the total cash consideration, $1.5 million in cash was paid at closing funded through operating cash. The additional $1.5 million was recorded as a promissory note and will be repaid in five equal, annual installments of $300,000 each on the first through fifth anniversaries of the closing date. Interest will be paid at a rate of 2.18% per annum, based on the applicable federal rate as of the closing date. This $1.5 million promissory note is included in Other Liabilities on the Consolidated Balance Sheet. Additionally, in a private placement exempt from registration with the SEC, the Company issued 23,501 shares of Company stock in December 2018. Assuming all future performance based targets are met, total stock consideration can reach $3.0 million, which would result in the Company issuing approximately 47,003 additional common shares based on the 10-day volume weighted average of the closing stock price of the Company ending five days prior to closing. The contingent consideration for the additional common shares, totaling $2.0 million, is included in Other Liabilities on the Consolidated Balance Sheet.

During 2018, the Company incurred $394 thousand of expenses related to the acquisition, comprised primarily of legal and accounting costs.

The Company recorded estimates for the customer list intangible and goodwill during 2018, as purchase accounting calculations were not yet complete. The Company expects the initial purchase accounting to be complete in the first quarter of 2019. The Company recorded a customer list intangible totaling $1,854,932 which is the portion of the acquisition purchase price which represents the value assigned to the existing customer base. The customer list intangible has a finite life and is amortized over the estimated useful life of the customer base. The Company recorded goodwill totaling $3,766,074 which is the excess of the consideration paid over the fair value of the net assets acquired. This goodwill is not deductible for tax purposes. See Note 6 to the Consolidated Financial Statements for additional information.

The Company accounted for the business combination under the acquisition method of accounting in accordance with ASC 805. The Company recognized the full fair value of the assets acquired and liabilities assumed at the acquisition date, net of applicable income tax effects.The Company considers all purchase accounting adjustments as provisional and fair values are subject to refinement for up to one year after the closing date.

Unaudited pro forma combined operating results for the years ended December 31, 2018 and 2017, giving effect to the Bates Companies acquisition as if it had occurred as of January 1, 2017, are as follows:

	Year Ended December 31,	
	2018	2017
	(dollars in thousands, except per share data)	
Net interest income	$ 142,368	$ 116,029
Noninterest income	$ 44,455	$ 33,044
Net income	$ 44,032	$ 35,627
Earnings per common share:		
Basic	$ 2.98	$ 2.67
Diluted	$ 2.92	$ 2.60

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 2. Mergers/Acquisitions (continued)

The pro forma results do not purport to be indicative of the results of operations that actually would have resulted had the acquisition occurred on January 1, 2017 or of future results of operations of the consolidated entities.

Springfield Bancshares, Inc.

On July 1, 2018, the Company merged with Springfield Bancshares, the holding company of SFC Bank, headquartered in Springfield, Missouri. The Company acquired 100% of Springfield Bancshares common stock in the merger. SFC Bank is a Missouri-chartered bank that operates one location in the Springfield, Missouri market. As a result of the transaction, SFC Bank became the Company's fifth independent charter.

The merger with Springfield Bancshares allowed the Company to enter the Springfield, Missouri market which is consistent with the Company's strategic plan to selectively acquire other high-performing financial institutions in vibrant mid-sized metropolitan markets with a high concentration of commercial clients. Financial metrics related to the transaction were favorable, as measured by EPS and ROAA accretion.

Stockholders of Springfield Bancshares received 0.3060 shares of the Company's common stock and $1.50 in cash in exchange for each common share of Springfield Bancshares held. On June 29, 2018, the last trading date before the closing, the Company's common stock closed at $47.45, resulting in stock consideration valued at $80.6 million and total consideration paid by the Company of $89.0 million. To help fund the cash portion of the purchase price, on June 29, 2018, the Company borrowed $4.1 million on its existing $10.0 million revolving line of credit. The Company also borrowed $4.9 million on this same revolving line of credit to fund the repayment of certain debt assumed in the merger shortly after closing. This note is included within Other Borrowings on the Consolidated Balance Sheets. The remaining cash consideration paid to the shareholders of Springfield Bancshares came from operating cash.

The Company accounted for the business combination under the acquisition method of accounting in accordance with ASC 805. The Company recognized the full fair value of the assets acquired and liabilities assumed at the merger date, net of applicable income tax effects. The Company considers all purchase accounting adjustments as provisional and fair values are subject to refinement for up to one year after the closing date.

During the fourth quarter of 2018, various measurement period adjustments were made. The result of these adjustments was an increase to goodwill of $447 thousand.

The excess of the consideration paid over the fair value of the net assets acquired is recorded as goodwill. This goodwill is not deductible for tax purposes.

The fair values of the assets acquired and liabilities assumed, after measurement period adjustments to date, including the consideration paid and resulting goodwill is as follows.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 2. Mergers/Acquisitions (continued)

	As of July 1, 2018
ASSETS	
Cash and due from banks	$ 4,586,326
Interest-bearing deposits at financial institutions	62,924,396
Securities	4,845,441
Loans/leases receivable, net	477,336,699
Bank-owned life insurance	7,091,883
Premises and equipment	6,091,978
Restricted investment securities	3,654,200
Intangibles	8,208,728
Other assets	1,470,689
Total assets acquired	$ 576,210,340
LIABILITIES	
Deposits	$ 439,579,328
Short-term borrowings	1,143,478
FHLB advances	74,539,463
Other borrowings	9,543,810
Other liabilities	8,408,463
Total liabilities assumed	$ 533,214,542
Net assets acquired	$ 42,995,798
CONSIDERATION PAID:	
Cash	$ 8,333,535
Common stock	80,637,194
Total consideration paid	$ 88,970,729
Goodwill	$ 45,974,931

The following table presents the purchased loans as of the merger date:

	PCI Loans	Performing Loans	Total
Contractually required principal payments	$ 7,552,912	$ 479,439,547	$ 486,992,459
Nonaccretable discount	(1,562,455)	—	(1,562,455)
Principal cash flows expected to be collected	$ 5,990,457	$ 479,439,547	$ 485,430,004
Accretable discount	(293,445)	(7,799,860)	(8,093,305)
Fair Value of acquired loans	$ 5,697,012	$ 471,639,687	$ 477,336,699

Changes in accretable yield for the loans acquired are as follows:

	For the year ended December 31, 2018		
	PCI Loans	Performing Loans	Total
Discount added at acquisition	$ (293,445)	$ (7,799,860)	$ (8,093,305)
Reclassification of nonaccretable discount to accretable	(891,569)	—	(891,569)
Accretion recognized	525,704	1,950,795	2,476,499
Balance at the end of the period	$ (659,310)	$ (5,849,065)	$ (6,508,375)

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 2. Mergers/Acquisitions (continued)

During 2018, there was no nonaccretable discount that was recognized due to the repayment of PCI loans. However, $892 thousand of nonaccretable discount was reclassified to accretable during the third quarter of 2018 due to significant improvement on one specific credit subsequent to the merger date. Of this amount, $396 thousand was accreted to income in 2018, while the remainder will be accreted over the next 8 months, which is the remaining contractual life of the loan.

Premises and equipment acquired with a fair value of $6.1 million includes one branch location. The fair value was determined with the assistance of a third party appraiser. The buildings and building write-ups will be recognized in depreciation expense over 39 years.

The Company recorded a core deposit intangible totaling $8.2 million which is the portion of the merger purchase price which represents the value assigned to the existing deposit base. The core deposit intangible has a finite life and is amortized using an accelerated method over the estimated useful life of the deposits (estimated to be ten years). See Note 6 to the Consolidated Financial Statements for additional information.

FHLB advances and other borrowings assumed with a fair value of $84.1 million included $40.0 million in overnight FHLB advances, $34.5 million of FHLB term advances, $4.7 million in subordinated debentures and a $4.8 million bank stock loan. The $4.8 million bank stock loan was paid off immediately after the merger date on July 2, 2018, at its book value. See Note 10 and 11 to the Consolidated Financial Statements for additional information.

During 2018, the Company incurred $1.4 million of expenses related to the merger comprised primarily of legal, accounting, and investment banking costs. These costs are presented on their own line within the consolidated statements of income. SFC Bank results are included in the consolidated statements of income effective on the merger date. For the period July 1, 2018 to December 31, 2018, SFC Bank reported revenues of $15.2 million and net income of $4.8 million, which included $391 thousand of after tax post-acquisition, compensation, transition and integration costs.

Unaudited pro forma combined operating results for the years ended December 31, 2018 and 2017, giving effect to the merger with Springfield Bancshares as if it had occurred as of January 1, 2017, are as follows:

	Year Ended December 31,	
	2018	2017
	(dollars in thousands, except per share data)	
Net interest income	$ 153,229	$ 136,190
Noninterest income	$ 42,538	$ 32,395
Net income	$ 49,542	$ 42,316
Earnings per common share:		
Basic	$ 3.17	$ 2.82

Diluted	$ 3.11	$ 2.75

The pro forma results do not purport to be indicative of the results of operations that actually would have resulted had the merger occurred on January 1, 2017 or of future results of operations of the consolidated entities.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 2. Mergers/Acquisitions (continued)

Guaranty Bank and Trust

On October 1, 2017 the Company acquired Guaranty Bank, headquartered in Cedar Rapids, Iowa, from Guaranty. Guaranty Bank is an Iowa-chartered bank that operates five banking locations throughout the Cedar Rapids metropolitan area.

The acquisition of Guaranty Bank allowed the Company to grow its market share in the Cedar Rapids market. Guaranty Bank has a strong core deposit base and retail franchise. Although Guaranty already had strong earnings, the Company has identified several opportunities for enhanced future earnings performance. Lastly, financial metrics related to the transaction were favorable, as measured by EPS accretion, ROAA accretion and earn back of tangible book value dilution.

In the acquisition, the Company acquired 100% of Guaranty Bank's outstanding common stock and purchased certain assets and assumed certain liabilities of Guaranty for aggregate consideration consisting of 79% QCR Holdings common stock (678,670 shares) and 21% cash ($7.8 million). On September 29, 2017, the last trading date before the closing, the Company's common stock closed at $45.50, resulting in stock consideration valued at $30.9 million and total consideration paid by the Company of $38.7 million.

To help fund the cash portion of the purchase price, on September 27, 2017, the Company executed a $7.0 million four-year term note with principal and interest due quarterly. See further information in Note 11. This note is included within other borrowings on the December 31, 2017 Consolidated Balance Sheets. The remaining cash consideration paid to Guaranty came from operating cash.

The Company accounted for the business combination under the acquisition method of accounting in accordance with ASC 805. The Company recognized the full fair value of the assets acquired and liabilities assumed at the acquisition date, net of applicable income tax effects. The Company considers all purchase accounting adjustments to be finalized.

The excess of the consideration paid over the fair value of the net assets acquired is recorded as goodwill. This goodwill is deductible over 15 years for tax purposes.

The Company has several areas of specialization, including government guaranteed lending, C&I lending, interest rate swaps, leasing, wealth management, private banking and municipal bond offerings that will be offered in this expanded market, increasing future earnings potential. Guaranty Bank has a strong core deposit base. There is also value added to the Company through having an expanded footprint in a market that has strong growth potential. The experience and value of the personnel at Guaranty Bank and their knowledge of the expanded market is also beneficial.

On December 2, 2017, the Company merged Guaranty Bank with and into CRBT, with CRBT as the surviving bank. As part of the merger, the Guaranty Bank branches located at 302 3rd Avenue SE, Cedar Rapids, Iowa and 1819 42nd Street NE, Cedar Rapids, Iowa, permanently closed. The three remaining Guaranty Bank branches have become

banking offices of CRBT.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 2. Mergers/Acquisitions (continued)

The fair values of the assets acquired and liabilities assumed including the consideration paid and resulting goodwill is as follows:

	As of October 1, 2017
ASSETS	
Cash and due from banks	$ 4,434,511
Interest-bearing deposits at financial institutions	3,953,907
Securities	49,703,419
Loans/leases receivable, net	192,517,677
Premises and equipment	4,808,343
Restricted investment securities	476,500
Core deposit intangible	2,698,301
Other assets	997,810
Total assets acquired	$ 259,590,468
LIABILITIES	
Deposits	$ 212,467,514
Short-term borrowings	13,102,043
FHLB advances	4,108,027
Junior subordinated debentures	3,857,275
Other liabilities	2,595,883
Total liabilities assumed	$ 236,130,742
Net assets acquired	$ 23,459,726
CONSIDERATION PAID:	
Cash	$ 7,803,420
Common stock	30,879,485
Total consideration paid	$ 38,682,905
Goodwill	$ 15,223,179

The following table presents the purchased loans as of the acquisition date:

	PCI Loans	Performing Loans	Total
Contractually required principal payments	$ 3,126,327	$ 192,982,439	$ 196,108,766
Nonaccretable discount	(1,147,198)	—	(1,147,198)
Principal cash flows expected to be collected	$ 1,979,129	$ 192,982,439	$ 194,961,568

Accretable discount	(219,902)	(2,223,989)	(2,443,891)
Fair Value of acquired loans	$ 1,759,227	$ 190,758,450	$ 192,517,677

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 2. Mergers/Acquisitions (continued)

Changes in accretable yield for the loans acquired are as follows:

	For the year ended December 31, 2018		
	PCI Loans	Performing Loans	Total
Balance at the beginning of the period	$ (165,832)	$ (2,197,153)	$ (2,362,985)
Accretion recognized	157,775	584,563	742,338
Balance at the end of the period	$ (8,057)	$ (1,612,590)	$ (1,620,647)

	For the year ended December 31, 2017		
	PCI Loans	Performing Loans	Total
Balance at the beginning of the period	$ —	$ —	$ —
Discount added at acquisition	(219,902)	(2,223,989)	(2,443,891)
Accretion recognized	54,070	26,836	80,906
Balance at the end of the period	$ (165,832)	$ (2,197,153)	$ (2,362,985)

During 2018 and 2017, there was also $137 thousand and $158 thousand, respectively, of nonaccretable discount that was recognized due to the repayment of PCI loans.

Premises and equipment acquired with a fair value of $4.8 million includes five branch locations with a fair value of $4.6 million. The fair value was determined with the assistance of a third party appraiser. The buildings and related fair value adjustments will be recognized in depreciation expense over 39 years.

The Company recorded a core deposit intangible totaling $2.7 million which is the portion of the acquisition purchase price which represents the value assigned to the existing deposit base. The core deposit intangible has a finite life and is amortized using an accelerated method over the estimated useful life of the deposits (estimated to be ten years). See Note 6 to the Consolidated Financial Statements for additional information.

During 2017, the Company incurred $805 thousand of expenses related to the acquisition, comprised primarily of legal, accounting and investment banking costs. These acquisition costs are presented on their own line within the consolidated statements of income. Also during 2017, the Company incurred $3.1 million of post-acquisition expenses, comprised primarily of personnel costs, IT integration, and conversion costs. Guaranty Bank results are included in the consolidated statements of income effective on the acquisition date.

Unaudited pro forma combined operating results for the years ended December 31, 2017 and 2016, giving effect to the Guaranty Bank acquisition as if it had occurred as of January 1, 2016, are as follows:

	Year Ended December 31,	
	2017	2016
	(dollars in thousands, except per share data)	
Net interest income	$ 122,923	$ 102,902
Noninterest income	$ 32,703	$ 34,238
Net income	$ 38,728	$ 27,103
Earnings per common share:		
Basic	$ 2.80	$ 2.05
Diluted	$ 2.73	$ 2.02

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 2. Mergers/Acquisitions (continued)

The pro forma results do not purport to be indicative of the results of operations that actually would have resulted had the acquisition occurred on January 1, 2016 or of future results of operations of the consolidated entities.

Community State Bank

On August 31, 2016, the Company acquired Community State Bank from Van Diest Investment Company. CSB is headquartered in Ankeny, Iowa and is an Iowa-chartered bank that operates ten banking locations throughout the Des Moines metropolitan area. The Company purchased 100% of the outstanding common stock of CSB for cash consideration of $80.0 million.

The acquisition of CSB allowed the Company to expand its footprint into the Des Moines market. CSB had an experienced and capable leadership team that was committed to leading the Company's efforts in the Des Moines area. CSB had demonstrated significant improvement in earnings and asset quality during the last three years. Additionally, CSB had a strong core deposit base and retail franchise. Although CSB already had strong earnings, the Company had identified several opportunities for enhanced future earnings performance. With $581 million of assets acquired, the Company believed this acquisition was large enough to provide meaningful impact on the financial results, but was not too large to overstrain existing infrastructure. Lastly, financial metrics related to the transaction were favorable, as measured by EPS accretion and earn-back of tangible book value dilution.

In connection with the acquisition, during the second quarter of 2016, the Company sold 1,215,000 shares of its common stock at a price of $24.75 per share, for net proceeds of $29.8 million, after deducting expenses. The shares were offered to institutional investors in a registered direct offering conducted without an underwriter or placement agent. The offering was a partial take-down of a previously filed shelf registration and closed on May 23, 2016.

Cash received from the common stock offering was used to help finance the purchase price of the acquisition. Additionally, the Company drew $5.0 million on its $10.0 million revolving line of credit and fully funded its $30.0 million term facility. Both of these facilities are described further in Note 11 to the Consolidated Financial Statements. Cash dividends of $15.2 million from QCBT and CRBT were used to fund the remainder of the purchase price.

The Company accounted for the business combination under the acquisition method of accounting in accordance with ASC 805. The Company recognized the full fair value of the assets acquired and liabilities assumed at the acquisition date, net of applicable income tax effects.

The excess of the consideration paid over the fair value of the net assets acquired is recorded as goodwill. This goodwill is not deductible for tax purposes.

The Company has several areas of specialization, including government guaranteed lending, C&I lending, interest rate swaps, leasing, wealth management, private banking and municipal bond offerings that will be offered in this new market, increasing future earnings potential. There is also value added to the Company through having a footprint in a market that has strong growth potential. Additionally, there are qualitative benefits gained through the addition of a new charter including better leverage of centralized operations and increased lending limits. The experience and value of the personnel at CSB and their knowledge of the Des Moines MSA is also beneficial.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 2. Mergers/Acquisitions (continued)

The fair values of the assets acquired and liabilities assumed including the consideration paid and resulting goodwill is as follows:

	As of August 31, 2016
ASSETS	
Cash and due from banks	$ 10,094,645
Federal funds sold	698,000
Interest-bearing deposits at financial institutions	14,730,157
Securities	102,640,029
Loans/leases receivable, net	419,029,277
Premises and equipment	20,684,880
Restricted investment securities	1,512,900
Core deposit intangible	6,352,653
Other real estate owned	650,000
Other assets	5,283,937
Total assets acquired	$ 581,676,478
LIABILITIES	
Deposits	$ 486,298,262
FHLB advances	20,368,877
Other liabilities	4,897,564
Total liabilities assumed	$ 511,564,703
Net assets acquired	$ 70,111,775
CONSIDERATION PAID:	
Cash	$ 80,000,000
Total consideration paid	$ 80,000,000
Goodwill	$ 9,888,225

The following table presents the purchased loans as of the acquisition date:

	PCI Loans	Performing Loans	Total
Contractually required principal payments	$ 8,349,688	$ 427,398,400	$ 435,748,088

Nonaccretable discount	(4,525,223)	—	(4,525,223)
Principal cash flows expected to be collected	$ 3,824,465	$ 427,398,400	$ 431,222,865
Accretable discount	(277,579)	(11,916,009)	(12,193,588)
Fair Value of acquired loans	$ 3,546,886	$ 415,482,391	$ 419,029,277

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 2. Mergers/Acquisitions (continued)

Changes in accretable yield for the loans acquired are as follows:

	For the year ended December 31, 2018		
	PCI Loans	Performing Loans	Total
Balance at the beginning of the period	$ (25,300)	$ (4,082,922)	$ (4,108,222)
Accretion recognized	25,300	1,888,043	1,913,343
Balance at the end of the period	$ —	$ (2,194,879)	$ (2,194,879)

	For the year ended December 31, 2017		
	PCI Loans	Performing Loans	Total
Balance at the beginning of the period	$ (194,306)	$ (9,115,614)	$ (9,309,920)
Accretion recognized	169,006	5,032,692	5,201,698
Balance at the end of the period	$ (25,300)	$ (4,082,922)	$ (4,108,222)

	For the year ended December 31, 2016		
	PCI Loans	Performing Loans	Total
Balance at the beginning of the period	$ —	$ —	$ —
Discount added at acquisition	(277,579)	(11,916,009)	(12,193,588)
Accretion recognized	83,273	2,800,395	2,883,668
Balance at the end of the period	$ (194,306)	$ (9,115,614)	$ (9,309,920)

During 2018, 2017 and 2016, there was also $25 thousand, $198 thousand and $186 thousand, respectively, of nonaccretable discount that was recognized due to the repayment of PCI loans.

Premises and equipment acquired with a fair value of $20.7 million includes ten branch locations with a fair value of $19.7 million, including a write-up of $8.3 million. The fair value was determined with the assistance of a third party appraiser. The buildings and building write-ups will be recognized in depreciation expense over 39 years.

The Company recorded a core deposit intangible totaling $6.4 million which is the portion of the acquisition purchase price which represents the value assigned to the existing deposit base. The core deposit intangible has a finite life and is amortized using an accelerated method over the estimated useful life of the deposits (estimated to be ten years). See Note 6 to the Consolidated Financial Statements for additional information.

During 2016, the Company incurred $1.4 million of expenses related to the acquisition, comprised primarily of legal, accounting, and investment banking costs. These acquisition costs are presented on their own line within the consolidated statements of income. Also during 2016, the Company incurred $1.0 million of post-acquisition expenses, comprised primarily of personnel costs, IT integration, and conversion costs. CSB results are included in the consolidated statements of income effective on the acquisition date. For the period August 31, 2016 to December 31, 2016, CSB reported revenues of $11.4 million and net income of $2.1 million, which included $473 thousand of after tax acquisition costs.

During the current year, the Company incurred $1.2 million of post-acquisition compensation, transition and integration costs, comprised entirely of a fee that was paid for a core processor conversion of CSB.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 2. Mergers/Acquisitions (continued)

Unaudited pro forma combined operating results for the year ended December 31, 2016, giving effect to the CSB acquisition as if it had occurred as of January 1, 2015, is as follows:

	Year Ended December 31, 2016 (dollars in thousands, except per share data)
Net interest income	$ 110,035
Noninterest income	$ 34,773
Net income	$ 34,137
Earnings per common share:	
Basic	$ 2.62
Diluted	$ 2.58

The pro forma results do not purport to be indicative of the results of operations that actually would have resulted had the acquisition occurred on January 1, 2015 or of future results of operations of the consolidated entities.

Note 3. Investment Securities

The amortized cost and fair value of investment securities as of December 31, 2018 and 2017 are summarized as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Fair Value
December 31, 2018:				
Securities HTM:				

Municipal securities	$ 400,862,885	$ 5,661,095	$ (6,802,765)	$ 399,721,215
Other securities	1,050,000	—	(632)	1,049,368
	$ 401,912,885	$ 5,661,095	$ (6,803,397)	$ 400,770,583
Securities AFS:				
U.S. govt. sponsored agency securities	$ 37,150,434	$ 38,620	$ (777,663)	$ 36,411,391
Residential mortgage-backed and related securities	163,697,973	181,868	(4,630,581)	159,249,260
Municipal securities	59,069,259	179,748	(702,985)	58,546,022
Other securities	6,754,164	100,700	(5,089)	6,849,775
	$ 266,671,830	$ 500,936	$ (6,116,318)	$ 261,056,448

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Fair Value
December 31, 2017:				
Securities HTM:				
Municipal securities	$ 378,424,205	$ 2,763,718	$ (2,488,119)	$ 378,699,804
Other securities	1,050,000	—	—	1,050,000
	$ 379,474,205	$ 2,763,718	$ (2,488,119)	$ 379,749,804
Securities AFS:				
U.S. govt. sponsored agency securities	$ 38,409,157	$ 37,344	$ (349,967)	$ 38,096,534
Residential mortgage-backed and related securities	165,459,470	155,363	(2,313,529)	163,301,304
Municipal securities	66,176,364	660,232	(211,100)	66,625,496
Other securities	4,014,004	896,384	(25,815)	4,884,573
	$ 274,058,995	$ 1,749,323	$ (2,900,411)	$ 272,907,907

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 3. Investment Securities (continued)

The Company's HTM municipal securities consist largely of private issues of municipal debt. The municipalities are located primarily within the Midwest. The municipal debt investments are underwritten using specific guidelines with ongoing monitoring.

The Company's residential mortgage-backed and related securities portfolio consists entirely of government sponsored or government guaranteed securities. The Company has not invested in commercial mortgage-backed securities or pooled trust preferred securities.

As discussed in Note 1, effective January 1, 2018, equity securities (previously included in other securities) are no longer included in available for sale securities and, instead, are carried in other assets at fair value with changes in fair value recognized in net income.

Gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, as of December 31, 2018 and 2017, are summarized as follows:

	Less than 12 Months		12 Months or More		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
December 31, 2018:						
Securities HTM:						
Municipal securities	$ 114,200,687	$ (2,186,574)	$ 69,412,341	$ (4,616,191)	$ 183,613,028	$ (6,802,765)
Other securities	549,368	(632)	—	—	549,368	(632)
	$ 114,750,055	$ (2,187,206)	$ 69,412,341	$ (4,616,191)	$ 184,162,396	$ (6,803,397)
Securities AFS:						
U.S. govt. sponsored agency securities	$ 1,565,136	$ (33,278)	$ 29,605,388	$ (744,385)	$ 31,170,524	$ (777,663)
Residential mortgage-backed and related securities	12,809,544	(147,592)	133,533,963	(4,482,989)	146,343,507	(4,630,581)
Municipal securities	28,356,204	(394,235)	15,932,376	(308,750)	44,288,580	(702,985)
Other securities	4,249,075	(5,089)	—		4,249,075	(5,089)
	$ 46,979,959	$ (580,194)	$ 179,071,727	$ (5,536,124)	$ 226,051,686	$ (6,116,318)

	Less than 12 Months	12 Months or More	Total

	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
December 31, 2017:						
Securities HTM:						
Municipal securities	$ 23,750,826	$ (354,460)	$ 72,611,780	$ (2,133,659)	$ 96,362,606	$ (2,488,119)
Securities AFS:						
U.S. govt. sponsored agency securities	$ 28,576,258	$ (200,022)	$ 3,640,477	$ (149,945)	$ 32,216,735	$ (349,967)
Residential mortgage-backed and related securities	88,927,779	(871,855)	57,931,731	(1,441,674)	146,859,510	(2,313,529)
Municipal securities	10,229,337	(41,151)	9,997,433	(169,949)	20,226,770	(211,100)
Other securities	923,535	(25,815)	—	—	923,535	(25,815)
	$ 128,656,909	$ (1,138,843)	$ 71,569,641	$ (1,761,568)	$ 200,226,550	$ (2,900,411)

At December 31, 2018, the investment portfolio included 611 securities. Of this number, 350 securities were in an unrealized loss position. The aggregate losses of these securities totaled approximately 1.9% of the total aggregate amortized cost. Of these 350 securities, 188 securities had an unrealized loss for 12 months or more. All of the debt securities in unrealized loss positions are considered acceptable credit risks. Based upon an evaluation of the available evidence, including the recent changes in market rates, credit rating information and information obtained from regulatory filings, management believes the declines in fair value for these debt securities are temporary. In addition, the Company lacks the intent to sell these securities and it is not more-likely-than-not that the Company will be required to sell these debt securities before their anticipated recovery.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 3. Investment Securities (continued)

The Company did not recognize OTTI on any investment securities for the years ended December 31, 2018, 2017 or 2016.

All sales of securities for the years ended December 31, 2018, 2017 and 2016, respectively, were from securities identified as AFS. Information on proceeds received, as well as the gains and losses from the sale of those securities are as follows:

	2018	2017	2016
Proceeds from sales of securities	$ 1,938,043	$ 71,091,580	$ 134,188,737
Gross gains from sales of securities	—	67,351	4,845,009
Gross losses from sales of securities	—	(155,236)	(252,611)

In September 2016, the Company sold an equity security and recognized a pre-tax gross gain on the sale of $4.0 million. The equity security was acquired by the Company at no cost as part of a membership in the invested company in 2002.

The amortized cost and fair value of securities as of December 31, 2018, by contractual maturity are shown below. Expected maturities of mortgage-backed and related securities may differ from contractual maturities because the mortgages underlying the securities may be called or prepaid without any penalties. Therefore, these securities are not included in the maturity categories in the following summary.

	Amortized Cost	Fair Value
Securities HTM:		
Due in one year or less	$ 2,232,726	$ 2,237,767
Due after one year through five years	27,569,566	27,716,775
Due after five years	372,110,593	370,816,041
	$ 401,912,885	$ 400,770,583
Securities AFS:		
Due in one year or less	$ 2,665,560	$ 2,665,829
Due after one year through five years	29,140,442	28,856,751
Due after five years	71,167,855	70,284,608
	102,973,857	101,807,188
Residential mortgage-backed and related securities	163,697,973	159,249,260
	$ 266,671,830	$ 261,056,448

Portions of the U.S. government sponsored agencies and municipal securities contain call options, at the discretion of the issuer, to terminate the security at predetermined dates prior to the stated maturity, summarized as follows:

	Amortized Cost	Fair Value
Securities HTM:		
Municipal securities	$ 209,953,250	$ 208,366,466
Securities AFS:		
U.S. govt. sponsored agency securities	4,999,072	4,918,050
Municipal securities	49,715,648	49,110,178
Other securities	6,505,918	6,602,900
	$ 61,220,638	$ 60,631,128

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 3. Investment Securities (continued)

As of December 31, 2018 and 2017, investment securities with a carrying value of $100.9 million and $78.6 million, respectively, were pledged on FHLB advances, customer and wholesale repurchase agreements, and for other purposes as required or permitted by law.

As of December 31, 2018, the Company's municipal securities portfolios were comprised of general obligation bonds issued by 110 issuers with fair values totaling $86.4 million and revenue bonds issued by 160 issuers, primarily consisting of states, counties, towns, villages and school districts with fair values totaling $371.9 million. The Company held investments in general obligation bonds in 26 states, including 6 states in which the aggregate fair value exceeded $5.0 million. The Company held investments in revenue bonds in 19 states, including 7 states in which the aggregate fair value exceeded $5.0 million.

As of December 31, 2017, the Company's municipal securities portfolios were comprised of general obligation bonds issued by 131 issuers with fair values totaling $108.0 million and revenue bonds issued by 145 issuers, primarily consisting of states, counties, towns, villages and school districts with fair values totaling $337.3 million. The Company held investments in general obligation bonds in 26 states, including 6 states in which the aggregate fair value exceeded $5.0 million. The Company held investments in revenue bonds in 16 states, including 7 states in which the aggregate fair value exceeded $5.0 million.

As of December 31, 2018, the Company held revenue bonds of one single issuer, located in Ohio, the aggregate book or market value of which exceeded 5% of the Company's stockholders' equity. The issuer's financial condition is strong and the source of repayment is diversified. The Compan monitors the investment and concentration closely. As of December 31, 2017, the Company did not hold general obligation or revenue bonds of any single issuer, the aggregate book or market value of which exceeded 5% of the Company's stockholders' equity. Of the general obligation and revenue bonds in the Company's portfolio, the majority are unrated bonds that represent small, private issuances. All unrated bonds were underwritten according to loan underwriting standards and have an average risk rating of 2, indicating very high quality. Additionally, many of these bonds are funding essential municipal services (water, sewer, education, medical facilities).

The Company's municipal securities are owned by each of the five charters, whose investment policies set forth limits for various subcategories within the municipal securities portfolio. Each charter is monitored individually and as of December 31, 2018, all were well-within policy limitations approved by the board of directors. Policy limits are calculated as a percentage of total risk-based capital.

As of December 31, 2018, the Company's standard monitoring of its municipal securities portfolio had not uncovered any facts or circumstances resulting in significantly different credits ratings than those assigned by a nationally recognized statistical rating organization, or in the case of unrated bonds, the rating assigned using the credit underwriting standards.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 4. Loans/Leases Receivable

The composition of the loan/lease portfolio as of December 31, 2018 and 2017 is presented as follows:

	2018	2017
C&I loans *	$ 1,429,409,587	$ 1,134,516,315
CRE loans		
Owner-occupied CRE	500,653,731	332,742,477
Commercial construction, land development, and other land	236,787,308	186,402,404
Other non owner-occupied CRE	1,028,669,736	784,347,000
	1,766,110,775	1,303,491,882
Direct financing leases **	117,968,682	141,448,232
Residential real estate loans ***	290,759,398	258,646,265
Installment and other consumer loans	119,381,780	118,610,799
	3,723,630,222	2,956,713,493
Plus deferred loan/lease origination costs, net of fees	9,123,820	7,771,907
	3,732,754,042	2,964,485,400
Less allowance	(39,847,108)	(34,355,728)
	$ 3,692,906,934	$ 2,930,129,672
** Direct financing leases:		
Net minimum lease payments to be received	$ 130,370,520	$ 156,583,887
Estimated unguaranteed residual values of leased assets	828,402	929,932
Unearned lease/residual income	(13,230,240)	(16,065,587)
	117,968,682	141,448,232
Plus deferred lease origination costs, net of fees	3,642,707	4,624,027
	121,611,389	146,072,259
Less allowance	(1,792,486)	(2,382,098)
	$ 119,818,903	$ 143,690,161

* Includes equipment financing agreements outstanding at m2, totaling $103.4 million and $66.8 million as of December 31, 2018 and 2017, respectively.

**Management performs an evaluation of the estimated unguaranteed residual values of leased assets on an annual basis, at a minimum. The evaluation consists of discussions with reputable and current vendors and management's expertise and understanding of the current states of particular industries to determine informal valuations of the

equipment. As necessary and where available, management will utilize valuations by independent appraisers. The large majority of leases with residual values contain a lease options rider which requires the lessee to pay the residual value directly, finance the payment of the residual value, or extend the lease term to pay the residual value. In these cases, the residual value is protected and the risk of loss is minimal.

At December 31, 2018, the Company had nine leases remaining with residual values totaling $828 thousand that were not protected with a lease end options rider. At December 31, 2017, the Company had 10 leases remaining with residual values totaling approximately $930 thousand that were not protected with a lease end options rider. Management has performed specific evaluations of these unguaranteed residual values and determined that the valuations are appropriate. There were no losses related to unguaranteed residual values during the years ended December 31, 2018, 2017, and 2016.

*** Includes residential real estate loans held for sale totaling $1.3 million and $645 thousand as of December 31, 2018 and 2017, respectively.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 4. Loans/Leases Receivable (continued)

Changes in accretable yield for the loans acquired in the mergers and acquisitions are as follows:

	For the year ended December 31, 2018		
	PCI Loans	Performing Loans	Total
Balance at the beginning of the period	$ (191,132)	$ (6,280,075)	$ (6,471,207)
Discount added at acquisition	(293,445)	(7,799,860)	(8,093,305)
Reclassification of nonaccretable discount to accretable	(891,569)	—	(891,569)
Accretion recognized	708,779	4,423,401	5,132,180
Balance at the end of the period	$ (667,367)	$ (9,656,534)	$ (10,323,901)

	For the year ended December 31, 2017		
	PCI Loans	Performing Loans	Total
Balance at the beginning of the period	$ (194,306)	$ (9,115,614)	$ (9,309,920)
Discount added at acquisition	(219,902)	(2,223,989)	(2,443,891)
Accretion recognized	223,076	5,059,528	5,282,604
Balance at the end of the period	$ (191,132)	$ (6,280,075)	$ (6,471,207)

	For the year ended December 31, 2016		
	PCI Loans	Performing Loans	Total
Balance at the beginning of the period	$ —	$ —	$ —
Discount added at acquisition	(277,579)	(11,916,009)	(12,193,588)
Accretion recognized	83,273	2,800,395	2,883,668
Balance at the end of the period	$ (194,306)	$ (9,115,614)	$ (9,309,920)

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 4. Loans/Leases Receivable (continued)

The aging of the loan/lease portfolio by classes of loans/leases as of December 31, 2018 and 2017 is presented as follows:

2018						
Classes of Loans/Leases	Current	30-59 Days Past Due	60-89 Days Past Due	Accruing Past Due 90 Days or More	Nonaccrual Loans/Leases	Total
C&I	$ 1,423,404,998	$ 930,321	$ 597,261	$ 389,138	$ 4,087,869	$ 1,429,409,587
CRE Owner-Occupied	500,138,489	—	193,157	106,470	215,615	500,653,731
CRE Commercial Construction, Land Development, and Other Land	234,704,132	1,763,953	—	—	319,223	236,787,308
Other Non Owner-Occupied CRE	1,022,663,569	483,953	—	—	5,522,214	1,028,669,736
Direct Financing Leases	114,077,839	1,641,883	487,938	—	1,761,022	117,968,682
Residential Real Estate	284,844,646	3,877,474	205,446	89,342	1,742,490	290,759,398
Installment and Other Consumer	118,343,671	355,685	24,324	46,794	611,306	119,381,780
	$ 3,698,177,344	$ 9,053,269	$ 1,508,126	$ 631,744	$ 14,259,739	$ 3,723,630,222
As a percentage of total loan/lease portfolio	99.32 %	0.24 %	0.04 %	0.02 %	0.38 %	100.00 %

2017						
Classes of Loans/Leases	Current	30-59 Days Past Due	60-89 Days Past Due	Accruing Past Due 90 Days or More	Nonaccrual Loans/Leases	Total
C&I	$ 1,124,734,486	$ 8,306,829	$ 243,647	$ —	$ 1,231,353	$ 1,134,516,315
CRE Owner-Occupied	331,868,142	540,435	—	—	333,900	332,742,477
CRE Commercial Construction, Land Development, and Other Land	181,558,092	—	—	—	4,844,312	186,402,404
Other Non Owner-Occupied CRE	782,526,249	572,877	4,146	—	1,243,728	784,347,000
Direct Financing Leases	137,708,397	1,305,191	259,600	—	2,175,044	141,448,232
Residential Real Estate	253,261,821	3,552,709	393,410	74,519	1,363,806	258,646,265
Installment and Other Consumer	117,773,259	517,537	56,760	14,152	249,091	118,610,799
	$ 2,929,430,446	$ 14,795,578	$ 957,563	$ 88,671	$ 11,441,234	$ 2,956,713,493
As a percentage of total loan/lease portfolio	99.08 %	0.50 %	0.03 %	0.00 %	0.39 %	100.00 %

96

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 4. Loans/Leases Receivable (continued)

NPLs by classes of loans/leases as of December 31, 2018 and 2017 is presented as follows:

Classes of Loans/Leases	2018 Accruing Past Due 90 Days or More*	Nonaccrual Loans/Leases**	Accruing TDRs	Total NPLs	Percentage of Total NPLs	
C&I	$ 389,138	$ 4,087,869	$ 454,229	$ 4,931,236	26.58	%
CRE						
Owner-Occupied CRE	106,470	215,615	—	322,085	1.74	%
Commercial Construction, Land Development, and Other Land	—	319,223	—	319,223	1.72	%
Other Non Owner-Occupied CRE	—	5,522,214	2,984,057	8,506,271	45.86	%
Direct Financing Leases	—	1,761,022	111,423	1,872,445	10.09	%
Residential Real Estate	89,342	1,742,490	100,040	1,931,872	10.41	%
Installment and Other Consumer	46,794	611,306	9,189	667,289	3.60	%
	$ 631,744	$ 14,259,739	$ 3,658,938	$ 18,550,421	100.00	%

* As of December 31, 2018 accruing past due 90 days or more included $495,608 of TDRs, including $389,138 in C&I loans and $106,470 in CRE

loans.

** At December 31, 2018, nonaccrual loans/leases included $2,311,198 of TDRs, including $265,181 in C&I loans, $1,378,090 in CRE loans, $321,050 in direct financing leases, $343,535 in residential real estate loans, and $3,342 in installment loans.

Classes of Loans/Leases	2017 Accruing Past Due 90 Days or More	Nonaccrual Loans/Leases ***	Accruing TDRs	Total NPLs	Percentage of Total NPLs	
C&I	$ —	$ 1,231,353	$ 5,224,182	$ 6,455,535	34.63	%
CRE						
Owner-Occupied CRE	—	333,900	107,322	441,222	2.37	%
Commercial Construction, Land Development, and Other Land	—	4,844,312	—	4,844,312	25.99	%
Other Non Owner-Occupied CRE	—	1,243,728	—	1,243,728	6.67	%
Direct Financing Leases	—	2,175,044	1,494,448	3,669,492	19.68	%
Residential Real Estate	74,519	1,363,806	272,493	1,710,818	9.18	%
Installment and Other Consumer	14,152	249,091	14,027	277,270	1.49	%
	$ 88,671	$ 11,441,234	$ 7,112,472	$ 18,642,377	100.00	%

*** At December 31, 2017, nonaccrual loans/leases included $2,282,495 of TDRs, including $122,598 in C&I loans, $1,336,871 in CRE loans, $700,255 in direct financing leases, $115,190 in residential real estate loans, and $7,581 in installment loans.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 4. Loans/Leases Receivable (continued)

Changes in the allowance by portfolio segment for the; years ended December 31, 2018, 2017, and 2016 are presented as follows:

	Year Ended December 31, 2018					
	C&I	CRE	Direct Financing Leases	Residential Real Estate	Installment and Other Consumer	Total
Balance, beginning	$ 14,323,036	$ 13,962,688	$ 2,382,098	$ 2,466,431	$ 1,221,475	$ 34,355,728
Provisions charged to expense	7,161,066	4,094,223	1,068,161	193,153	141,846	12,658,449
Loans/leases charged off	(5,358,683)	(387,499)	(2,002,227)	(126,566)	(44,422)	(7,919,397)
Recoveries on loans/leases previously charged off	294,798	49,839	344,454	23,618	39,619	752,328
Balance, ending	$ 16,420,217	$ 17,719,251	$ 1,792,486	$ 2,556,636	$ 1,358,518	$ 39,847,108

	Year Ended December 31, 2017					
	C&I	CRE	Direct Financing Leases	Residential Real Estate	Installment and Other Consumer	Total
Balance, beginning	$ 12,545,110	$ 11,670,609	$ 3,111,898	$ 2,342,344	$ 1,087,487	$ 30,757,448
Provisions charged to expense	2,736,296	4,044,460	1,369,624	197,034	122,505	8,469,919
Loans/leases charged off	(1,149,790)	(1,795,229)	(2,284,910)	(102,088)	(41,196)	(5,373,213)
Recoveries on loans/leases previously charged off	191,420	42,848	185,486	29,141	52,679	501,574

Balance, ending	$ 14,323,036	$ 13,962,688	$ 2,382,098	$ 2,466,431	$ 1,221,475	$ 34,355,728

	Year Ended December 31, 2016					
	C&I	CRE	Direct Financing Leases	Residential Real Estate	Installment and Other Consumer	Total
Balance, beginning	$ 10,484,080	$ 9,375,117	$ 3,395,088	$ 1,790,150	$ 1,096,471	$ 26,140,906
Provisions (credits) charged to expense	2,478,912	2,286,953	2,127,463	628,114	(43,276)	7,478,166
Loans/leases charged off	(527,152)	(24,304)	(2,503,417)	(76,820)	(112,490)	(3,244,183)
Recoveries on loans/leases previously charged off	109,270	32,843	92,764	900	146,782	382,559
Balance, ending	$ 12,545,110	$ 11,670,609	$ 3,111,898	$ 2,342,344	$ 1,087,487	$ 30,757,448

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 4. Loans/Leases Receivable (continued):

The allowance by impairment evaluation and by portfolio segment as of December 31, 2018 and 2017 is presented as follows:

2018	C&I	CRE	Direct Financing Leases	Residential Real Estate	Installment and Other Consumer	Total
owance impaired ns/leases owance	$ 972,647	$ 2,123,685	$ 194,008	$ 257,014	$ 111,191	$ 3,658,545
nimpaired ns/leases	15,447,570	15,595,566	1,598,478	2,299,622	1,247,327	36,188,563
	$ 16,420,217	$ 17,719,251	$ 1,792,486	$ 2,556,636	$ 1,358,518	$ 39,847,108
paired ns/leases	$ 4,499,451	$ 10,446,748	$ 2,248,597	$ 2,109,612	$ 898,150	$ 20,202,558
nimpaired ns/leases	1,424,910,136	1,755,664,027	115,720,085	288,649,786	118,483,630	3,703,427,664
	$ 1,429,409,587	$ 1,766,110,775	$ 117,968,682	$ 290,759,398	$ 119,381,780	$ 3,723,630,222
owance a centage mpaired ns/leases	21.62 %	20.33 %	8.63 %	12.18 %	12.38 %	18.11
owance a centage nimpaired ns/leases	1.08 %	0.89 %	1.38 %	0.80 %	1.05 %	0.98
al owance as ercentage otal ns/leases	1.15 %	1.00 %	1.52 %	0.88 %	1.14 %	1.07

	2017					
	C&I	CRE	Direct Financing Leases	Residential Real Estate	Installment and Other Consumer	Total
owance impaired ns/leases	$ 715,627	$ 1,429,460	$ 504,469	$ 355,167	$ 38,596	$ 3,043,319
owance himpaired ns/leases	13,607,409	12,533,228	1,877,629	2,111,264	1,182,879	31,312,409
	$ 14,323,036	$ 13,962,688	$ 2,382,098	$ 2,466,431	$ 1,221,475	$ 34,355,728
paired ns/leases	$ 6,248,209	$ 6,529,262	$ 3,669,492	$ 1,704,846	$ 202,354	$ 18,354,163
nimpaired ns/leases	1,128,268,106	1,296,962,620	137,778,740	256,941,419	118,408,445	2,938,359,330
	$ 1,134,516,315	$ 1,303,491,882	$ 141,448,232	$ 258,646,265	$ 118,610,799	$ 2,956,713,493
owance a centage mpaired ns/leases	11.45 %	21.89 %	13.75 %	20.83 %	19.07 %	16.58
owance a centage himpaired ns/leases	1.21 %	0.97 %	1.36 %	0.82 %	1.00 %	1.07
al owance as ercentage otal ns/leases	1.26 %	1.07 %	1.68 %	0.95 %	1.03 %	1.16

99

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 4. Loans/Leases Receivable (continued)

Loans/leases, by classes of financing receivable, considered to be impaired as of and for the years ended December 31, 2018, 2017, and 2016 are presented below. The recorded investment represents customer balances net of any partial charge-offs recognized on the loan/lease. The unpaid principal balance represents the recorded balance outstanding on the loan/lease prior to any partial charge-offs.

	2018					
Classes of Loans/Leases	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized	Interest Income Recognized for Cash Payments Received
Impaired Loans/Leases with No Specific Allowance Recorded:						
C&I	$ 1,846,136	$ 4,539,729	$ —	$ 2,346,184	$ 209,854	$ 209,854
CRE Owner-Occupied	106,470	106,470	—	106,892	—	—
CRE Commercial Construction, Land Development, and Other Land	506,603	506,603	—	101,321	—	—
Other Non Owner-Occupied CRE	1,804,125	1,804,125	—	540,298	—	—
Direct Financing Leases	1,929,061	1,929,061	—	2,193,339	60,483	60,483
Residential Real Estate	983,753	1,058,532	—	723,424	9,043	9,043
Installment and Other Consumer	761,465	761,465	—	198,035	290	290
	$ 7,937,613	$ 10,705,985	$ —	$ 6,209,493	$ 279,670	$ 279,670

Impaired Loans/Leases with Specific Allowance Recorded:						
C&I	$ 2,653,315	$ 2,653,315	$ 972,647	$ 1,118,374	$ 43,052	$ 43,052
CRE Owner-Occupied	304,043	660,329	38,533	176,874	—	—
CRE Commercial Construction, Land Development, and Other Land	148,795	148,795	33,095	159,389	—	—
Other Non Owner-Occupied CRE	7,576,712	7,576,712	2,052,057	3,054,716	57,760	57,760
Direct Financing Leases	319,536	319,536	194,008	273,352	—	—
Residential Real Estate	1,125,859	1,125,859	257,014	552,539	11,515	11,515
Installment and Other Consumer	136,685	136,685	111,191	124,812	—	—
	$ 12,264,945	$ 12,621,231	$ 3,658,545	$ 5,460,056	$ 112,327	$ 112,327
Total Impaired Loans/Leases:						
C&I	$ 4,499,451	$ 7,193,044	$ 972,647	$ 3,464,558	$ 252,906	$ 252,906
CRE Owner-Occupied	410,513	766,799	38,533	283,766	—	—
CRE Commercial Construction, Land Development, and Other Land	655,398	655,398	33,095	260,710	—	—
Other Non Owner-Occupied CRE	9,380,837	9,380,837	2,052,057	3,595,014	57,760	57,760
Direct Financing Leases	2,248,597	2,248,597	194,008	2,466,691	60,483	60,483
Residential Real Estate	2,109,612	2,184,391	257,014	1,275,963	20,558	20,558
Installment and Other Consumer	898,150	898,150	111,191	322,847	290	290
	$ 20,202,558	$ 23,327,216	$ 3,658,545	$ 11,669,549	$ 391,997	$ 391,997

100

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 4. Loans/Leases Receivable (continued)

	2017					
Classes of Loans/Leases	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized	Interest Income Recognized for Cash Payments Received
Impaired Loans/Leases with No Specific Allowance Recorded:						
C&I	$ 1,634,269	$ 1,644,706	$ —	$ 1,406,310	$ 71,183	$ 71,183
CRE Owner-Occupied	289,261	289,261	—	79,317	11,902	11,902
CRE Commercial Construction, Land Development, and Other Land	—	—	—	—	—	—
Other Non Owner-Occupied CRE	1,171,565	1,171,565	—	1,176,738	—	—
Direct Financing Leases	2,944,540	2,944,540	—	2,879,695	132,167	132,167
Residential Real Estate	943,388	1,018,167	—	685,807	1,161	1,161
Installment and Other Consumer	134,245	134,245	—	126,474	—	—
	$ 7,117,268	$ 7,202,484	$ —	$ 6,354,341	$ 216,413	$ 216,413
Impaired Loans/Leases with Specific Allowance						

Recorded:						
C&I	$ 4,613,940	$ 4,617,879	$ 715,627	$ 4,584,142	$ 203,221	$ 203,221
CRE Owner-Occupied	151,962	151,962	48,462	221,260	—	—
CRE Commercial Construction, Land Development, and Other Land	4,844,312	4,844,312	1,379,235	4,447,831	—	—
Other Non Owner-Occupied CRE	72,163	72,163	1,763	44,667	—	—
Direct Financing Leases	724,953	724,953	504,469	625,107	—	—
Residential Real Estate	761,458	761,458	355,167	549,286	14,990	14,990
Installment and Other Consumer	68,109	68,109	38,596	40,152	410	410
	$ 11,236,897	$ 11,240,836	$ 3,043,319	$ 10,512,445	$ 218,621	$ 218,621
Total Impaired Loans/Leases:						
C&I	$ 6,248,209	$ 6,262,585	$ 715,627	$ 5,990,452	$ 274,404	$ 274,404
CRE Owner-Occupied	441,222	441,222	48,462	300,577	11,902	11,902
CRE Commercial Construction, Land Development, and Other Land	4,844,312	4,844,312	1,379,235	4,447,831	—	—
Other Non Owner-Occupied CRE	1,243,728	1,243,728	1,763	1,221,405	—	—
Direct Financing Leases	3,669,492	3,669,492	504,469	3,504,802	132,167	132,167
Residential Real Estate	1,704,846	1,779,625	355,167	1,235,093	16,151	16,151
Installment and Other Consumer	202,354	202,354	38,596	166,626	410	410
	$ 18,354,163	$ 18,443,318	$ 3,043,319	$ 16,866,786	$ 435,034	$ 435,034

101

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 4. Loans/Leases Receivable (continued)

	2016					
Classes of Loans/Leases	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized	Interest Income Recognized for Cash Payments Received
Impaired Loans/Leases with No Specific Allowance Recorded:						
C&I	$ 841,895	$ 951,600	$ —	$ 2,858,343	$ 16,748	$ 16,748
CRE Owner-Occupied	—	93,774	—	312,242	—	—
CRE Commercial Construction, Land Development, and Other Land	—	—	—	—	—	—
Other Non Owner-Occupied CRE	1,196,549	1,196,549	—	1,322,654	—	—
Direct Financing Leases	1,690,121	1,690,121	—	1,731,982	43,461	43,461
Residential Real Estate	853,294	892,495	—	964,590	9,903	9,903
Installment and Other Consumer	55,734	55,734	—	321,175	4,475	4,475
	$ 4,637,593	$ 4,880,273	$ —	$ 7,510,986	$ 74,587	$ 74,587
Impaired Loans/Leases with Specific Allowance						

Recorded:						
C&I	$ 8,094,556	$ 8,098,395	$ 1,771,537	$ 2,959,495	$ 17,742	$ 17,742
CRE Owner-Occupied	322,148	322,148	57,398	385,269	—	—
CRE Commercial Construction, Land Development, and Other Land	4,353,817	4,353,819	577,611	1,022,930	—	—
Other Non Owner-Occupied CRE	239,600	239,600	58,910	47,920	—	—
Direct Financing Leases	1,566,143	1,566,143	848,919	841,733	36,303	36,303
Residential Real Estate	807,886	882,018	289,112	573,211	11,675	11,675
Installment and Other Consumer	50,356	50,356	39,481	40,384	527	527
	$ 15,434,506	$ 15,512,479	$ 3,642,968	$ 5,870,942	$ 66,247	$ 66,247
Total Impaired Loans/Leases:						
C&I	$ 8,936,451	$ 9,049,995	$ 1,771,537	$ 5,817,838	$ 34,490	$ 34,490
CRE Owner-Occupied	322,148	415,922	57,398	697,511	—	—
CRE Commercial Construction, Land Development, and Other Land	4,353,817	4,353,819	577,611	1,022,930	—	—
Other Non Owner-Occupied CRE	1,436,149	1,436,149	58,910	1,370,574	—	—
Direct Financing Leases	3,256,264	3,256,264	848,919	2,573,715	79,764	79,764
Residential Real Estate	1,661,180	1,774,513	289,112	1,537,801	21,578	21,578
Installment and Other Consumer	106,090	106,090	39,481	361,559	5,002	5,002
	$ 20,072,099	$ 20,392,752	$ 3,642,968	$ 13,381,928	$ 140,834	$ 140,834

Impaired loans/leases for which no allowance has been provided have adequate collateral, based on management’s current estimates.

For C&I and CRE loans, the Company’s credit quality indicator is internally assigned risk ratings. Each commercial loan is assigned a risk rating upon origination. The risk rating is reviewed every 15 months, at a minimum, and on an as needed basis depending on the specific circumstances of the loan. See Note 1 for further discussion on the Company’s risk ratings.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 4. Loans/Leases Receivable (continued)

For direct financing leases, residential real estate loans, and installment and other consumer loans, the Company's credit quality indicator is performance determined by delinquency status. Delinquency status is updated daily by the Company's loan system.

For each class of financing receivable, the following presents the recorded investment by credit quality indicator as of December 31, 2018 and 2017:

2018		CRE				
Internally Assigned Risk Rating	C&I	Owner-Occupied CRE	Non-Owner Occupied Commercial Construction, Land Development, and Other Land	Other CRE	Total	As a % of Total
Pass (Ratings 1 through 5)	$ 1,294,417,614	$ 487,948,800	$ 230,473,570	$ 1,008,626,078	$ 3,021,466,062	97.72 %
Special Mention (Rating 6)	23,302,472	9,599,493	3,847,691	5,308,625	42,058,281	1.36 %
Substandard (Rating 7)	8,286,398	3,105,438	2,466,047	14,735,033	28,592,916	0.92 %
Doubtful (Rating 8)	—	—	—	—	—	— %
	$ 1,326,006,484	$ 500,653,731	$ 236,787,308	$ 1,028,669,736	$ 3,092,117,259	100.00 %

2018		Direct Financing	Residential Real	Installment and		As a % of
Delinquency Status *	C&I	Leases	Estate	Other Consumer	Total	Total
Performing	$ 102,712,527	$ 116,096,237	$ 288,827,527	$ 118,714,491	$ 626,350,782	99.18 %

Nonperforming	690,576	1,872,445	1,931,871	667,289	5,162,181	0.82	%
	$ 103,403,103	$ 117,968,682	$ 290,759,398	$ 119,381,780	$ 631,512,963	100.00	%

	2017					
		CRE				
Internally Assigned Risk Rating	C&I	Owner-Occupied CRE	Non-Owner Occupied Commercial Construction, Land Development, and Other Land	Other CRE	Total	As a % of Total
Pass (Ratings 1 through 5)	$ 1,031,963,703	$ 318,293,608	$ 179,142,839	$ 767,119,909	$ 2,296,520,059	96.85
Special Mention (Rating 6)	10,944,924	8,230,060	1,780,000	10,068,870	31,023,854	1.31
Substandard (Rating 7)	24,578,731	6,218,809	5,479,565	7,158,221	43,435,326	1.83
Doubtful (Rating 8)	270,559	—	—	—	270,559	0.01
	$ 1,067,757,917	$ 332,742,477	$ 186,402,404	$ 784,347,000	$ 2,371,249,799	100.00

	2017						
		Direct Financing	Residential Real	Installment and		As a % of	
Delinquency Status *	C&I	Leases	Estate	Other Consumer	Total	Total	
Performing	$ 65,847,177	$ 137,778,740	$ 256,935,447	$ 118,333,529	$ 578,894,893	98.88	%
Nonperforming	911,220	3,669,492	1,710,818	277,270	6,568,800	1.12	%
	$ 66,758,397	$ 141,448,232	$ 258,646,265	$ 118,610,799	$ 585,463,693	100.00	%

* Performing = loans/leases accruing and less than 90 days past due. Nonperforming = loans/leases on nonaccrual, accruing loans/leases that are greater than or equal to 90 days past due, and accruing troubled debt restructurings.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 4. Loans/Leases Receivable (continued)

TDRs totaled $6,465,744 and $9,394,967 as of December 31, 2018 and 2017, respectively.

For each class of financing receivable, the following presents the number and recorded investment of TDRs, by type of concession, that were restructured during the years ended December 31, 2018 and 2017. The difference between the pre-modification recorded investment and the post-modification recorded investment would be any partial charge-offs at the time of restructuring. The specific allowance is as of December 31, 2018 and 2017, respectively. The following excludes any TDRs that were restructured and paid off or charged off in the same year.

	2018			
Classes of Loans/Leases	Number of Loans / Leases	Pre-Modification Recorded Investment	Post-Modification Recorded Investment	Specific Allowance
CONCESSION - Significant Payment Delay				
C&I	5	$ 425,649	$ 425,649	$ 250,000
Other Non Owner-Occupied CRE	1	500,000	500,000	60,000
Residential Real Estate	1	46,320	46,320	—
Direct Financing Leases	3	75,066	75,066	—
	10	$ 1,047,035	$ 1,047,035	$ 310,000
CONCESSION - Extension of Maturity				
Other Non Owner-Occupied CRE	2	$ 2,975,703	$ 2,975,703	$ 1,492,057
Residential Real Estate	2	100,215	100,215	8,392
	4	$ 3,075,918	$ 3,075,918	$ 1,500,449
TOTAL	14	$ 4,122,953	$ 4,122,953	$ 1,810,449

	2017			
Classes of Loans/Leases	Number of Loans/Leases	Pre-Modification Recorded Investment	Post-Modification Recorded Investment	Specific Allowance
CONCESSION - Significant Payment Delay				
C&I	7	$ 826,531	$ 826,531	$ 62,596

CRE - Owner Occupied	1	107,322	107,322	—
Direct Financing Leases	24	1,703,255	1,703,255	—
	32	$ 2,637,108	$ 2,637,108	$ 62,596
CONCESSION - Extension of Maturity				
Direct Financing Leases	3	$ 115,236	$ 115,236	$ —
	3	$ 115,236	$ 115,236	$ —
TOTAL	35	$ 2,752,344	$ 2,752,344	$ 62,596

Of the TDRs reported above, three with a post-modification recorded investment totaling $796,320 were on nonaccrual as of December 31, 2018 and seven with a post-modification recorded investment totaling $279,245 were on nonaccrual as of December 31, 2017.

For the year ended December 31, 2018, the Company had five TDRs totaling $398,869 that redefaulted within 12 months subsequent to restructure, where default is defined as delinquency of 90 days or more and/or placement on nonaccrual status. For the year ended December 31, 2017, the Company had six TDRs totaling $251,940 that redefaulted within 12 months subsequent to restructure, where default is defined as delinquency of 90 days or more and/or placement on nonaccrual status.

Not included in the table above, the Company had 13 TDRs that were restructured and charged off in 2018, totaling $895,563. There were two TDRs that were both restructured and charged off in 2017, totaling $65,623.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 4. Loans/Leases Receivable (continued)

Loans are made in the normal course of business to directors, executive officers, and their related interests. The terms of these loans, including interest rates and collateral, are similar to those prevailing for comparable transactions with other persons. An analysis of the changes in the aggregate committed amount of loans greater than or equal to $60,000 during the years ended December 31, 2018, 2017, and 2016, is as follows:

	2018	2017	2016
Balance, beginning	$ 66,441,948	$ 61,608,976	$ 42,012,313
Net increase due to change in related parties	41,797,001	11,926,759	19,945,960
Advances	43,453,609	13,090,798	4,806,616
Repayments	(26,196,333)	(20,184,585)	(5,155,913)
Balance, ending	$ 125,496,225	$ 66,441,948	$ 61,608,976

The Company’s loan portfolio includes a geographic concentration in the Midwest. Additionally, the loan portfolio includes a concentration of loans in certain industries as of December 31, 2018 and 2017 as follows:

	2018		2017	
Industry Name	Balance	Percentage of Total Loans/Leases	Balance	Percentage of Total Loans/Leases
Lessors of Non-Residential Buildings	$ 632,534,255	17 %	$ 400,622,681	14 %
Lessors of Residential Buildings	594,345,563	16 %	370,353,561	12 %
Administration of Urban Planning & Community & Rural Development	111,579,461	3 %	83,343,541	3 %
Hotels	83,105,821	2 %	73,199,925	2 %
Bank Holding Companies	75,600,713	2 %	66,950,294	2 %
Nonresidential Property Managers	70,211,971	2 %	51,984,722	2 %

Concentrations within the leasing portfolio are monitored by equipment type – none of which represent a concentration within the total loans/leases portfolio. Within the leasing portfolio, diversification is spread among construction, manufacturing and the service industries. Geographically, the lease portfolio is diversified across all 50 states. No individual state represents a concentration within the total loan/lease portfolio.

Note 5. Premises and Equipment

The following summarizes the components of premises and equipment as of December 31, 2018 and 2017:

	2018	2017
Land	$ 15,581,430	$ 13,466,930
Buildings (useful lives 15 to 50 years)	64,299,322	53,633,788
Furniture and equipment (useful lives 3 to 10 years)	36,399,218	31,984,631
Premises and equipment	116,279,970	99,085,349
Less accumulated depreciation	40,697,852	36,247,094
Premises and equipment, net	$ 75,582,118	$ 62,838,255

Certain facilities are leased under operating leases. Rental expense was $555,436, $348,467, and $334,977 for the years ended December 31, 2018, 2017, and 2016, respectively.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 5. Premises and Equipment (continued)

Future minimum rental commitments under noncancelable leases are as follows as of December 31, 2018:

Year ending December 31:	
2019	591,688
2020	452,457
2021	200,167
2022	123,828
2023	73,035
Thereafter	1,403
	$ 1,442,578

During 2016, the Company entered into a material related party transaction with an entity that is owned and controlled by a CRBT director. That business was chosen as the general contractor for the remodel of the Waterloo branch. The business was the original contractor for the branch and is recognized as a leader in Iowa and the Midwest market for the design and construction of financial services and professional office buildings. Based on the entity's expertise, its experience as the original designer/builder of the branch location and a decline to bid from two other contractors, management chose the entity as the general contractor. Management determined that the bids received from the entity were at market rates.

The project total was estimated at $3.7 million. This was the full contract price, as subcontractors were utilized to complete the work. It is estimated that the entity received $2.2 million for its work as the general contractor, including payments for a portion of the actual construction costs as the entity completed a portion of the subcontracting work in addition to being the general contractor. As of December 31, 2017, the project was complete and there was no outstanding commitment remaining.

Note 6. Goodwill and Intangibles

The following table presents the changes in the carrying amount of goodwill for the years ended December 31, 2018, 2017 and 2016:

	2018	2017	2016
Balance at the beginning of period	$ 28,334,092	$ 13,110,913	$ 3,222,688
Goodwill from merger with Springfield Bancshares	45,974,931	—	—
Goodwill from acquisition of the Bates Companies	3,766,074	—	—

Goodwill from acquisition of Guaranty Bank	—	15,223,179	—
Goodwill from acquisition of Guaranty Bank - measurement period adjustment	(243,195)	—	—
Goodwill from acquisition of CSB	—	—	9,888,225
Balance at the end of period	$ 77,831,902	$ 28,334,092	$ 13,110,913

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 6. Goodwill and Intangibles (continued)

The following table presents the changes in core deposit intangibles (included in Intangibles on the consolidated balance sheets) during the years ended December 31, 2018 ,2017 and 2016:

	2018	2017	2016
Balance at the beginning of the period	$ 9,078,953	$ 7,381,213	$ 1,471,409
Core deposit intangible from merger with Springfield Bancshares	8,208,728	—	—
Core deposit intangible from acquisition of Guaranty Bank	—	2,698,301	—
Core deposit intangible from acquisition of CSB	—	—	6,352,653
Amortization expense	(1,692,431)	(1,000,561)	(442,849)
Balance at the end of the period	$ 15,595,250	$ 9,078,953	$ 7,381,213
Gross carrying amount	$ 19,254,809	$ 11,046,081	$ 8,347,780
Accumulated amortization	(3,659,559)	(1,967,128)	(966,567)
Net book value	$ 15,595,250	$ 9,078,953	$ 7,381,213

The following table presents the estimated amortization of the core deposit intangibles:

Years ending December 31,	Amount
2019	$ 2,129,141
2020	2,084,985
2021	2,032,204
2022	1,970,792
2023	1,776,065
Thereafter	5,602,063
	$ 15,595,250

The following table presents the changes in customer list intangible (included in Intangibles on the consolidated balance sheets) during the year ended December 31, 2018:

	2018
Balance at the beginning of period	$ —
Customer list intangible from acquisition of Bates Companies	1,854,932
Balance at the end of period	1,854,932

The following table presents the estimated amortization of the customer list intangible:

Years ending December 31,	Amount
2019	$ 123,662
2020	123,662
2021	123,662
2022	123,662
2023	123,662
Thereafter	1,236,622
	$ 1,854,932

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 7. Derivatives and Hedging Activities

The Company uses interest rate swap and cap instruments to manage interest rate risk related to the variability of interest payments due to changes in interest rates. The Company entered into interest rate caps on June 5, 2014 to hedge against the risk of rising interest rates on short-term liabilities. The short-term liabilities consist of $30.0 million of 1-month FHLB advances, and the benchmark rate hedged is 1-month LIBOR. The interest rate caps are designated as a cash flow hedge in accordance with ASC 815. An initial premium of $2.1 million was paid upfront for the two caps. The details of the interest rate caps are as follows:

Hedged Instrument	Effective Date	Maturity Date	Balance Sheet Location	Notional Amount	1-Month LIBOR Strike Rate	Fair Value as of December 31, 2018	December 31, 2017
1-month FHLB Advance	6/3/2014	6/5/2019	Other Assets	$ 15,000,000	0.93%	$ 116,775	$ 190,085
1-month FHLB Advance	6/5/2014	6/5/2021	Other Assets	15,000,000	1.43%	342,037	316,615
				$ 30,000,000		$ 458,812	$ 506,700

On June 21, 2018, the Company entered into interest rate swaps to hedge against the risk of rising rates on its variable rate trust preferred securities. The floating rate trust preferred securities are tied to 3-month LIBOR, and the interest rate swaps utilize 3-month LIBOR, so the hedge is effective. The interest rate swaps are designated as a cash flow hedge in accordance with ASC 815. The details of the interest rate swaps are as follows:

Hedged Instrument	Effective Date	Maturity Date	Balance Sheet Location	Notional Amount	Receive Rate	Pay Rate	Fair Value as of December 31, 2018
QCR Holdings Statutory Trust II	9/30/2018	9/30/2028	Other Liabilities	$ 10,000,000	5.65%	5.85%	$ (298,367)
QCR Holdings Statutory Trust III	9/30/2018	9/30/2028	Other Liabilities	8,000,000	5.65%	5.85%	(238,693)

QCR Holdings Statutory Trust V	7/7/2018	7/7/2028	Other Liabilities	10,000,000	3.99%	4.54%	(287,716)
Community National Statutory Trust II	9/20/2018	9/20/2028	Other Liabilities	3,000,000	4.96%	5.17%	(89,008)
Community National Statutory Trust III	9/15//2018	9/15/2028	Other Liabilities	3,500,000	4.54%	4.75%	(103,858)
Guaranty Bankshares Statutory Trust I	9/15/2018	9/15/2028	Other Liabilities	4,500,000	4.54%	4.75%	(133,532)
				$ 39,000,000	4.94%	5.24%	$ (1,151,174)

Changes in the fair values of derivative financial instruments accounted for as cash flow hedges to the extent they are effective hedges, are recorded as a component of accumulated other comprehensive income. The following is a summary of how AOCI was impacted during the reporting periods:

	Year Ended	
	December 31, 2018	December 31, 2017
Unrealized loss at beginning of period, net of tax	$ (805,027)	$ (932,156)
Amount reclassified from accumulated other comprehensive income to noninterest expense related to hedge ineffectiveness	27,407	79,757
Amount reclassified from accumulated other comprehensive income to interest expense related to caplet amortization	575,247	405,134
Amount of loss recognized in other comprehensive income, net of tax	(1,073,815)	(357,762)
Unrealized loss at end of period, net of tax	$ (1,276,188)	$ (805,027)

Changes in the fair value related to the ineffective portion of cash flow hedges, are reported in noninterest income during the period of the change. As shown in the table above, $27 thousand and $80 thousand of expense from the change in fair value for the years ending December 31, 2018 and 2017, respectively, was due to ineffectiveness.

The Company has also entered into interest rate swap contracts that are not designated as hedging instruments. These derivative contracts relate to transactions in which the Company enters into an interest rate swap with a customer while at the same time entering into an offsetting interest rate swap with a third part financial institution. Because the Company acts as an intermediary for the customer, changes in the fair value of the underlying derivative contracts, for the most part, offset each other and do not significantly impact the Company’s results of operations.

	December 31, 2018		December 31, 2017	
	Notional Amount	Estimated Fair Value	Notional Amount	Estimated Fair Value

Non-Hedging Interest Rate Derivatives Assets:				
Interest rate swap contracts	$ 445,021,807	$ 22,195,713	$ 230,434,728	$ 4,397,238
Non-Hedging Interest Rate Derivatives Liabilities:				
Interest rate swap contracts	$ 445,021,807	$ 22,195,713	$ 230,434,728	$ 4,397,238

Swap fee income totaled $10.8 million, $3.1 million and $1.7 million for the years ended December 31, 2018, 2017, and 2016, respectively.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 8. Deposits

The aggregate amount of certificates of deposit, each with a minimum denomination of $250,000, was $592.7 million and $364.3 million as of December 31, 2018 and 2017, respectively.

As of December 31, 2018, the scheduled maturities of certificates of deposit were as follows:

Year ending December 31:	
2019	$ 796,333,079
2020	116,147,111
2021	31,872,141
2022	20,834,858
2023	9,258,973
Thereafter	257,874
	$ 974,704,036

The Company has public entity deposits that are collateralized by investment securities with carrying values as follows:

	2018	2017
U.S. govt. sponsored agency securities	$ 980,160	$ 983,670
Residential mortgage-backed and related securities	9,882,921	9,035,755
	$ 10,863,081	$ 10,019,425

The Company had a $80.8 million PUD LOC with the FHLB of Des Moines and a $11.0 million PUD LOC with the FHLB of Chicago for the purpose of providing additional collateral on public deposits as of December 31, 2018. As of December 31, 2017, the Company had a $35.0 million PUD LOC with the FHLB of Des Moines and a $10.1 million PUD LOC with the FHLB of Chicago. There were no amounts outstanding under these letters of credit as of December 31, 2018 or 2017.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 9. Short-Term Borrowings

Short-term borrowings as of December 31, 2018 and 2017 are summarized as follows:

	2018	2017
Overnight repurchase agreements with customers	$ 2,084,157	$ 7,003,122
Federal funds purchased	26,690,000	6,990,000
	$ 28,774,157	$ 13,993,122

The Company's overnight repurchase agreements with customers are collateralized by investment securities with carrying values as follows:

	2018	2017
U.S. govt. sponsored agency securities	$ 3,661,995	$ 2,077,702
Residential mortgage-backed and related securities	20,654,345	18,816,280
Total securities pledged to overnight customer repurchase agreements	24,316,340	20,893,982
Less: overcollateralized position	22,232,183	13,890,860
	$ 2,084,157	$ 7,003,122

Inherent in the overnight purchase agreements is a risk that the fair value of the collateral pledged on the agreements could decline below the amount obligated under our customer repurchase agreements. The Company considers this risk minimal. The Company monitors balances daily to ensure that collateral is sufficient to meet obligations. Additionally, the Company maintains an overcollateralized position that is sufficient to cover any interest rate movements.

The securities underlying the agreements as of December 31, 2018 and 2017 were under the Company's control in safekeeping at third-party financial institutions.

Information concerning overnight repurchase agreements with customers is summarized as follows as of December 31, 2018 and 2017:

	2018		2017	
Average daily balance during the period	$ 7,830,860		$ 7,475,824	
Average daily interest rate during the period	0.38	%	0.08	%
Maximum month-end balance during the period	$ 10,391,529		$ 11,829,201	
Weighted average rate as of end of period	0.90	%	0.15	%

Information concerning federal funds purchased is summarized as follows as of December 31, 2018 and 2017:

	2018		2017	
Average daily balance during the period	$ 13,059,102		$ 13,486,239	
Average daily interest rate during the period	2.18	%	1.31	%
Maximum month-end balance during the period	$ 32,330,000		$ 33,650,000	
Weighted average rate as of end of period	2.46	%	1.24	%

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 10. FHLB Advances

The subsidiary banks are members of the FHLB of Des Moines or Chicago. Maturity and interest rate information on advances from the FHLB as of December 31, 2018 and 2017 is as follows:

	December 31, 2018		December 31, 2017	
	Amount Due	Weighted Average Interest Rate at Year-End	Amount Due	Weighted Average Interest Rate at Year-End
Maturity:				
Year ending December 31:				
2018	$ —	—	$ 190,400,000	1.82 %
2019	239,957,672	2.60	—	—
2020	11,484,203	1.74	1,600,000	1.75
2021	15,050,164	2.32	—	—
Total FHLB advances	$ 266,492,039	2.55 %	$ 192,000,000	1.82 %

Advances are collateralized by loans of $1.3 billion and $850.1 million as of December 31, 2018 and 2017, respectively, in aggregate. On pledged loans, the FHLB applies varying collateral maintenance levels from 125% to 333% based on the loan type. Advances are also collateralized by securities of $26.9 million and $6.7 million as of December 31, 2018 and 2017, respectively, in aggregate. The Company continues to pledge loans under blanket liens to provide off balance sheet liquidity.

As of December 31, 2018 and included with the 2019 maturity grouping above are $190.2 million of short-term advances from the FHLB. These advances have maturities ranging from 1 day to 1 month. Short-term and overnight advances totaled $165.4 million as of December 31, 2017 and had maturities ranging from 1 day to 1 month.

Throughout 2016, the Company executed several balance sheet restructuring strategies in an effort to reduce reliance on wholesale funding. These strategies will continue to be evaluated in the future. A summary of prepayments of FHLB advances related to these restructurings is summarized in the following table for the year ended December 31, 2016.

2016

Date of Restructuring	Amount	Weighted Average Interest Rate	Range of Maturity Dates	Prepayment Fees
First Quarter of 2016	$ 10,000,000	3.86 %	December 2017	$ 524,197

Third Quarter of 2016	5,000,000	2.84	%	February 2018	127,310
Fourth Quarter of 2016	15,000,000	3.14	%	September 2017 to November 2017	357,161
Total for 2016	$ 30,000,000	3.33	%		$ 1,008,668

All prepayment fees shown in the table above are included in losses on debt extinguishment in the statements of income.

As of December 31, 2018 and 2017, the subsidiary banks held $15.7 million and $11.7 million, respectively, of FHLB stock, which is included in restricted investment securities on the consolidated balance sheet.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 11. Other Borrowings and Unused Lines of Credit

Other borrowings as of December 31, 2018 and 2017 are summarized as follows:

	2018	2017
Wholesale structured repurchase agreements	$ 35,000,000	$ 35,000,000
Term notes	23,250,000	31,000,000
Subordinated debentures	4,782,318	—
Revolving line of credit	9,000,000	—
	$ 72,032,318	$ 66,000,000

The Company's wholesale structured repurchase agreements are collateralized by investment securities with carrying values as follows:

	2018	2017
Residential mortgage-backed and related securities	$ 38,870,228	$ 40,503,002
Total securities pledged to wholesale customer repurchase agreements	38,870,228	40,503,002
Less: overcollateralized position	3,870,228	5,503,002
	$ 35,000,000	$ 35,000,000

Inherent in the wholesale structured repurchase agreements is a risk that the fair value of the collateral pledged on the agreements could decline below the amount obligated under the agreements. The Company considers this risk minimal. The Company maintains an overcollateralized position that is sufficient to cover any minor interest rate movements.

Throughout 2016, the Company executed several balance sheet restructuring strategies in an effort to reduce reliance on wholesale funding. These strategies will continue to be evaluated in the future. A summary of prepayments of wholesale structured repurchase agreements related to these restructurings is summarized in the following table for the year ended December 31, 2016.

	2016				
Date of Restructuring	Amount	Weighted Average Interest Rate		Range of Maturity Dates	Prepayment Fees
First Quarter of 2016	$ 10,000,000	3.97	%	July 2018	$ 759,000
Third Quarter of 2016	55,000,000	3.27	%	February 2019 to September 2020	4,010,000
Total for 2016	$ 65,000,000	3.38	%		$ 4,769,000

All prepayment fees shown in the table above are included in losses on debt extinguishment in the statements of income. There were no material modifications of borrowings during 2018 or 2017.

Maturity and interest rate information concerning wholesale structured repurchase agreements is summarized as follows:

	December 31, 2018		December 31, 2017	
	Amount Due	Weighted Average Interest Rate at Year-End	Amount Due	Weighted Average Interest Rate at Year-End
Maturity:				
Year ending December 31:				
2019	$ 10,000,000	3.59 %	$ 10,000,000	3.44 %
2020	25,000,000	2.48	25,000,000	2.48
Total Wholesale Structured Repurchase Agreements	$ 35,000,000	2.80 %	$ 35,000,000	2.76 %

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 11. Other Borrowings and Unused Lines of Credit (continued)

The Company has two term notes. The first is a term note with a maturity date of December 31, 2021. The outstanding balance on the term note totals $18.0 million and $24.0 million at December 31, 2018 and 2017, respectively. Interest on the term note is calculated at the effective LIBOR rate plus 3.00% per annum (5.52% and 4.56% at December 31, 2018 and 2017, respectively). The proceeds from this note were used to fund a portion of the cash consideration for the acquisition of CSB. The second is a term note originated in the third quarter of 2017 with a maturity date of December 31, 2021 and a balance outstanding of $5.3 million and $7.0 million at December 31, 2018 and 2017, respectively. Interest is calculated at the effective LIBOR rate plus 3.00% per annum (5.52% and 4.56% at December 31, 2018 and 2017, respectively). The proceeds from this note were used to fund a portion of the cash consideration for the acquisition of Guaranty Bank. The collateral on both borrowings is the original stock certificates and stock powers of all bank subsidiaries.

For the term notes, the Company is required to make quarterly principal payments of $1,937,500 with maturity information as of December 31, 2018, summarized as follows:

	As of December 31, 2018
2019	$ 7,750,000
2020	7,750,000
2021	7,750,000
	$ 23,250,000

As part of the merger with Springfield Bancshares, the Company assumed two subordinated debentures with a fair value of $4.8 million. Maturity and interest rate information concerning the subordinated debentures is summarized as follows:

	Amount Outstanding as of December 31, 2018	Interest Rate as of December 31, 2018	Maturity Date
Subordinated debenture dated 4/30/16	$ 2,000,000	4.00 %	4/30/2026
Subordinated debenture dated 9/15/16	3,000,000	4.00 %	9/15/2026
Market Value Discount per ASC 805	(217,682)		
Total Subordinated Debentures	$ 4,782,318		

The interest rate on the subordinated debentures is fixed for the first five years of the term and then converts to floating for the remaining term, at a rate of Prime floating daily. The debentures may be called after a minimum of five years following issuance and at the prior approval of the appropriate regulatory agencies. The subordinated debentures are unsecured.

The Company has a $10.0 million revolving line of credit note for which the outstanding balance is $9.0 million as of December 31, 2018. Interest on the revolving line of credit is calculated at the effective LIBOR rate plus 2.50% per annum (5.02% at December 31, 2018). The collateral on the revolving line of credit is the original stock certificates and stock powers of all bank subsidiaries.

In February 2019, the Company completed a subordinated notes offering, a portion of the proceeds of which were used to pay off outstanding term notes and the revolving line of credit. See Note 23 of the Consolidated Financial Statements for further information on this subsequent event.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 11. Other Borrowings and Unused Lines of Credit (continued)

Unused lines of credit of the subsidiary banks as of December 31, 2018 and 2017 are summarized as follows:

	2018	2017
Secured	$ 1,690,108	$ 2,967,441
Unsecured	362,000,000	372,000,000
	$ 363,690,108	$ 374,967,441

The Company pledges select C&I and CRE loans to the Federal Reserve Bank of Chicago for borrowing at the Discount Window.

Note 12.Junior Subordinated Debentures

Junior subordinated debentures are summarized as of December 31, 2018 and 2017 as follows:

	2018	2017
Note Payable to QCR Holdings Capital Trust II	$ 10,310,000	$ 10,310,000
Note Payable to QCR Holdings Capital Trust III	8,248,000	8,248,000
Note Payable to QCR Holdings Capital Trust V	10,310,000	10,310,000
Note Payable to Community National Trust II	3,093,000	3,093,000
Note Payable to Community National Trust III	3,609,000	3,609,000
Note Payable to Guaranty Bankshares Statutory Trust I*	4,640,000	4,640,000
Market Value Discount per ASC 805**	(2,539,957)	(2,723,513)
	$ 37,670,043	$ 37,486,487

* As part of the acquisition of Guaranty Bank, the Company assumed one junior subordinated debenture with a fair value of $3,857,275.

** Market value discount includes discount on junior subordinated debt acquired in 2013 as part of the purchase of Community National and junior subordinated debt acquired in 2017 as part of the purchase of Guaranty Bank.

A schedule of the Company’s non-consolidated subsidiaries formed for the issuance of trust preferred securities, including the amounts outstanding as of December 31, 2018 and 2017, is as follows:

Amount Outstanding December 31,	Amount Outstanding December 31,	Interest Rate as of	Interest Rate as of

Name	Date Issued	2018	2017	Interest Rate	December 31, 2018	December 31, 2017
QCR Holdings Statutory Trust II*	February 2004	$ 10,310,000	$ 10,310,000	2.85% over 3-month LIBOR	5.65 %	4.54 %
QCR Holdings Statutory Trust III	February 2004	8,248,000	8,248,000	2.85% over 3-month LIBOR	5.65 %	4.54 %
QCR Holdings Statutory Trust V	February 2006	10,310,000	10,310,000	1.55% over 3-month LIBOR	3.99 %	2.91 %
Community National Statutory Trust II	September 2004	3,093,000	3,093,000	2.17% over 3-month LIBOR	4.96 %	3.80 %
Community National Statutory Trust III	March 2007	3,609,000	3,609,000	1.75% over 3-month LIBOR	4.54 %	3.32 %
Guaranty Bankshares Statutory Trust I	May 2005	4,640,000	4,640,000	1.75% over 3-month LIBOR	4.54 %	3.34 %
		$ 40,210,000	$ 40,210,000	Weighted Average Rate	4.94 %	3.82 %

* Original amount issued for QCR Holdings Statutory Trust II was $12,372,000.

Securities issued by all of the trusts listed above mature 30 years from the date of issuance, but all are currently callable at par at any time. Interest rate reset dates vary by Trust.

In 2016, the Company extinguished $5.1 million of the QCR Holdings Capital Trust IV junior subordinated debentures (the full balance outstanding) and recorded a $1.2 million gain on extinguishment (pre-tax), as the Company was able to acquire the related security at a discount through auction. This gain is included within the overall net losses on debt extinguishments in the statements of income for 2016. The interest rate on these debentures floated at 3 month LIBOR plus 1.80% and had a rate of 2.42% at the time of extinguishment. QCR Holdings Capital Trust IV was dissolved after the extinguishment.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 12.Junior Subordinated Debentures (continued)

Interest rate swaps are also used for the purpose of hedging interest rate risk on junior subordinated debt. See Note 7 to the Consolidated Financial Statements for the details of these instruments.

Note 13. Federal and State Income Taxes

Federal and state income tax expense was comprised of the following components for the years ended December 31, 2018, 2017, and 2016:

	2018	2017	2016
Current	$ 2,722,635	$ 10,976,005	$ 11,969,194
Deferred	6,292,477	(6,029,555)	(3,066,407)
	$ 9,015,112	$ 4,946,450	$ 8,902,787

A reconciliation of the expected federal income tax expense to the income tax expense included in the consolidated statements of income was as follows for the years ended December 31, 2018, 2017, and 2016:

	Year Ended December 31,					
	2018		2017		2016	
	Amount	% of Pretax Income	Amount	% of Pretax Income	Amount	% of Pretax Income
Computed "expected" tax expense	$ 10,948,310	21.0 %	$ 14,228,535	35.0 %	$ 12,806,351	35.0 %
Effect of graduated tax rates	—	—	—	—	(250,013)	(0.7)
Tax exempt income, net	(3,957,851)	(7.6)	(5,653,979)	(13.9)	(4,343,270)	(11.9)
Bank-owned life insurance	(342,667)	(0.6)	(630,855)	(1.5)	(619,988)	(1.7)
State income taxes, net of federal benefit, current year	2,680,581	5.2	1,764,671	4.3	1,245,524	3.4
Change in unrecognized tax benefits	(44,629)	(0.1)	(53,699)	(0.1)	121,008	0.3
New Markets Tax Credits and other credits	(154,200)	(0.3)	(341,268)	(0.8)	(180,000)	(0.5)

Acquisition costs	226,599	0.4		—	—		176,050	0.5	
Excess tax benefit on stock options exercised and restricted stock awards vested	(425,142)	(0.8)		(1,219,483)	(3.0)		—	—	
Re-measurement of deferred tax asset to incorporate newly enacted tax rates	—	—		(2,918,606)	(7.2)		—	—	
Other	84,111	0.1		(228,866)	(0.6)		(52,875)	(0.1)	
Federal and state income tax expense	$ 9,015,112	17.3	%	$ 4,946,450	12.2	%	$ 8,902,787	24.3	%

Changes in the unrecognized tax benefits included in other liabilities are as follows for the years ended December 31, 2018 and 2017:

	2018	2017
Balance, beginning	$ 1,293,268	$ 1,346,967
Impact of tax positions taken during current year	286,994	333,253
Gross decrease related to tax positions of prior years	(178,058)	(40,584)
Reduction as a result of a lapse of the applicable statute of limitations	(153,565)	(346,368)
Balance, ending	$ 1,248,639	$ 1,293,268

Included in the unrecognized tax benefits liability at December 31, 2018 are potential benefits of approximately $1.0 million that, if recognized, would affect the effective tax rate.

The liability for unrecognized tax benefits includes accrued interest for tax positions, which either do not meet the more-likely-than-not recognition threshold or where the tax benefit is measured at an amount less than the tax benefit claimed or expected to be claimed on an income tax return. At December 31, 2018 and 2017, accrued interest on uncertain tax positions was approximately $205 thousand and $150 thousand, respectively. Estimated interest related to the underpayment of income taxes is classified as a component of “income tax expense” in the statements of income.

The Company’s federal income tax returns are open and subject to examination from the 2015 tax return year and later. Various state franchise and income tax returns are generally open from the 2014 and later tax return years based on individual state statutes of limitations.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 13. Federal and State Income Taxes (continued)

The net deferred tax assets consisted of the following as of December 31, 2018 and 2017:

	2018	2017
Deferred tax assets:		
Alternative minimum tax credits	$ 2,911,031	$ 6,513,502
Historic tax credits	1,937,170	—
New markets tax credits	—	2,164,727
Net unrealized losses on securities available for sale and derivative instruments	1,687,162	498,860
Compensation	6,771,593	6,282,603
Loan/lease losses	9,548,985	8,029,714
Net operating loss carryforwards, federal and state	849,335	959,627
Other	52,738	34,962
	23,758,014	24,483,995
Deferred tax liabilities:		
Premises and equipment	2,716,592	2,400,397
Equipment financing leases	18,329,372	15,367,705
Acquisition fair value adjustments	2,739,038	1,864,599
Investment accretion	30,533	30,656
Deferred loan origination fees, net	482,380	115,153
Other	424,335	430,125
	24,722,250	20,208,635
Net deferred tax assets (liabilities)	$ (964,236)	$ 4,275,360

At December 31, 2018, the Company had $4.0 million of federal tax net operating loss carryforwards which are set to expire in varying amounts between 2029 and 2033. At December 31, 2018, the Company had $2.1 million of state tax net operating loss carryforwards which are set to expire in varying amounts between 2023 and 2028. All of the federal tax net operating loss carryforwards and the state tax net operating loss carryforwards were acquired from Community National and CNB.

The change in deferred income taxes was reflected in the Consolidated Financial Statements as follows for the years ended December 31, 2018, 2017, and 2016:

	2018	2017	2016
Provision for income taxes	$ 6,292,477	$ (6,029,555)	$ (3,066,407)
Net deferred tax asset acquired	—	—	(3,310,553)
Net deferred tax asset resulting from acquisition adjustments	(52,717)	243,195	5,110,015
Re-measurement of deferred tax asset to incorporate newly enacted tax rates	—	2,918,606	—

Statement of stockholders' equity- Other comprehensive income (loss)	(1,000,164)	668,085	(202,691)
	$ 5,239,596	$ (2,199,669)	$ (1,469,636)

The Tax Act was enacted on December 22, 2017 and reduces the federal corporate tax rate from 35% to 21%. As a result, the Company revalued the deferred tax assets and liabilities to reflect the lower federal corporate tax rate, which resulted in the Company recognizing a benefit of $2.9 million in the fourth quarter of 2017. Additionally, while the Tax Act eliminated the corporate alternative minimum tax, it did preserve the alternative minimum tax credit and the usability.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 14. Employee Benefit Plans

The Company has a profit sharing plan which includes a provision designed to qualify under Section 401(k) of the Internal Revenue Code of 1986, as amended, to allow for participant contributions. All employees are eligible to participate in the plan. The Company matches 100% of the first 3% of employee contributions, and 50% of the next 3% of employee contributions, up to a maximum amount of 4.5% of an employee's compensation. Additionally, at its discretion, the Company may make additional contributions to the plan which are allocated to the accounts of participants in the plan based on relative compensation. There were no discretionary contributions for the years ended December 31, 2018, 2017 and 2016. Company matching contributions for the years ended December 31, 2018, 2017, and 2016 were as follows:

	2018	2017	2016
Matching contribution	$ 2,000,257	$ 1,663,198	$ 1,365,111

The Company has entered into nonqualified supplemental executive retirement plans (SERPs) with certain executive officers. The SERPs allow certain executives to accumulate retirement benefits beyond those provided by the qualified plans. Changes in the liability related to the SERPs, included in other liabilities, are as follows for the years ended December 31, 2018, 2017 and 2016:

	2018	2017	2016
Balance, beginning	$ 4,330,313	$ 4,093,355	$ 3,934,605
Increase in	456,782	400,784	322,575
Cash payments made	(163,826)	(163,826)	(163,825)
Balance, ending	$ 4,623,269	$ 4,330,313	$ 4,093,355

The Company has entered into deferred compensation agreements with certain executive officers. Under the provisions of the agreements, the officers may defer compensation and the Company matches the deferral up to certain maximums. The Company's matching contribution varies by officer and is a maximum of between $8,000 and $25,000 annually. Interest on the deferred amounts is earned at The Wall Street Journal's prime rate subject to a minimum of 4% and a maximum of 12% with such limits differing by officer. The Company has also entered into deferred compensation agreements with certain other officers. Under the provisions of the agreements the officers may defer compensation and the Company matches the deferral up to certain maximums. The Company's matching contribution differs by officer and is a maximum between 4% and 10% of the officer's compensation. Interest on the deferred amounts is earned at The Wall Street Journal's prime rate plus one percentage point, and has a minimum of 4% and shall not exceed 8%.

Upon retirement, the officer will receive the deferral balance in 180 equal monthly installments. As of December 31, 2018 and 2017, the liability related to the agreements totaled $15.0 million and $12.3 million, respectively.

Changes in the deferred compensation agreements, included in other liabilities, are as follows for the years ended December 31, 2018, 2017, and 2016:

	2018	2017	2016
Balance, beginning	$ 12,346,935	$ 10,455,183	$ 8,875,025
Employee deferrals	1,406,959	932,921	794,168
Company match and interest	1,367,776	1,024,933	848,831
Cash payments made	(92,265)	(66,102)	(62,841)
Balance, ending	$ 15,029,405	$ 12,346,935	$ 10,455,183

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 15. Stock-Based Compensation

The Company's Board of Directors adopted in January 2008, and the stockholders approved in May 2008, the QCR Holdings, Inc. 2008 Equity Incentive Plan ("2008 Equity Incentive Plan"). The Company's Board of Directors adopted in February 2010, and the stockholders approved in May 2010, the QCR Holdings, Inc. 2010 Equity Incentive Plan ("2010 Equity Incentive Plan"). The Company's Board of Directors adopted in February 2013, and the stockholders approved in May 2013, the QCR Holdings, Inc. 2013 Equity Incentive Plan ("2013 Equity Incentive Plan"). The Company's Board of Directors adopted in February 2016, and the stockholders approved in May 2016, the QCR Holdings, Inc. 2016 Equity Incentive Plan ("2016 Equity Incentive Plan"). Up to 250,000, 350,000, 350,000, and 400,000 shares of common stock, respectively, may be issued to employees and directors of the Company and its subsidiaries pursuant to equity incentive awards granted under these plans.

The 2008 Equity Incentive Plan, the 2010 Equity Incentive Plan, the 2013 Equity Incentive Plan, and the 2016 Equity Incentive Plan (collectively, the "Stock Option Plans") are administered by the Compensation Committee of the Board of Directors (the "Committee"). As of December 31, 2018, there were 302,066 remaining shares of common stock available for grant under the Stock Option Plans; however, such additional shares may be issued only under the 2016 Equity Incentive Plan.

The number and exercise price of options granted under the stock option plans are determined by the Committee at the time the option is granted. In no event can the exercise price be less than the value of the common stock at the date of the grant for stock options. All options have a 10 year life and will vest and become exercisable from 3 to 7 years after the date of the grant.

Stock-based compensation expense was reflected in the Consolidated Financial Statements as follows for the years ended December 31, 2018, 2017, and 2016.

	2018	2017	2016
Stock options	$ 471,849	$ 554,435	$ 424,904
Restricted stock awards	856,731	552,907	460,853
Stock purchase plan	114,766	79,694	61,417
	$ 1,443,346	$ 1,187,036	$ 947,174

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 15. Stock-Based Compensastion (continued)

Stock options:

A summary of the stock option plans as of December 31, 2018, 2017, and 2016 and changes during the years then ended is presented below:

	December 31, 2018		2017		2016	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Outstanding, beginning	513,554	$ 17.13	587,961	$ 14.83	623,176	$ 13.88
Granted	16,315	44.02	43,250	43.86	76,749	22.92
Exercised	(60,127)	13.56	(114,100)	15.12	(111,423)	14.97
Forfeited	(170)	16.81	(3,557)	26.74	(541)	18.36
Outstanding, ending	469,572	18.52	513,554	17.13	587,961	14.83
Exercisable, ending	358,270		354,269		385,372	
Weighted average fair value per option granted	$ 14.68		$ 14.75		$ 7.31	

A further summary of options outstanding as of December 31, 2018 is presented below:

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Number Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
$7.99 to $8.93	24,175	2.07	$ 8.10	24,175	$ 8.10
$9.00 to $9.30	121,724	2.10	9.21	121,724	9.21
$15.08 to $16.13	74,703	4.24	15.63	72,303	15.64
$17.10 to $18.00	125,137	5.56	17.31	99,573	17.29
$21.71 to $31.53	66,291	7.11	22.92	29,633	22.64
$42.65 to $48.50	57,542	8.46	43.94	10,862	43.79
	469,572			358,270	

Restricted stock awards:

A summary of changes in the Company's nonvested restricted stock awards as of December 31, 2018, 2017 and 2016 is presented below:

	December 31, 2018	2017	2016
Outstanding, beginning	46,389	39,438	45,046
Granted*	37,315	28,289	22,382
Released	(19,605)	(21,338)	(27,490)
Forfeited	—	—	(500)
Outstanding, ending	64,099	46,389	39,438
Weighted average fair value per share granted	$ 43.50	$ 44.44	$ 22.64

* Includes 22,660 of restricted stock awards and 14,655 of restricted stock units.

The total grant value of restricted stock awards that were released during the years ended December 31, 2018, 2017 and 2016 was $622 thousand, $509 thousand and $474 thousand, respectively.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 15. Stock-Based Compensation (continued):

Stock purchase plan:

The Company's Board of Directors and its stockholders adopted in October 2002 the QCR Holdings, Inc. Employee Stock Purchase Plan (the "Purchase Plan"). On May 2, 2012, the Company's stockholders approved a complete amendment and restatement of the Purchase Plan. As of January 1, 2018, there were 175,507 shares of common stock available for issuance under the Purchase Plan. For each six-month offering period, the Board of Directors will determine how many of the total number of available shares will be offered. The purchase price is the lesser of 85% of the fair market value at the date of the grant or the investment date. The investment date, as established by the Board of Directors, is the date common stock is purchased after the end of each calendar quarter during an offering period. The maximum dollar amount any one participant can elect to contribute in an offering period is $10,000. Additionally, the maximum percentage that any one participant can elect to contribute is 10% of his or her compensation for the year ended December 31, 2018 and 2017 and 8% for the year ended December 31, 2016. Information for the stock purchase plan for the years ended December 31, 2018, 2017, and 2016 is presented below:

	2018	2017	2016
Shares granted	17,305	12,414	18,711
Shares purchased	15,528	13,318	20,192
Weighted average fair value per share granted	$ 6.63	$ 6.42	$ 3.28

Note 16. Regulatory Capital Requirements and Restrictions on Dividends

The Company (on a consolidated basis) and the subsidiary banks are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company and subsidiary banks' financial statements.

Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the subsidiary banks must meet specific capital guidelines that involve quantitative measures of their assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors. Quantitative measures established by regulation to ensure capital adequacy require the Company and the subsidiary banks to maintain minimum amounts and ratios (set forth in the following table) of total common equity Tier 1 and Tier 1 capital to risk-weighted assets and of Tier 1 capital to average assets, each as defined by regulation. Management believes, as of December 31, 2018 and 2017, that the Company and the subsidiary banks met all capital adequacy requirements to which they are subject.

Under the regulatory framework for prompt corrective action, to be categorized as “well capitalized,” an institution must maintain minimum total risk-based, Tier 1 risk-based, Tier 1 leverage and common equity Tier 1 ratios as set forth in the following tables. The Company and the subsidiary banks’ actual capital amounts and ratios as of December 31, 2018 and 2017 are also presented in the following table (dollars in thousands). As of December 31, 2018 and 2017, the subsidiary banks met the requirements to be “well capitalized”.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 16. Regulatory Capital Requirements and Restrictions on Dividends (continued)

	Actual		For Capital Adequacy Purposes		For Capital Adequacy Purposes With Capital Conservation Buffer*		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2018:								
Company:								
Total risk-based capital	$ 460,416	10.69 %	$ 344,551	> 8.00 %	$ 425,305	> 9.875 %	$ 430,689	> 10.00 %
Tier 1 risk-based capital	420,569	9.77 %	258,413	> 6.00	339,168	> 7.875	344,551	> 8.00
Tier 1 leverage	420,569	8.87 %	189,858	> 4.00	189,858	> 4.000	237,322	> 5.00
Common equity Tier 1	382,899	8.89 %	193,810	> 4.50	274,564	> 6.375	279,948	> 6.50
Quad City Bank & Trust:								
Total risk-based capital	$ 162,009	11.38 %	$ 113,900	> 8.00 %	$ 140,596	> 9.875 %	$ 142,376	> 10.00 %
Tier 1 risk-based capital	148,529	10.43 %	85,425	> 6.00	112,121	> 7.875	113,900	> 8.00
Tier 1 leverage	148,529	9.04 %	65,744	> 4.00	65,744	> 4.000	82,180	> 5.00
Common equity Tier 1	148,529	10.43 %	64,069	> 4.50	90,764	> 6.375	92,544	> 6.50
Cedar Rapids Bank & Trust:								
Total risk-based capital	$ 146,292	11.55 %	$ 101,310	> 8.00 %	$ 125,054	> 9.875 %	$ 126,637	> 10.00 %
Tier 1 risk-based capital	133,982	10.58 %	75,982	> 6.00	99,727	> 7.875	101,310	> 8.00
Tier 1 leverage	133,982	9.98 %	53,682	> 4.00	53,682	> 4.000	67,103	> 5.00
Common equity Tier 1	133,982	10.58 %	56,987	> 4.50	80,731	> 6.375	82,314	> 6.50
Community State Bank:								
Total risk-based capital	$ 75,233	11.24 %	$ 53,567	> 8.00 %	$ 66,122	> 9.875 %	$ 66,959	> 10.00 %
Tier 1 risk-based capital	69,101	10.32 %	40,175	> 6.00	52,730	> 7.875	53,567	> 8.00
Tier 1 leverage	69,101	9.19 %	30,070	> 4.00	30,070	> 4.000	37,588	> 5.00

Common equity Tier 1	69,101	10.32 %	30,131	>	4.50		42,686	>	6.375	43,523	>	6.50
Rockford Bank & Trust:												
Total risk-based capital	$ 50,648	10.89 %	$ 37,208	>	8.00	%	$ 45,929	>	9.875 %	$ 46,511	>	10.00 %
Tier 1 risk-based capital	44,821	9.64 %	27,906	>	6.00		36,627	>	7.875	37,208	>	8.00
Tier 1 leverage	44,821	8.93 %	20,081	>	4.00		20,081	>	4.000	25,101	>	5.00
Common equity Tier 1	44,821	9.64 %	20,930	>	4.50		29,650	>	6.375	30,232	>	6.50
Springfield First Community Bank:												
Total risk-based capital	$ 57,051	12.24 %	$ 37,278	>	8.00	%	$ 46,016	>	9.875 %	$ 46,598	>	10.00 %
Tier 1 risk-based capital	51,279	11.00 %	27,959	>	6.00		36,696	>	7.875	37,278	>	8.00
Tier 1 leverage	51,279	9.39 %	21,849	>	4.00		21,849	>	4.000	27,312	>	5.00
Common equity Tier 1	51,279	11.00 %	20,969	>	4.50		29,706	>	6.375	30,289	>	6.50

	Actual		For Capital Adequacy Purposes			For Capital Adequacy Purposes With Capital Conservation Buffer*			To Be Well Capitalized Under Prompt Corrective Action Provisions		
	Amount	Ratio	Amount		Ratio	Amount		Ratio	Amount		Ratio
As of December 31, 2017:											
Company:											
Total risk-based capital	$ 383,282	11.15 %	$ 275,090	>	8.00 %	$ 318,073	>	9.25 %	$ 343,862	>	10.00 %
Tier 1 risk-based capital	348,530	10.14 %	206,317	>	6.00	249,300	>	7.25	275,090	>	8.00
Tier 1 leverage	348,530	8.98 %	155,256	>	4.00	155,256	>	4.00	194,070	>	5.00
Common equity Tier 1	313,012	9.10 %	154,738	>	4.50	197,721	>	5.75	223,510	>	6.50
Quad City Bank & Trust:											
Total risk-based capital	$ 160,112	12.35 %	$ 103,711	>	8.00 %	$ 119,916	>	9.25 %	$ 129,639	>	10.00 %
Tier 1 risk-based capital	147,472	11.38 %	77,783	>	6.00	93,988	>	7.25	103,711	>	8.00
Tier 1 leverage	147,472	9.52 %	61,985	>	4.00	61,985	>	4.00	77,481	>	5.00
Common equity Tier 1	147,472	11.38 %	58,337	>	4.50	74,542	>	5.75	84,265	>	6.50
Cedar Rapids Bank & Trust:											

Total risk-based capital	$ 138,492	11.88 %	$ 93,272	>	8.00 %	$ 107,846	>	9.25 %	$ 116,590	>	10.00 %
Tier 1 risk-based capital	126,601	10.86 %	69,954	>	6.00	84,528	>	7.25	93,272	>	8.00
Tier 1 leverage	126,601	11.68 %	43,348	>	4.00	43,348	>	4.00	54,185	>	5.00
Common equity Tier 1	126,601	10.86 %	52,465	>	4.50	67,039	>	5.75	75,783	>	6.50
Community State Bank:											
Total risk-based capital	$ 66,271	11.71 %	$ 45,293	>	8.00 %	$ 52,370	>	9.25 %	$ 56,616	>	10.00 %
Tier 1 risk-based capital	61,941	10.94 %	33,970	>	6.00	41,047	>	7.25	45,293	>	8.00
Tier 1 leverage	61,941	9.77 %	25,354	>	4.00	25,354	>	4.00	31,693	>	5.00
Common equity Tier 1	61,941	10.94 %	25,477	>	4.50	32,554	>	5.75	36,801	>	6.50
Rockford Bank & Trust:											
Total risk-based capital	$ 45,684	11.28 %	$ 32,413	>	8.00 %	$ 37,477	>	9.25 %	$ 40,516	>	10.00 %
Tier 1 risk-based capital	40,615	10.02 %	24,310	>	6.00	29,374	>	7.25	32,413	>	8.00
Tier 1 leverage	40,615	8.94 %	18,177	>	4.00	18,177	>	4.00	22,721	>	5.00
Common equity Tier 1	40,615	10.02 %	18,232	>	4.50	23,297	>	5.75	26,335	>	6.50

* The minimums under Basel III increase by .625% (the capital conservation buffer) for all ratios other than Tier 1 leverage annually until 2019.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 16. Regulatory Capital Requirements and Restrictions on Dividends (continued)

The fully phased-in minimums are 10.5% (Total risk-based capital), 8.5% (Tier 1 risk-based capital), and 7.0% (Common equity Tier 1).

The Company's ability to pay dividends to its stockholders may be affected by both general corporate law considerations and policies of the Federal Reserve applicable to bank holding companies.

The payment of dividends by any financial institution or its holding company is affected by the requirement to maintain adequate capital pursuant to applicable capital adequacy guidelines and regulations, and a financial institution generally is prohibited from paying any dividends if, following payment thereof, the institution would be undercapitalized. Notwithstanding the availability of funds for dividends, however, the Federal Reserve may prohibit the payment of any dividends by the subsidiary banks if the Federal Reserve determines such payment would constitute an unsafe or unsound practice.

The Company also has certain contractual restrictions on its ability to pay dividends. The Company has issued junior subordinated debentures in four private placements and assumed three issues of junior subordinated debentures in connection with the acquisitions. Under the terms of the debentures, the Company may be prohibited, under certain circumstances, from paying dividends on shares of its common stock. These circumstances did not exist at December 31, 2018 or 2017.

The Company filed a universal shelf registration statement on Form S 3 with the SEC on October 27, 2016, as amended on January 11, 2017. Declared effective by the SEC on January 31, 2017, the registration statement allows the Company to offer and sell various types of securities, including common stock, preferred stock, debt securities and/or warrants, from time to time up to an aggregate amount of $100 million. The specific terms and prices of any securities offered pursuant to the registration statement will be determined at the time of any future offering and described in a separate prospectus supplement, which would be filed with the SEC at the time of the particular offering, if any. In February 2019, the Company completed a subordinated notes offering. See Note 23 of the Consolidated Financial Statements for further information on this subordinated notes offering.

Note 17. Earnings per Share

The following information was used in the computation of basic and diluted EPS for the years ended December 31, 2018, 2017, and 2016:

	2018	2017	2016
Net income	$ 43,119,699	$ 35,706,507	$ 27,686,787
Basic EPS	$ 2.92	$ 2.68	$ 2.20

Diluted EPS	$ 2.86	$ 2.61	$ 2.17
Weighted average common shares outstanding*	14,768,687	13,325,128	12,570,767
Weighted average common shares issuable upon exercise of stock options and under the employee stock purchase plan**	296,043	355,344	195,236
Weighted average common and common equivalent shares outstanding	15,064,730	13,680,472	12,766,003

* The increase in weighted average common shares outstanding from 2016 to 2018 was primarily due to the common stock issuances that occurred in conjunction with the Springfield Bancshares merger and Guaranty Bank acquisition.

** Excludes anti-dilutive shares of 91,954, 49,919, and 17,739 at December 31, 2018, 2017 and 2016, respectively.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 18. Commitments and Contingencies

In the normal course of business, the subsidiary banks make various commitments and incur certain contingent liabilities that are not presented in the accompanying Consolidated Financial Statements. The commitments and contingent liabilities include various guarantees, commitments to extend credit, and standby letters of credit.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The subsidiary banks evaluate each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the subsidiary banks upon extension of credit, is based upon management's credit evaluation of the counterparty. Collateral held varies but may include accounts receivable, marketable securities, inventory, property, plant and equipment, and income-producing commercial properties.

Standby letters of credit are conditional commitments issued by the subsidiary banks to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support public and private borrowing arrangements and, generally, have terms of one year or less. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The subsidiary banks hold collateral, as described above, supporting those commitments if deemed necessary. In the event the customer does not perform in accordance with the terms of the agreement with the third party, the subsidiary banks would be required to fund the commitments. The maximum potential amount of future payments the subsidiary banks could be required to make is represented by the contractual amount. If the commitment is funded, the subsidiary banks would be entitled to seek recovery from the customer. At December 31, 2018 and 2017, no amounts had been recorded as liabilities for the subsidiary banks' potential obligations under these guarantees.

As of December 31, 2018 and 2017, commitments to extend credit aggregated $1.2 billion and $791.6 million, respectively. As of December 31, 2018 and 2017, standby letters of credit aggregated $20.3 million and $17.3 million, respectively. Management does not expect that all of these commitments will be funded.

The Company has also executed contracts for the sale of mortgage loans in the secondary market in the amount of $1.3 million and $645 thousand as of December 31, 2018 and 2017, respectively. These amounts are included in loans held for sale at the respective balance sheet dates.

Residential mortgage loans sold to investors in the secondary market are sold with varying recourse provisions. Essentially, all loan sales agreements require the repurchase of a mortgage loan by the seller in situations such as breach of representation, warranty, or covenant, untimely document delivery, false or misleading statements, failure to obtain certain certificates of insurance, unmarketability, etc. Certain loan sales agreements contain repurchase requirements based on payment-related defects that are defined in terms of the number of days/months since the purchase, the sequence number of the payment, and/or the number of days of payment delinquency. Based on the specific terms stated in the agreements of investors purchasing residential mortgage loans from the Company's subsidiary banks, the Company had $12.4 million and $300 thousand of sold residential mortgage loans with recourse provisions still in effect at December 31, 2018 and 2017, respectively. The subsidiary banks did not repurchase any

loans from secondary market investors under the terms of loans sales agreements during the years ended December 31, 2018, 2017, and 2016. In the opinion of management, the risk of recourse and the subsequent requirement of loan repurchase to the subsidiary banks is not significant, and accordingly no liabilities have been established related to such.

Aside from cash on-hand and in-vault, the majority of the Company’s cash is maintained at upstream correspondent banks. The total amount of cash on deposit, certificates of deposit, and federal funds sold exceeded federal insured limits by approximately $52.6 million and $42.9 million as of December 31, 2018 and 2017, respectively. In the opinion of management, no material risk of loss exists due to the financial condition of the upstream correspondent banks.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 18. Commitments and Contingencies (continued)

In an arrangement with Goldman Sachs, CRBT offers a cash management program for select customers. Based on a predetermined minimum balance, which must be maintained in the account, excess funds are automatically swept daily to an institutional money market fund administered by Goldman Sachs. At December 31, 2018 and 2017, the Company had $96.6 million and $136.0 million, respectively of customer funds invested in this cash management program. In the opinion of management, no material risk of loss exists due to the financial condition of Goldman Sachs.

Note 19. Quarterly Results of Operations (Unaudited)

	Year Ended December 31, 2018			
	March 2018	June 2018	September 2018	December 2018
Total interest income	$ 39,546,296	$ 40,798,214	$ 49,830,471	$ 52,704,261
Total interest expense	7,143,378	8,713,718	11,516,988	13,109,573
Net interest income	32,402,918	32,084,496	38,313,483	39,594,688
Provision for loan/lease losses	2,539,839	2,300,735	6,205,828	1,612,047
Noninterest income	8,541,449	8,912,266	8,808,825	15,278,554
Noninterest expense	25,863,497	26,369,823	30,499,610	36,410,489
Income before taxes	12,541,031	12,326,204	10,416,870	16,850,706
Federal and state income tax expense (benefit)	1,991,070	1,880,819	1,608,035	3,535,188
Net income	$ 10,549,961	$ 10,445,385	$ 8,808,835	$ 13,315,518
EPS:				
Basic	$ 0.76	$ 0.75	$ 0.56	$ 0.85
Diluted	$ 0.74	$ 0.73	$ 0.55	$ 0.84

	Year Ended December 31, 2017			
	March 2017	June 2017	September 2017	December 2017
Total interest income	$ 31,345,099	$ 32,453,268	$ 33,840,865	$ 37,878,086
Total interest expense	3,676,216	4,406,571	5,284,517	6,084,733
Net interest income	27,668,883	28,046,697	28,556,348	31,793,353
Provision for loan/lease losses	2,105,109	2,022,993	2,086,436	2,255,381
Noninterest income	7,283,754	6,782,518	6,701,303	9,714,717
Noninterest expense	21,273,117	21,404,629	23,395,747	31,351,204
Income before taxes	11,574,411	11,401,593	9,775,468	7,901,485
Federal and state income tax expense	2,389,446	2,635,576	1,921,533	(2,000,105)

Net income	$ 9,184,965	$ 8,766,017	$ 7,853,935	$ 9,901,590
EPS:				
Basic	$ 0.70	$ 0.67	$ 0.60	$ 0.72
Diluted	$ 0.68	$ 0.65	$ 0.58	$ 0.70

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 20. Parent Company Only Financial Statements

The following is condensed financial information of QCR Holdings, Inc. (parent company only):

Condensed Balance Sheets
December 31, 2018 and 2017

	2018	2017
Assets		
Cash and due from banks	$ 6,606,126	$ 4,325,582
Interest-bearing deposits at financial institutions	1,000,552	601
Securities available for sale, at fair value	—	1,690,726
Loans/leases receivable, held for investment	—	1,710,000
Investment in bank subsidiaries	532,163,635	410,105,525
Investment in nonbank subsidiaries	4,879,873	2,956,337
Premises and equipment, net	6,956,040	4,947,572
Goodwill	3,766,074	—
Intangibles	1,854,932	—
Other assets	14,794,944	11,630,304
Total assets	$ 572,022,176	$ 437,366,647
Liabilities and Stockholders' Equity		
Liabilities:		
Other borrowings	$ 32,250,000	$ 31,000,000
Junior subordinated debentures	37,670,043	37,486,487
Other liabilities	28,963,730	15,593,031
Total liabilities	98,883,773	84,079,518
Stockholders' Equity:		
Common stock	15,718,208	13,918,168
Additional paid-in capital	270,760,511	189,077,550
Retained earnings	192,203,333	151,962,661
Accumulated other comprehensive loss	(5,543,649)	(1,671,250)
Total stockholders' equity	473,138,403	353,287,129
Total liabilities and stockholders' equity	$ 572,022,176	$ 437,366,647

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 20. Parent Company Only Financial Statements (continued)

Condensed Statements of Income
Years Ended December 31, 2018, 2017, and 2016

	2018	2017	2016
Total interest income	$ 87,532	$ 12,802	$ 74,489
Equity in net income of bank subsidiaries	55,209,382	45,103,593	33,467,712
Equity in net income of nonbank subsidiaries	(435,941)	75,344	32,674
Securities gains	—	6,312	37,596
Other	(322,119)	2,700	(2,933)
Total income	54,538,854	45,200,751	33,609,538
Interest expense	3,637,126	2,658,414	1,735,769
Salaries and employee benefits	6,597,881	5,021,998	4,607,887
Professional fees	1,871,655	1,344,721	949,442
Acquisition costs	1,654,323	1,068,918	1,400,004
Post-acquisition compensation, transition and integration costs	165,314	3,151,384	313,598
Gains on debt extinguishment	—	—	(1,200,000)
Other	1,026,016	1,134,139	988,057
Total expenses	14,952,315	14,379,574	8,794,757
Income before income tax benefit	39,586,539	30,821,177	24,814,781
Income tax benefit	3,533,160	4,885,330	2,872,006
Net income	$ 43,119,699	$ 35,706,507	$ 27,686,787

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 20. Parent Company Only Financial Statements (continued)

Condensed Statements of Cash Flows
Years Ended December 31, 2018, 2017, and 2016

	2018	2017	2016
Cash Flows from Operating Activities:			
Net income	$ 43,119,699	$ 35,706,507	$ 27,686,787
Adjustments to reconcile net income to net cash provided by operating activities:			
Earnings of bank subsidiaries	(55,209,382)	(45,103,593)	(33,467,712)
Earnings (losses) of nonbank subsidiaries	435,941	(75,344)	(32,674)
Distributions from bank subsidiaries	34,500,000	21,000,000	26,000,000
Distributions from nonbank subsidiaries	63,270	38,734	32,860
Accretion of acquisition fair value adjustments	183,556	149,010	136,150
Depreciation	248,827	225,947	222,256
Stock-based compensation expense	1,443,346	1,187,036	947,174
Securities gains, net	—	(6,312)	(37,596)
Gains on debt extinguishment	—	—	(1,200,000)
Decrease (increase) in other assets	2,232,402	(968,808)	(2,346,253)
(Decrease) increase in other liabilities	(7,226,127)	(6,918,921)	5,105,251
Net cash provided by operating activities	19,791,532	5,234,256	23,046,243
Cash Flows from Investing Activities:			
Net increase (decrease) in interest-bearing deposits at financial institutions	(999,951)	50	50
Activity in securities portfolio:			
Purchases	—	—	(3,873,060)
Calls, maturities and redemptions	—	6,312	3,800,000
Sales	—	31,713	132,738
Capital infusion, bank subsidiaries	(3,500,000)	—	—
Net cash paid for acquisitions	(5,182,804)	(3,368,909)	(80,000,000)
Purchase of premises and equipment	(2,257,295)	(68,842)	(824,498)
Net cash (used in) investing activities	(11,940,050)	(3,399,676)	(80,764,770)
Cash Flows from Financing Activities:			
Activity in other borrowings:			
Proceeds from other borrowings	9,000,000	7,000,000	35,000,000
Calls, maturities and scheduled principal payments	(12,550,000)	(11,000,000)	—
Retirement of junior subordinated debentures	—	—	(3,955,000)

Payment of cash dividends on common and preferred stock	(3,300,091)	(2,494,260)	(1,981,541)
Proceeds from issuance of common stock, net	1,279,153	2,055,507	31,934,690
Net cash provided by (used in) financing activities	(5,570,938)	(4,438,753)	60,998,149
Net increase (decrease) in cash and due from banks	2,280,544	(2,604,173)	3,279,622
Cash and due from banks:			
Beginning	4,325,582	6,929,755	3,650,133
Ending	$ 6,606,126	$ 4,325,582	$ 6,929,755

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 21. Fair Value

Accounting guidance on fair value measurements uses a hierarchy intended to maximize the use of observable inputs and minimize the use of unobservable inputs. This hierarchy includes three levels and is based upon the valuation techniques used to measure assets and liabilities. The three levels are as follows:

- Level 1 – Inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in markets;
- Level 2 – Inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument; and
- Level 3 – Inputs to the valuation methodology are unobservable and significant to the fair value measurement

Assets measured at fair value on a recurring basis comprised the following at December 31, 2018 and 2017:

		Fair Value Measurements at Reporting Date Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2018:				
Securities AFS:				
U.S. govt. sponsored agency securities	$ 36,411,391	$ —	$ 36,411,391	$ —
Residential mortgage-backed and related securities	159,249,260	—	159,249,260	—
Municipal securities	58,546,022	—	58,546,022	—
Other securities	6,849,775	—	6,849,775	—
Interest rate caps	458,812	—	458,812	—
Interest rate swaps - assets	22,195,713	—	22,195,713	—
Total assets measured at fair value	$ 283,710,973	$ —	$ 283,710,973	$ —
Interest rate swaps - liabilities	$ 23,346,887	$ —	$ 23,346,887	$ —
Total liabilities measured at fair value	$ 23,346,887	$ —	$ 23,346,887	$ —
December 31, 2017:				
Securities AFS:				
U.S. govt. sponsored agency securities	$ 38,096,534	$ —	$ 38,096,534	$ —
Residential mortgage-backed and related securities	163,301,304	—	163,301,304	—
Municipal securities	66,625,496	—	66,625,496	—
Other securities	4,884,573	1,028	4,883,545	—

Interest rate caps	506,700	—	506,700	—
Interest rate swaps - assets	4,397,238	—	4,397,238	—
Total assets measured at fair value	$ 277,811,845	$ 1,028	$ 277,810,817	$ —
Interest rate swaps - liabilities	$ 4,397,238	$ —	$ 4,397,238	$ —
Total liabilities measured at fair value	$ 4,397,238	$ —	$ 4,397,238	$ —

There were no transfers of assets or liabilities between Levels 1, 2, and 3 of the fair value hierarchy during the years ended December 31, 2018 or 2017.

The remainder of the securities available for sale portfolio consists of securities whereby the Company obtains fair values from an independent pricing service. The fair values are determined by pricing models that consider observable market data, such as interest rate volatilities, LIBOR yield curve, credit spreads and prices from market makers and live trading systems (Level 2 inputs).

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 21. Fair Value (continued)

Interest rate caps are used for the purpose of hedging interest rate risk. See Note 7 to the Consolidated Financial Statements for the details of these instruments. The fair values are determined by pricing models that consider observable market data for derivative instruments with similar structures (Level 2 inputs).

Interest rate swaps are executed for select commercial customers. See Note 7 to the Consolidated Financial Statements for the detail of these instruments. The fair values are determined by comparing the contractual rate on the swap with the then-current market rate for the remaining term of the transaction (Level 2 inputs).

Interest rate swaps are also used for the purpose of hedging interest rate risk on junior subordinated debt. See Note 7 to the Consolidated Financial Statements for the details of these instruments. The fair values are determined by comparing the contract rate on the swap with the then-current market rate for the remaining term of the transaction (Level 2 inputs).

Certain financial assets are measured at fair value on a non-recurring basis; that is, the assets are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment).

Assets measured at fair value on a non-recurring basis comprised the following at December 31, 2018 and 2017:

		Fair Value Measurements at Reporting Date Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
December 31, 2018:				
Impaired loans/leases	$ 9,656,912	$ —	$ —	$ 9,656,912
OREO	10,127,954	—	—	10,127,954
	$ 19,784,866	$ —	$ —	$ 19,784,866
December 31, 2017:				
Impaired loans/leases	$ 8,972,337	$ —	$ —	$ 8,972,337
OREO	14,642,973	—	—	14,642,973
	$ 23,615,310	$ —	$ —	$ 23,615,310

Impaired loans/leases are evaluated and valued at the time the loan/lease is identified as impaired, at the lower of cost or fair value, and are classified as a Level 3 in the fair value hierarchy. Fair value is measured based on the value of the collateral securing these loans/leases. Collateral may be real estate and/or business assets including equipment, inventory and/or accounts receivable and is determined based on appraisals by qualified licensed appraisers hired by

the Company. Appraised and reported values may be discounted based on management's historical knowledge, changes in market conditions from the time of valuation, and/or management's expertise and knowledge of the client and client's business.

Other real estate owned in the table above consists of property acquired through foreclosures and settlements of loans. Property acquired is carried at the estimated fair value of the property, less disposal costs, and is classified as a Level 3 in the fair value hierarchy. The estimated fair value of the property is determined based on appraisals by qualified licensed appraisers hired by the Company. Appraised and reported values are discounted based on management's historical knowledge, changes in market conditions from the time of valuation, and/or management's expertise and knowledge of the property.

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 21. Fair Value (continued)

The following table presents additional quantitative information about assets measured at fair value on a non-recurring basis for which the Company has utilized Level 3 inputs to determine fair value:

	Quantitative Information about Level Fair Value Measurements					
	Fair Value December 31, 2018	Fair Value December 31, 2017	Valuation Technique	Unobservable Input	Range	
Impaired loans/leases	$ 9,656,912	$ 8,972,337	Appraisal of collateral	Appraisal adjustments	(10.00)% to	(30.00)%
OREO	10,127,954	14,642,973	Appraisal of collateral	Appraisal adjustments	0.00 % to	(35.00)%

For impaired loans/leases and other real estate owned, the Company records carrying value at fair value less disposal or selling costs. The amounts reported in the tables above are fair values before the adjustment for disposal or selling costs.

There have been no changes in valuation techniques used for any assets measured at fair value during the years ended December 31, 2018 or 2017.

The following table presents the carrying values and estimated fair values of financial assets and liabilities carried on the Company's consolidated balance sheet, including those financial assets and liabilities that are not measured and reported at fair value on a recurring basis or non-recurring basis:

	Fair Value Hierarchy Level	As of December 31, 2018 Carrying Value	As of December 31, 2018 Estimated Fair Value	As of December 31, 2017 Carrying Value	As of December 31, 2017 Estimated Fair Value
Cash and due from banks	Level 1	$ 85,522,685	$ 85,522,685	$ 75,721,663	$ 75,721,663
Federal funds sold	Level 2	26,398,000	26,398,000	30,197,000	30,197,000
Interest-bearing deposits at financial institutions	Level 2	133,198,095	133,198,095	55,765,012	55,765,012
Investment securities:					
HTM	Level 2	401,912,885	400,770,583	379,474,205	379,749,804
AFS		261,056,448	261,056,448	272,907,907	272,907,907

	See Previous Table				
Loans/leases receivable, net	Level 3	8,941,585	9,656,912	8,307,719	8,972,337
Loans/leases receivable, net	Level 2	3,683,965,349	3,639,329,000	2,921,821,953	2,892,963,000
Interest rate caps	Level 2	458,812	458,812	506,700	506,700
Interest rate swaps - assets	Level 2	22,195,713	22,195,713	4,397,238	4,397,238
Deposits:					
Nonmaturity deposits	Level 2	3,002,326,538	3,002,326,538	2,670,583,178	2,670,583,178
Time deposits	Level 2	974,704,036	968,906,000	596,071,878	591,772,000
Short-term borrowings	Level 2	28,774,157	28,774,157	13,993,122	13,993,122
FHLB advances	Level 2	266,492,039	265,926,000	192,000,000	192,115,000
Other borrowings	Level 2	72,032,318	72,703,000	66,000,000	66,520,000
Junior subordinated debentures	Level 2	37,670,043	29,992,198	37,486,487	29,253,624
Interest rate swaps - liabilities	Level 2	23,346,887	23,346,887	4,397,238	4,397,238

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 22. Business Segment Information

Selected financial and descriptive information is required to be disclosed for reportable operating segments, applying a “management perspective” as the basis for identifying reportable segments. The management perspective is determined by the view that management takes of the segments within the Company when making operating decisions, allocating resources, and measuring performance. The segments of the Company have been defined by the structure of the Company’s internal organization, focusing on the financial information that the Company’s operating decision-makers routinely use to make decisions about operating matters.

The Company’s primary segment, Commercial Banking, is geographically divided by markets into the secondary segments which are the five subsidiary banks wholly-owned by the Company: QCBT, CRBT, CSB, RB&T and SFC Bank. Each of these secondary segments offer similar products and services, but are managed separately due to different pricing, product demand, and consumer markets. Each offers commercial, consumer, and mortgage loans and deposit services.

The Company’s Wealth Management segment represents trust and asset management and investment management and advisory services offered at the Company’s three subsidiary banks in aggregate. This segment generates income primarily from fees charged based on assets under administration for corporate and personal trusts, custodial services, and investments managed. No assets of the subsidiary banks have been allocated to the Wealth Management segment.

The Company’s All Other segment includes the corporate operations of the parent and operations of all other consolidated subsidiaries and/or defined operating segments that fall below the segment reporting thresholds.

131

Table of Contents

QCR Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 22. Business Segment Information (continued)

Selected financial information on the Company's business segments, with all intercompany accounts and transactions eliminated, is presented as follows as of and for the years ended December 31, 2018, 2017, and 2016:

nking CRBT	Guaranty Bank*	CSB	SFC Bank	RB&T	Wealth Management	All other
$ 69,864,300	$ —	$ 36,069,287	$ 15,153,047	$ 20,848,171	$ 13,432,963	$ 232,624
43,038,038	—	28,762,834	11,834,782	13,638,969	—	(3,561,502)
1,833,226	—	1,523,462	990,000	4,618,833	—	—
20,044,067	—	8,389,007	4,816,326	667,809	2,951,991	(12,096,341)
14,979,984	—	9,888,225	45,974,931	—	—	3,766,074
3,186,136	—	4,674,613	7,734,501	—	—	1,854,932
1,379,222,278	—	785,363,891	632,849,228	509,621,731	—	45,671,799
$ 45,367,035	$ 1,806,078	$ 31,944,152	$ —	$ 18,035,971	$ 11,057,519	$ 232,660
31,042,302	1,551,356	27,020,674	—	12,707,651	—	(2,663,780)
1,050,000	—	2,783,000	—	728,000	—	—
10,712,174	346,835	7,047,671	—	2,660,364	2,241,494	(9,397,086)
15,223,179	—	9,888,225	—	—	—	—
3,693,592	—	5,385,361	—	—	—	—
1,307,376,687	—	670,516,373	—	461,650,765	—	28,267,478
$ 37,242,901	$ —	$ 11,406,291	$ —	$ 16,043,894	$ 9,156,948	$ 109,563
29,205,047	—	10,004,729	—	11,887,201	—	(1,661,280)
950,000	—	1,460,000	—	900,000	—	—
12,317,545	—	2,132,252	—	3,235,711	1,665,453	(5,780,925)
—	—	9,888,225	—	—	—	—
1,271,897	—	6,109,316	—	—	—	—
913,055,738	—	600,075,798	—	391,154,780	—	34,998,902

* Represents financial results for Guaranty Bank for the period from October 1, 2017 through December 2, 2017, when Guaranty Bank was merged into CRBT.

Note 23. Subsequent Event: Subordinated Notes

On February 12, 2019 the Company completed an underwritten public offering of $65.0 million in aggregate principal amount of 5.375% Fixed-to-Floating Rate Subordinated Notes maturing on February 15, 2029. Net proceeds, after deducting the underwriting discount and estimated expenses, were approximately $63.5 million. Immediately following issuance, the Company repaid term notes totaling $21.4 million and the outstanding balance of $9.0 million on its revolving line of credit. This debt is included in Other Borrowings on the December 31, 2018 Consolidated Balance Sheet with balances of $23.3 million and $9.0 million, respectively, as of that date. The Company intends to use the remaining net proceeds from this offering for general corporate purposes, including the pursuit of possible opportunistic acquisitions of similar or complementary financial service organizations, repaying indebtedness, financing investments and capital expenditures, repurchasing shares of our common stock, investing in the subsidiary banks as regulatory capital and other strategic opportunities that may arise in the future.

The Subordinated Notes bear interest at a fixed rate of 5.375% per year until and including February 12, 2024. After this date, the interest rate will change to three-month LIBOR plus 282 points until the maturity date.

The Notes are subordinate to all exisiting debt and general creditors.

Table of Contents

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures

Evaluation of disclosure controls and procedures. An evaluation was performed under the supervision and with the participation of the Company's management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rule 13a 15(e) and 15d – 15(e) promulgated under the Exchange Act) as of December 31, 2018. Based on that evaluation, the Company's management, including the Chief Executive Officer and Chief Financial Officer, concluded that the Company's disclosure controls and procedures were effective to ensure that information required to be disclosed in the reports filed and submitted under the Exchange Act was: (1) accumulated and communicated to our management, including the Chief Executive Officer and Chief Financial Officer, to allow for timely decisions regarding required disclosures; and (2) recorded, processed, summarized and reported as and when required.

Management's Report on Internal Control over Financial Reporting. The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a 15(f) and 15d 15(f) of the Exchange Act). Internal control over financial reporting includes controls and procedures designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Internal control over financial reporting includes those policies and procedures that: (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions of the Company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the financial statements.

All internal control systems, no matter how well designed, have inherent limitations, including the possibility of human error and the circumvention of overriding controls. Accordingly, even effective internal control can provide only reasonable assurance with respect to financial statement preparation. Further, because of changes in conditions, the effectiveness of internal control may vary over time.

The Company's management has excluded SFC Bank and the Bates Companies from its assessment of internal control over financial reporting as of December 31, 2018, because they were acquired by the Company in the third and fourth quarter of 2018, respectively.

The Company's management assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2018. Management's assessment is based on the criteria established in the Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013 and was designed to provide reasonable assurance that the Company maintained effective internal control over financial reporting as of December 31, 2018. Based on this assessment, management believes that the Company maintained effective internal control over financial reporting as of December 31, 2018.

RSM US LLP, the Company's independent registered public accounting firm has issued an attestation report on the Company's internal control over financial reporting as of December 31, 2018, which is included on the following pages of this Form 10 K.

133

Table of Contents

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of QCR Holdings, Inc.

Opinion on the Internal Control Over Financial Reporting

We have audited QCR Holdings, Inc. and subsidiaries' (the Company) internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013. In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the consolidated balance sheets of QCR Holdings, Inc. and subsidiaries as of December 31, 2018 and 2017, and the related consolidated statements of income, comprehensive income, changes in stockholders' equity and cash flows for each of the three years in the period ended December 31, 2018 and our report dated March 15, 2019 expressed an unqualified opinion.

As described in Management's Report on Internal Control over Financial Reporting, management has excluded Springfield First Community Bank (SFC Bank) and Bates Financial Advisors, Inc., Bates Financial Services, Inc., Bates Securities, Inc., and Bates Financial Group, Inc. (Bates Companies) from its assessment of internal control over financial reporting as of December 31, 2018, because they were acquired by the Company in business combinations in the third and fourth quarter, respectively, of 2018. We have also excluded these entities from our audit of internal control over financial reporting. SFC Bank and the Bates Companies are wholly owned subsidiaries whose total assets represent approximately 13% and less than 1%, respectively, of the Company's consolidated assets as of December 31, 2018.

Basis for Opinion

The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's

internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

Table of Contents

Definition and Limitations of Internal Control Over Financial Reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Davenport, Iowa

March 15, 2019

135

Table of Contents

Changes in Internal Control over Financial Reporting. There have been no significant changes to the Company's internal control over financial reporting during the period covered by this report that have materially affected, or are reasonably like to materially affect, the Company's internal control over financial reporting.

Item 9B. Other Information

None.

Table of Contents

Part III

Item 10. Directors, Executive Officers and Corporate Governance

The information required by this item is set forth under the captions “Proposal 1: Election of Directors,” “Corporate Governance and the Board of Directors” and “Section 16(a) Beneficial Ownership Reporting Compliance” in the Company’s 2019 Proxy Statement and is incorporated herein by reference.

Item 11. Executive Compensation

The information required by this item is set forth under the captions “Executive Compensation” and “Director Compensation” in the Company’s 2019 Proxy Statement and is incorporated herein by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The information required by this item is set forth under the caption “Security Ownership of Certain Beneficial Owners” in the Company’s 2019 Proxy Statement and is incorporated herein by reference.

The table below sets forth the following information as of December 31, 2018 for (i) all compensation plans previously approved by the Company’s stockholders and (ii) all compensation plans not previously approved by the Company’s stockholders:

(a) The number of securities to be issued upon the exercise of outstanding options, warrants, and rights;
(b) The weighted-average exercise price of such outstanding options, warrants, and rights; and
(c) Other than securities to be issued upon the exercise of such outstanding options, warrants, and rights, the number of securities remaining available for future issuance under the plans.

EQUITY COMPENSATION PLAN INFORMATION

Plan category	Number of securities to be issued upon exercise of outstanding options, warrants, and rights (a)	Weighted-average exercise price of outstanding options, warrants, and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)	
Equity compensation plans approved by stockholders	488,673	$ 18.62	460,268	(1)
Equity compensation plans not approved by stockholders	—	—	—	
Total	488,673	$ 18.62	460,268	(1)

(1) Includes 158,202 shares available under the QCR Holdings, Inc. Employee Stock Purchase Plan.

Item 13. Certain Relationships and Related Transactions, and Director Independence

The information required by this item is set forth under the captions “Corporate Governance and the Board of Directors” and “Transactions with Management and Directors” in the Company’s 2019 Proxy Statement and is incorporated herein by reference.

Table of Contents

Item 14. Principal Accountant Fees and Services

The information required by this item is set forth under the caption “Proposal 3: Ratification of Selection of Independent Registered Public Accounting Firm” in the Company’s 2019 Proxy Statement and is incorporated herein by reference.

Table of Contents

Part IV

Item 15. Exhibits and Financial Statement Schedules

(a) 1. Financial Statements
These documents are listed in the Index to Consolidated Financial Statements under Item 8.

(a) 2. Financial Statement Schedules
Financial statement schedules are omitted, as they are not required or are not applicable, or the required information is shown in the Consolidated Financial Statements and the accompanying notes thereto.

(a) 3. Exhibits
The following exhibits are either filed as a part of this Annual Report on Form 10 K or are incorporated herein by reference:

Exhibit Number	Exhibit Description
2.1*	Agreement and Plan of Merger with Springfield Bancshares, Inc. dated as of April 17, 2018 (incorporated by reference to Exhibit 2.1 of the Company's Form 8-K filed with the SEC on April 18, 2018).
3.1	Certificate of Incorporation of QCR Holdings, Inc., as amended (incorporated by reference to Exhibit 3.1 of the Company's Quarterly Report on Form 10 Q/A Amendment No. 1 for the period ended September 30, 2011).
3.2	Bylaws of QCR Holdings, Inc. (incorporated by reference to Exhibit 3.1 of the Company's Form 8 K filed February 19, 2019).
4.1	Amended and Restated Rights Agreement between QCR Holdings, Inc. and Quad City Bank and Trust Company dated May 8, 2013 (incorporated by reference to Exhibit 4.1 of Company's Form 8 K filed May 8, 2013).
4.2	First Amendment to Amended and Restated Rights Agreement between QCR Holdings, Inc. and Quad City Bank and Trust Company dated February 11, 2016 (incorporated by reference to Exhibit 4.1 of Company's Form 8 K filed on February 18, 2016).
4.3	Certain instruments defining the rights of holders of long-term debt of the Company, none of which authorize a total amount of indebtedness in excess of 10% of the total assets of the Company and its subsidiaries on a consolidated basis, have not been filed as exhibits. The Company hereby agrees to furnish a copy of any of these agreements to the Securities and Exchange Commission upon request.
10.1+	First Amendment to Employment Agreement between QCR Holdings, Inc. and Ronald Nagel, dated September 10, 2018 (incorporated by reference to Exhibit 10.1 to the Company's 8-K filed with the SEC on September 13, 2018.)
10.2+	Employment Agreement between QCR Holdings, Inc., Quad City Bank and Trust Company and Douglas M. Hultquist dated January 1, 2004 (incorporated by reference to Exhibit 10.2 of Company's Annual Report on Form 10 K for the year ended December 31, 2003).

139

Table of Contents

10.3+	Employment Agreement between Cedar Rapids Bank and Trust Company and Larry J. Helling dated January 1, 2004 (incorporated by reference to Exhibit 10.6 of Company's Annual Report on Form 10_K for the year ended December 31, 2003).
10.4+	Employment Agreement between QCR Holdings, Inc. and Todd A. Gipple dated January 1, 2004 (incorporated by reference to Exhibit 10.11 of Company's Annual Report on Form 10_K for the year ended December 31, 2003).
10.5	Dividend Reinvestment Plan of QCR Holdings, Inc. (incorporated by reference to Exhibit 99.1 of Company's Form S_3D, File No. 333_102699 dated January 24, 2003).
10.6	Second Amended and Restated Operating Agreement between Quad City Bank and Trust Company and John Engelbrecht dated August 26, 2005 (incorporated by reference to Exhibit 10.1 of Company's Quarterly Report on Form 10_Q for the quarter ended September 30, 2005).
10.7+	First Amendment to the Employment Agreement among QCR Holdings, Inc., Quad City Bank and Trust Company and Douglas M. Hultquist dated December 27, 2008 (incorporated by reference to Exhibit 10.19 of the Company's Annual Report on Form 10_K for the year ended December 31, 2008).
10.8+	First Amendment to the Employment Agreement between Cedar Rapids Bank and Trust Company and Larry J. Helling dated December 30, 2008 (incorporated by reference to Exhibit 10.20 of the Company's Annual Report on Form 10_K for the year ended December 31, 2008).
10.9+	First Amendment to the Employment Agreement between QCR Holdings, Inc. and Todd A. Gipple dated December 30, 2008 (incorporated by reference to Exhibit 10.21 of the Company's Annual Report on Form 10_K for the year ended December 31, 2008).
10.10+	Executive Deferred Compensation Plan of QCR Holdings, Inc. (incorporated by reference to Exhibit 10.22 of the Company's Annual Report on Form 10_K for the year ended December 31, 2008).
10.11+	Amended and Restated Executive Deferred Compensation Plan Participation Agreement among QCR Holdings, Inc., Quad City Bank and Trust Company and Douglas M. Hultquist dated December 19, 2013 (incorporated by reference to exhibit 10.11 to the Company's Annual Report on Form10_K for the year ended December 31, 2014).
10.12+	Amended and Restated Executive Deferred Compensation Plan Participation Agreement between Cedar Rapids Bank and Trust Company and Larry J. Helling dated December 19, 2013 (incorporated by reference to exhibit 10.12 to the Company's Annual Report on Form10_K for the year ended December 31, 2014).
10.13+	Amended and Restated Executive Deferred Compensation Plan Participation Agreement between QCR Holdings, Inc. and Todd A. Gipple dated December 19, 2013 (incorporated by reference to exhibit 10.13 to the Company's Annual Report on Form 10_K for the year ended December 31, 2014).
10.14+	Non-Qualified Supplemental Executive Retirement Plan Joinder Agreement among QCR Holdings, Inc., Quad City Bank and Trust Company and Douglas M. Hultquist dated December 31, 2008 (incorporated by reference to Exhibit 10.28 of the Company's Annual Report on Form 10_K for the year ended December 31, 2008).

10.15+ Non-Qualified Supplemental Executive Retirement Plan Joinder Agreement between Cedar Rapids Bank and Trust Company and Larry J. Helling dated December 31, 2008 (incorporated by reference to Exhibit 10.29 of the Company's Annual Report on Form 10_K for the year ended December 31, 2008).

Table of Contents

10.16+		Non-Qualified Supplemental Executive Retirement Plan Joinder Agreement among QCR Holdings, Inc., and Todd A. Gipple dated December 31, 2008 (incorporated by reference to Exhibit 10.30 of the Company's Annual Report on Form 10-K for the year ended December 31, 2008).
10.17+		First Amendment to the Non-Qualified Supplemental Executive Retirement Plan Joinder Agreement among QCR Holdings, Inc., Quad City Bank and Trust Company and Douglas M. Hultquist dated December 29, 2015 (incorporated by reference to Exhibit 10.1 of the Company's Form 8-K dated December 31, 2015).
10.18	+	QCR Holdings, Inc. Amended and Restated Employee Stock Purchase Plan (incorporated by reference to Appendix A to the Company's Definitive Proxy Statement on Schedule 14A dated March 21, 2012).
10.19		Amendment No. 1 to the Second Amended and Restated Operating Agreement between Quad City Bank and Trust Company and John Engelbrecht, dated August 26, 2012 (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2012).
10.20	+	QCR Holdings, Inc. 2013 Equity Incentive Plan (incorporated by reference to Appendix A to the Company's Definitive Proxy Statement on Schedule 14A dated March 20, 2013).
10.21	+	Form of Participation Agreement under the QCR Holdings, Inc. Executive Deferred Compensation Plan (incorporated by reference to exhibit 10.23 to the Company's Annual Report on Form 10-K for the year ended December 31, 2014).
10.22	+	Employment Agreement between Quad City Bank and Trust Company and John Anderson dated October 30, 2009 (incorporated by reference to exhibit 10.24 to the Company's Annual Report on Form 10-K for the year ended December 31, 2014).
10.23	+	First Amendment to the Employment Agreement between Quad City Bank and Trust Company and John Anderson dated December 18, 2012 (incorporated by reference to exhibit 10.25 to the Company's Annual Report on Form 10-K for the year ended December 31, 2014).
10.24	+	Employment Agreement between Rockford Bank and Trust Company and Thomas Budd dated December 30, 2008 (incorporated by reference to exhibit 10.26 to the Company's Annual Report on Form 10-K for the year ended December 31, 2014).
10.25	+	First Amendment to the Employment Agreement between Rockford Bank and Trust Company and Thomas Budd dated December 30, 2008 (incorporated by reference to exhibit 10.27 to the Company's Annual Report on Form 10-K for the year ended December 31, 2014).
10.26	+	Employment Agreement between QCR Holdings, Inc. and Cathie Whiteside dated August 27, 2007 (incorporated by reference to exhibit 10.28 to the Company's Annual Report on Form 10-K for the year ended December 31, 2014).
10.27	+	First Amendment to the Employment Agreement between QCR Holdings, Inc. and Cathie Whiteside dated December 28, 2008 (incorporated by reference to exhibit 10.29 to the Company's Annual Report on Form 10-K for the year ended December 31, 2014).
10.28	+	QCR Holdings, Inc. 2016 Equity Incentive Plan (incorporated by reference to Appendix A of the Company's Definitive Proxy Statement on Schedule 14A filed on April 1, 2016).

141

Table of Contents

10.29+	QCR Holdings, Inc., Non-Qualified Supplemental Executive Retirement Plan, as amended and restated December 22, 2016 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8_K filed on December 28, 2016).
10.30+	Non-Qualified Supplemental Executive Retirement Plan Joinder Agreement between Quad City Bank and Trust Company and John H. Anderson dated December 22, 2016 (incorporated by reference to Exhibit 10.2 of the Company's Current Report on Form 8_K filed on December 28, 2016).
10.31+	Form of QCR Holdings, Inc. 2016 Equity Incentive Plan Nonqualified Stock Option Award Agreement (incorporated by reference to Exhibit 4.5 of the Company's Form S_8 filed on October 27, 2016 (File No. 333_214282)).
10.32+	Form of QCR Holdings, Inc. 2016 Equity Incentive Plan Restricted Stock Award Agreement (incorporated by reference to Exhibit 4.6 of the Company's Form S_8 filed on October 27, 2016 (File No. 333_214282)).
10.33+	Form of QCR Holdings, Inc. 2016 Equity Incentive Plan Restricted Stock Unit Award Agreement (incorporated by reference to Exhibit 4.7 of the Company's Form S_8 filed on October 27, 2016 (File No. 333_214282)).
10.34+	Transitional Employment Agreement, dated November 19, 2018, between QCR Holdings, Inc. and Douglas M. Hultquist (incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K filed November 19, 2018).
10.35+	Employment Agreement, dated November 19, 2018, between QCR Holdings, Inc. and Larry Helling (incorporated by reference to Exhibit 10.2 of the Registrant's Current Report on Form 8-K filed November 19, 2018).
10.36+	Employement Agreement, dated November 19, 2018, between QCR Holdings, Inc. and Todd Gipple (incorporated by reference to Exhibit 10.3 of the Registrant's Current Report on Form 8-K filed November 19, 2018).
21.1	Subsidiaries of QCR Holdings, Inc. (exhibit is being filed herewith).
23.1	Consent of Independent Registered Pubic Accounting Firm - RSM US LLP (exhibit is being filed herewith).
31.1	Certification of Chief Executive Officer Pursuant to Rule 13a_14(a)/15d_14(a) (exhibit is being filed herewith).
31.2	Certification of Chief Financial Officer Pursuant to Rule 13a_14(a)/15d_14(a) (exhibit is being filed herewith).
32.1	Certification of Chief Executivve Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (exhibit is being filed herewith).
32.2	

Certification of Chief Finanical Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (exhibit is being filed herewith).

Table of Contents

101 Interactive Data File
Interactive data files pursuant to Rule 405 of Regulation S-T: (i) Consolidated Balance Sheets at December 31, 2018 and December 31, 2017; (ii) Consolidated Statements of Income for the years ended December 31, 2018, December 31, 2017 and December 31, 2016; (iii) Consolidated Statements of Comprehensive Income (Loss) for the years ended December 31, 2018, December 31, 2017, and December 31, 2016; (iv) Consolidated Statements of Changes in Stockholders' Equity for the years ended December 31, 2018, December 31, 2017 and December 31, 2016; (v) Consolidated Statements of Cash Flows for the years ended December 31, 2018, December 31, 2017 and December 31, 2016; and (vi) Notes to Consolidated Financial Statements.

* The Company has omitted schedules and similar attachments to the subject agreement pursuant to Item 601(b) of Regulation S-K. The Company will furnish a copy of any omitted schedule or similar attachment to the SEC upon request.

+ A compensatory arrangement.

Item 16. Form 10 K Summary

None

Table of Contents

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

QCR HOLDINGS, INC.

Dated: March 15, 2019 By: /s/ Douglas M. Hultquist
Douglas M. Hultquist
President and Chief Executive Officer

Dated: March 15, 2019 By: /s/ Todd A. Gipple
Todd A. Gipple
Executive Vice President, Chief Operating Officer and Chief Financial Officer

Dated: March 15, 2019 By: /s/ Elizabeth A. Grabin
Elizabeth A. Grabin
Senior Vice President, Chief Accounting Officer
(Principal Accounting Officer)

Pursuant to the requirements of the Securities and Exchange Act of 1934, this report has been signed by the following persons on behalf of the Registrant in the capacities and on the dates indicated.

144

Table of Contents

SIGNATURES

Signature	Title	Date
/s/ Patrick S. Baird Patrick S. Baird	Chair of the Board of Directors	March 15, 2019
/s/ Marie Z. Ziegler Marie Z. Ziegler	Vice-Chair of the Board of Directors	March 15, 2019
/s/ Douglas M. Hultquist Douglas M. Hultquist	President, Chief Executive Officer and Director	March 15, 2019
/s/ John Paul E. Besong John Paul E. Besong	Director	March 15, 2019
/s/ Todd A. Gipple Todd A. Gipple	Executive Vice President, Chief Operating Officer, Chief Financial Officer and Director	March 15, 2019
/s/ Larry J. Helling Larry J. Helling	Director	March 15, 2019
/s/ Mark C. Kilmer Mark C. Kilmer	Director	March 15, 2019
/s/ Linda K. Neuman Linda K. Neuman	Director	March 15, 2019
/s/ Michael L. Peterson Michael L. Peterson	Director	March 15, 2019
/s/ Timothy O’Reilly Timothy O’Reilly	Director	March 15, 2019
/s/ George T. Ralph III George T. Ralph III	Director	March 15, 2019

/s/ Donna J. Sorensen, J.D. Donna J. Sorensen, J.D.	Director	March 15, 2019
/s/ Mary Kay Bates Mary Kay Bates	Director	March 15, 2019

Table of Contents

Appendix A

SUPERVISION AND REGULATION

General

FDIC-insured institutions, their holding companies and their affiliates are extensively regulated under federal and state law. As a result, the growth and earnings performance of the Company may be affected not only by management decisions and general economic conditions, but also by the requirements of federal and state statutes and by the regulations and policies of various bank regulatory agencies, including the Iowa Division of Banking, the IDFPR, the Missouri Division of Finance, the Federal Reserve, the FDIC and the CFPB. Furthermore, taxation laws administered by the Internal Revenue Service and state taxing authorities, accounting rules developed by the Financial Accounting Standards Board, securities laws administered by the SEC and state securities authorities, and anti-money laundering laws enforced by the Treasury have an impact on the business of the Company. The effect of these statutes, regulations, regulatory policies and accounting rules are significant to the Company's operations and results.

Federal and state banking laws impose a comprehensive system of supervision, regulation and enforcement on the operations of FDIC-insured institutions, their holding companies and affiliates that is intended primarily for the protection of the FDIC-insured deposits and depositors of banks, rather than stockholders. These laws, and the regulations of the bank regulatory agencies issued under them, affect, among other things, the scope of the Company's business, the kinds and amounts of investments the Company and the Banks may make, reserve requirements, required capital levels relative to assets, the nature and amount of collateral for loans, the establishment of branches, the ability to merge, consolidate and acquire, dealings with the Company's and the Banks' insiders and affiliates and the Company's payment of dividends. In reaction to the global financial crisis and particularly following the passage of the Dodd Frank Act, the Company experienced heightened regulatory requirements and scrutiny. Although the reforms primarily targeted systemically important financial service providers, their influence filtered down in varying degrees to community banks over time and caused the Company's compliance and risk management processes, and the costs thereof, to increase. After the 2016 federal elections, momentum to decrease the regulatory burden on community banks gathered strength. In May 2018, the Economic Growth, Regulatory Relief and Consumer Protection Act (the "Regulatory Relief Act") was enacted to modify or remove certain financial reform rules and regulations. While the Regulatory Relief Act maintains most of the regulatory structure established by the Dodd-Frank Act, it amends certain aspects of the regulatory framework for small depository institutions with assets of less than $10 billion, like the Company, and for large banks with assets of more than $50 billion. Many of these changes are intended to result in meaningful regulatory relief for community banks and their holding companies, including new rules that may make the capital requirements less complex. For a discussion of capital requirements, see "-The Role of Capital." It also eliminated questions about the applicability of certain Dodd-Frank Act reforms to community bank systems, including relieving the Banks of any requirement to engage in mandatory stress tests or comply with the Volcker Rule's complicated prohibitions on proprietary trading and ownership of private funds. The Company believes these reforms are favorable to its operations, but the true impact remains difficult to predict until rulemaking is complete and the reforms are fully implemented.

The supervisory framework for U.S. banking organizations subjects banks and bank holding companies to regular examination by their respective regulatory agencies, which results in examination reports and ratings that are not publicly available and that can impact the conduct and growth of their business. These examinations consider not only compliance with applicable laws and regulations, but also capital levels, asset quality and risk, management ability and performance, earnings, liquidity, and various other factors. The regulatory agencies generally have broad discretion to impose restrictions and limitations on the operations of a regulated entity where the agencies determine,

among other things, that such operations are unsafe or unsound, fail to comply with applicable law or are otherwise inconsistent with laws and regulations.

The following is a summary of the material elements of the supervisory and regulatory framework applicable to the Company and its subsidiary banks, beginning with a discussion of the continuing regulatory emphasis on the Company's capital levels. It does not describe all of the statutes, regulations and regulatory policies that apply, nor does it

Table of Contents

restate all of the requirements of those that are described. The descriptions are qualified in their entirety by reference to the particular statutory and regulatory provision.

The Role of Capital

Regulatory capital represents the net assets of a banking organization available to absorb losses. Because of the risks attendant to their business, FDIC-insured institutions are generally required to hold more capital than other businesses, which directly affects the Company's earnings capabilities. While capital has historically been one of the key measures of the financial health of both bank holding companies and banks, its role became fundamentally more important in the wake of the global financial crisis, as the banking regulators recognized that the amount and quality of capital held by banks prior to the crisis was insufficient to absorb losses during periods of severe stress. Certain provisions of the Dodd-Frank Act and Basel III, discussed below, establish capital standards for banks and bank holding companies that are meaningfully more stringent than those in place previously.

Minimum Required Capital Levels. Banks have been required to hold minimum levels of capital based on guidelines established by the bank regulatory agencies since 1983. The minimums have been expressed in terms of ratios of capital divided by total assets. As discussed below, bank capital measures have become more sophisticated over the years and have focused more on the quality of capital and the risk of assets. Bank holding companies have historically had to comply with less stringent capital standards than their bank subsidiaries and have been able to raise capital with hybrid instruments such as trust preferred securities. The Dodd-Frank Act mandated the Federal Reserve to establish minimum capital levels for holding companies on a consolidated basis as stringent as those required for FDIC-insured institutions. A result of this change is that the proceeds of hybrid instruments, such as trust preferred securities, were excluded from capital over a phase-out period. However, if such securities were issued prior to May 19, 2010 by bank holding companies with less than $15 billion of assets, they may be retained, subject to certain restrictions. Because the Company has assets of less than $15 billion, the Company is able to maintain its trust preferred proceeds as capital but the Company has to comply with new capital mandates in other respects and will not be able to raise capital in the future through the issuance of trust preferred securities.

The Basel International Capital Accords. The risk-based capital guidelines for U.S. banks since 1989 were based upon the 1988 capital accord known as "Basel I" adopted by the international Basel Committee on Banking Supervision, a committee of central banks and bank supervisors that acts as the primary global standard-setter for prudential regulation, as implemented by the U.S. bank regulatory agencies on an interagency basis. The accord recognized that bank assets for the purpose of the capital ratio calculations needed to be assigned risk weights (the theory being that riskier assets should require more capital) and that off-balance sheet exposures needed to be factored in the calculations. Basel I had a very simple formula for assigning risk weights to bank assets from 0% to 100% based on four categories. In 2008, the banking agencies collaboratively began to phase-in capital standards based on a second capital accord, referred to as "Basel II," for large or "core" international banks (generally defined for U.S. purposes as having total assets of $250 billion or more, or consolidated foreign exposures of $10 billion or more) known as "advanced approaches" banks. The primary focus of Basel II was on the calculation of risk weights based on complex models developed by each advanced approaches bank. Because most banks were not subject to Basel II, the U.S. bank regulators worked to improve the risk sensitivity of Basel I standards without imposing the complexities of Basel II. This "standardized approach" increased the number of risk-weight categories and recognized risks well above the original 100% risk weight. It is institutionalized by the Dodd-Frank Act for all banking organizations, even for the advanced approaches banks, as a floor.

On September 12, 2010, the Group of Governors and Heads of Supervision, the oversight body of the Basel Committee on Banking Supervision, announced agreement on a strengthened set of capital requirements for banking organizations around the world, known as Basel III, to address deficiencies recognized in connection with the global financial crisis.

The Basel III Rule. In July 2013, the U.S. federal banking agencies approved the implementation of the Basel III regulatory capital reforms in pertinent part, and, at the same time, promulgated rules effecting certain changes required by the Dodd-Frank Act (the "Basel III Rule"). In contrast to capital requirements historically, which were in the form of guidelines, Basel III was released in the form of enforceable regulations by each of the regulatory agencies. The Basel III Rule is applicable to all banking organizations that are subject to minimum capital requirements, including federal and

Table of Contents

state banks and savings and loan associations, as well as to bank and savings and loan holding companies, other than "small bank holding companies" (generally holding companies with consolidated assets of less than $3 billion that do not have securities registered with the SEC). Banking organizations became subject to the Basel III Rule on January 1, 2015 and all parts of it were fully phased-in as of January 1, 2019.

The Basel III Rule increased the required quantity and quality of capital and for nearly every class of assets, it requires a more complex, detailed and calibrated assessment of risk and calculation of risk weight amounts.

Not only did the Basel III Rule increase most of the required minimum capital ratios in effect prior to January 1, 2015, but it introduced the concept of Common Equity Tier 1 Capital, which consists primarily of common stock, related surplus (net of Treasury stock), retained earnings, and Common Equity Tier 1 minority interests subject to certain regulatory adjustments. The Basel III Rule also changed the definition of capital by establishing more stringent criteria that instruments must meet to be considered Additional Tier 1 Capital (primarily non-cumulative perpetual preferred stock that meets certain requirements) and Tier 2 Capital (primarily other types of preferred stock and subordinated debt, subject to limitations). A number of instruments that qualified as Tier 1 Capital under Basel I do not qualify, or their qualifications changed. For example, noncumulative perpetual preferred stock, which qualified as simple Tier 1 Capital under Basel I, does not qualify as Common Equity Tier 1 Capital, but qualifies as Additional Tier 1 Capital. The Basel III Rule also constrained the inclusion of minority interests, mortgage-servicing assets, and deferred tax assets in capital and requires deductions from Common Equity Tier 1 Capital in the event that such assets exceed a certain percentage of a banking institution's Common Equity Tier 1 Capital.

The Basel III Rule required minimum capital ratios as of January 1, 2015, as follows:

- A ratio of minimum Common Equity Tier 1 Capital equal to 4.5% of risk-weighted assets;
- An increase in the minimum required amount of Tier 1 Capital from 4% to 6% of risk-weighted assets;
- A continuation of the minimum required amount of Total Capital (Tier 1 plus Tier 2) at 8% of risk-weighted assets; and
- A minimum leverage ratio of Tier 1 Capital to total quarterly average assets equal to 4% in all circumstances.

In addition, institutions that seek the freedom to make capital distributions (including for dividends and repurchases of stock) and pay discretionary bonuses to executive officers without restriction must also maintain 2.5% in Common Equity Tier 1 Capital attributable to a capital conservation buffer fully phased-in as of January 1, 2019. The purpose of the conservation buffer is to ensure that banking institutions maintain a buffer of capital that can be used to absorb losses during periods of financial and economic stress. Factoring in the conservation buffer increases the minimum ratios depicted above to 7% for Common Equity Tier 1 Capital, 8.5% for Tier 1 Capital and 10.5% for Total Capital.

Well-Capitalized Requirements. The ratios described above are minimum standards in order for banking organizations to be considered "adequately capitalized." Bank regulatory agencies uniformly encourage banks to hold more capital and be "well-capitalized" and, to that end, federal law and regulations provide various incentives for banking organizations to maintain regulatory capital at levels in excess of minimum regulatory requirements. For example, a banking organization that is well-capitalized may: (i) qualify for exemptions from prior notice or application requirements otherwise applicable to certain types of activities; (ii) qualify for expedited processing of other required notices or applications; and (iii) accept, roll-over or renew brokered deposits. Higher capital levels could also be required if warranted by the particular circumstances or risk profiles of individual banking organizations. For example, the Federal Reserve's capital guidelines contemplate that additional capital may be required to take adequate account of, among other things, interest rate risk, or the risks posed by concentrations of credit, nontraditional activities or securities trading activities. Further, any banking organization experiencing or anticipating significant growth would be expected to maintain capital ratios, including tangible capital positions (i.e., Tier 1 Capital less all intangible assets), well above the minimum levels.

Under the capital regulations of the FDIC and Federal Reserve, in order to be well capitalized, a banking organization must maintain:

· A Common Equity Tier 1 Capital ratio to risk-weighted assets of 6.5% or more;

Table of Contents

- A ratio of Tier 1 Capital to total risk-weighted assets of 8% or more (6% under Basel I);
- A ratio of Total Capital to total risk-weighted assets of 10% or more (the same as Basel I); and
- A leverage ratio of Tier 1 Capital to total adjusted average quarterly assets of 5% or greater.

It is possible under the Basel III Rule to be well-capitalized while remaining out of compliance with the capital conservation buffer discussed above.

As of December 31, 2018: (i) none of the Banks were subject to a directive from the Iowa Division of Banking, the IDFPR, the Missouri Division of Finance, the Federal Reserve or the FDIC, as applicable, to increase its capital and (ii) the Banks were well-capitalized, as defined by FDIC regulations. As of December 31, 2018, the Company had regulatory capital in excess of the Federal Reserve's requirements and met the Basel III Rule requirements to be well-capitalized.

Prompt Corrective Action. The concept of an institution being "well-capitalized" is a part of a regulatory enforcement regime that provides the federal banking regulators with broad power to take prompt corrective action to resolve the problems of institutions based on the capital level of each particular institution. The extent of the regulators' powers depends on whether the institution in question is "adequately capitalized," "undercapitalized," "significantly undercapitalized" or "critically undercapitalized," in each case as defined by regulation. Depending upon the capital category to which an institution is assigned, the regulators' corrective powers include: (i) requiring the institution to submit a capital restoration plan; (ii) limiting the institution's asset growth and restricting its activities; (iii) requiring the institution to issue additional capital stock (including additional voting stock) or to sell itself; (iv) restricting transactions between the institution and its affiliates; (v) restricting the interest rate that the institution may pay on deposits; (vi) ordering a new election of directors of the institution; (vii) requiring that senior executive officers or directors be dismissed; (viii) prohibiting the institution from accepting deposits from correspondent banks; (ix) requiring the institution to divest certain subsidiaries; (x) prohibiting the payment of principal or interest on subordinated debt; and (xi) ultimately, appointing a receiver for the institution.

The Potential for Community Bank Capital Simplification. Community banks have long raised concerns with bank regulators about the regulatory burden, complexity, and costs associated with certain provisions of the Basel III Rule. In response, Congress provided a potential Basel III "off-ramp" for institutions, like the Company, with total consolidated assets of less than $10 billion. Section 201 of the Regulatory Relief Act instructed the federal banking regulators to establish a single CBLR of between 8% and 10%. On November 21, 2018, the agencies proposed setting the CBLR at 9% of tangible equity to total assets for a qualifying bank to be well-capitalized. Under the proposal, a community bank organization would be eligible to elect the new framework if it has less than $10 billion in total consolidated assets, limited amounts of certain assets and off-balance sheet exposures, and a CBLR greater than 9%. The electing institution would not be required to calculate the existing risk-based and leverage capital requirements of the Basel III Rule and would not need to risk weight its assets for purposes of capital calculations.

The Company is in the process of considering the Federal Reserve's CBLR proposal and will await the final regulation to determine whether it will elect the framework.

Regulation and Supervision of the Company

General. The Company, as the sole stockholder of the Banks, is a bank holding company. As a bank holding company, the Company is registered with, and is subject to regulation supervision and enforcement by, the Federal Reserve under the BHCA. The Company is legally obligated to act as a source of financial strength to the Banks and to commit resources to support the Banks in circumstances where the Company might not otherwise do so. Under the BHCA, the Company is subject to periodic examination by the Federal Reserve. The Company is required to file with the Federal Reserve periodic reports of the Company's operations and such additional information regarding the Company and its

subsidiaries as the Federal Reserve may require.

Acquisitions, Activities and Financial Holding Company Election. The primary purpose of a bank holding company is to control and manage banks. The BHCA generally requires the prior approval of the Federal Reserve for any merger involving a bank holding company or any acquisition by a bank holding company of another bank or bank holding

Table of Contents

company. Subject to certain conditions (including deposit concentration limits established by the BHCA), the Federal Reserve may allow a bank holding company to acquire banks located in any state of the United States. In approving interstate acquisitions, the Federal Reserve is required to give effect to applicable state law limitations on the aggregate amount of deposits that may be held by the acquiring bank holding company and its FDIC-insured institution affiliates in the state in which the target bank is located (provided that those limits do not discriminate against out-of-state institutions or their holding companies) and state laws that require that the target bank have been in existence for a minimum period of time (not to exceed five years) before being acquired by an out-of-state bank holding company. Furthermore, in accordance with the Dodd-Frank Act, bank holding companies must be well-capitalized and well-managed in order to effect interstate mergers or acquisitions. For a discussion of the capital requirements, see "—The Role of Capital" above.

The BHCA generally prohibits the Company from acquiring direct or indirect ownership or control of more than 5% of the voting shares of any company that is not a bank and from engaging in any business other than that of banking, managing and controlling banks or furnishing services to banks and their subsidiaries. This general prohibition is subject to a number of exceptions. The principal exception allows bank holding companies to engage in, and to own shares of companies engaged in, certain businesses found by the Federal Reserve prior to November 11, 1999 to be "so closely related to banking ... as to be a proper incident thereto." This authority permits the Company to engage in a variety of banking-related businesses, including the ownership and operation of a savings association, or any entity engaged in consumer finance, equipment leasing, the operation of a computer service bureau (including software development) and mortgage banking and brokerage services. The BHCA does not place territorial restrictions on the domestic activities of nonbank subsidiaries of bank holding companies. The Company operates Bates Financial Advisors, Inc., a registered investment advisor, and Bates Securities, Inc., a broker-dealer, as nonbanking subsidiaries under this authority.

Additionally, bank holding companies that meet certain eligibility requirements prescribed by the BHCA and elect to operate as financial holding companies may engage in, or own shares in companies engaged in, a wider range of nonbanking activities, including securities and insurance underwriting and sales, merchant banking and any other activity that the Federal Reserve, in consultation with the Secretary of the Treasury, determines by regulation or order is financial in nature or incidental to any such financial activity or that the Federal Reserve determines by order to be complementary to any such financial activity and does not pose a substantial risk to the safety or soundness of FDIC-insured institutions or the financial system generally. The Company has elected to operate as a financial holding company.

In order to maintain its status as a financial holding company, the Company and the Banks must be well-capitalized, well-managed, and the Banks must have a least a satisfactory CRA rating. If the Federal Reserve determines that a financial holding company is not well-capitalized or well-managed, the Company has a period of time in which to achieve compliance, but during the period of noncompliance, the Federal Reserve may place any limitations on the Company it believes to be appropriate. Furthermore, if the Federal Reserve determines that a financial holding company's subsidiary bank has not received a satisfactory CRA rating, that company will not be able to commence any new financial activities or acquire a company that engages in such activities.

Change in Control. Federal law also prohibits any person or company from acquiring "control" of an FDIC-insured depository institution or its holding company without prior notice to the appropriate federal bank regulator. "Control" is conclusively presumed to exist upon the acquisition of 25% or more of the outstanding voting securities of a bank or bank holding company, but may arise under certain circumstances between 10% and 24.99% ownership.

Capital Requirements. Bank holding companies are required to maintain capital in accordance with Federal Reserve capital adequacy requirements. For a discussion of capital requirements, see "—The Role of Capital" above.

Dividend Payments. The Company's ability to pay dividends to its stockholders may be affected by both general corporate law considerations and policies of the Federal Reserve applicable to bank holding companies. As a Delaware corporation, the Company is subject to the limitations of the DGCL, which allow the Company to pay dividends only out of its surplus (as defined and computed in accordance with the provisions of the DGCL) or if the Company has no such surplus, out of its net profits for the fiscal year in which the dividend is declared and/or the preceding fiscal year.

As a general matter, the Federal Reserve has indicated that the board of directors of a bank holding company should eliminate, defer or significantly reduce dividends to stockholders if: (i) the company's net income available to

Table of Contents

stockholders for the past four quarters, net of dividends previously paid during that period, is not sufficient to fully fund the dividends; (ii) the prospective rate of earnings retention is inconsistent with the company's capital needs and overall current and prospective financial condition; or (iii) the company will not meet, or is in danger of not meeting, its minimum regulatory capital adequacy ratios. The Federal Reserve also possesses enforcement powers over bank holding companies and their nonbank subsidiaries to prevent or remedy actions that represent unsafe or unsound practices or violations of applicable statutes and regulations. Among these powers is the ability to proscribe the payment of dividends by banks and bank holding companies. In addition, under the Basel III Rule, institutions that seek the freedom to pay dividends have to maintain 2.5% in Common Equity Tier 1 Capital attributable to the capital conservation buffer. See "—The Role of Capital" above.

Incentive Compensation. There have been a number of developments in recent years focused on incentive compensation plans sponsored by bank holding companies and banks, reflecting recognition by the bank regulatory agencies and Congress that flawed incentive compensation practices in the financial industry were one of many factors contributing to the global financial crisis. Layered on top of that are the abuses in the headlines dealing with product cross-selling incentive plans. The result is interagency guidance on sound incentive compensation practices.

The interagency guidance recognized three core principles. Effective incentive plans should: (i) provide employees incentives that appropriately balance risk and reward; (ii) be compatible with effective controls and risk-management; and (iii) be supported by strong corporate governance, including active and effective oversight by the organization's board of directors. Much of the guidance addresses large banking organizations and, because of the size and complexity of their operations, the regulators expect those organizations to maintain systematic and formalized policies, procedures, and systems for ensuring that the incentive compensation arrangements for all executive and non-executive employees covered by this guidance are identified and reviewed, and appropriately balance risks and rewards. Smaller banking organizations like the Company that use incentive compensation arrangements are expected to be less extensive, formalized, and detailed than those of the larger banks.

Monetary Policy. The monetary policy of the Federal Reserve has a significant effect on the operating results of financial or bank holding companies and their subsidiaries. Among the tools available to the Federal Reserve to affect the money supply are open market transactions in U.S. government securities, changes in the discount rate on bank borrowings and changes in reserve requirements against bank deposits. These means are used in varying combinations to influence overall growth and distribution of bank loans, investments and deposits, and their use may affect interest rates charged on loans or paid on deposits.

Federal Securities Regulation. The Company's common stock is registered with the SEC under the Securities Act of 1933, as amended, and the Exchange Act. Consequently, the Company is subject to the information, proxy solicitation, insider trading and other restrictions and requirements of the SEC under the Exchange Act.

Corporate Governance. The Dodd-Frank Act addressed many investor protection, corporate governance and executive compensation matters that will affect most U.S. publicly traded companies. The Dodd Frank Act increased stockholder influence over boards of directors by requiring companies to give stockholders a nonbinding vote on executive compensation and so-called "golden parachute" payments, and authorizing the SEC to promulgate rules that would allow stockholders to nominate and solicit voters for their own candidates using a company's proxy materials. The legislation also directed the Federal Reserve to promulgate rules prohibiting excessive compensation paid to executives of bank holding companies, regardless of whether such companies are publicly traded.

Supervision and Regulation of the Banks

General. The Company owns five subsidiary banks: QCBT, CRBT and CSB are chartered under Iowa law (collectively, the "Iowa Banks") and RB&T is chartered under Illinois law. SFC Bank is chartered under Missouri law.

The deposit accounts of the Banks are insured by the FDIC's DIF to the maximum extent provided under federal law and FDIC regulations, currently $250,000 per insured depositor category. All five of the Company's subsidiary banks are members of the Federal Reserve System ("member banks"). QCBT owns QCIA, a registered investment advisor, as a wholly-owned subsidiary.

Table of Contents

As Iowa-chartered, FDIC-insured banks, the Iowa Banks are subject to the examination, supervision, reporting and enforcement requirements of the Iowa Division of Banking, as the chartering authority for Iowa banks. As an Illinois-chartered, FDIC-insured bank, RB&T is subject to the examination, supervision, reporting and enforcement requirements of the IDFPR, as the chartering authority for Illinois banks. As a Missouri-chartered, FDIC-insured bank, SFC Bank is subject to the examination, supervision, reporting and enforcement requirements of the Missouri Division of Finance, as the chartering authority for Missouri banks. The Banks are also subject to the examination, reporting and enforcement requirements of the Federal Reserve, as the primary federal regulator of member banks. In addition, the FDIC, as administrator of the DIF, has regulatory authority over the Banks.

Deposit Insurance. As FDIC-insured institutions, the Banks are required to pay deposit insurance premium assessments to the FDIC. The FDIC has adopted a risk-based assessment system whereby FDIC-insured institutions pay insurance premiums at rates based on their risk classification. For institutions like the Banks that are not considered large and highly complex banking organizations, assessments are now based on examination ratings and financial ratios. The total base assessment rates currently range from 1.5 basis points to 30 basis points. At least semi-annually, the FDIC updates its loss and income projections for the DIF and, if needed, increases or decreases the assessment rates, following notice and comment on proposed rulemaking. The assessment base against which an FDIC-insured institution's deposit insurance premiums paid to the DIF has been calculated since effectiveness of the Dodd-Frank Act based on its average consolidated total assets less its average tangible equity. This method shifted the burden of deposit insurance premiums toward those large depository institutions that rely on funding sources other than U.S. deposits.

The reserve ratio is the FDIC insurance fund balance divided by estimated insured deposits. The Dodd-Frank Act altered the minimum reserve ratio of the DIF, increasing the minimum from 1.15% to 1.35% of the estimated amount of total insured deposits, and eliminating the requirement that the FDIC pay dividends to FDIC-insured institutions when the reserve ratio exceeds certain thresholds. The reserve ratio reached 1.36% on September 30, 2018. (most recent available), exceeding the statutory required minimum reserve ratio of 1.35%. The FDIC will provide assessment credits to insured depository institutions, like the Banks, with total consolidated assets of less than $10 billion for the portion of their regular assessments that contribute to growth in the reserve ratio between 1.15% and 1.35%. The FDIC will apply the credits each quarter that the reserve ratio is at least 1.38% to offset the regular deposit insurance assessments of institutions with credits.

FICO Assessments. In addition to paying basic deposit insurance assessments, FDIC-insured institutions must pay FICO assessments. FICO is a mixed-ownership governmental corporation chartered by the former Federal Home Loan Bank Board pursuant to the Competitive Equality Banking Act of 1987 to function as a financing vehicle for the recapitalization of the former Federal Savings and Loan Insurance Corporation. FICO issued 30 year noncallable bonds of approximately $8.1 billion that mature in 2018 through 2019. FICO's authority to issue bonds ended on December 12, 1991. Since 1996, federal legislation has required that all FDIC-insured institutions pay assessments to cover interest payments on FICO's outstanding obligations. The FICO assessment rate is adjusted quarterly and for the fourth quarter of 2018 was 32 cents per $100 dollars of assessable deposits.

Supervisory Assessments. Each of the Banks is required to pay supervisory assessments to its respective state banking regulator to fund the operations of that agency. The amount of the assessment payable by each Bank is calculated on the basis of that Bank's total assets. During the year ended December 31, 2018, the Iowa Banks paid supervisory assessments to the Iowa Division of Banking totaling $288 thousand and RB&T paid supervisory assessments to the IDFPR totaling $42 thousand. SFC Bank paid supervisory assessments to the Missouri Division of Finance totaling $47 thousand.

Capital Requirements. Banks are generally required to maintain capital levels in excess of other businesses. For a discussion of capital requirements, see "—The Role of Capital" above.

Liquidity Requirements. Liquidity is a measure of the ability and ease with which bank assets may be converted to cash. Liquid assets are those that can be converted to cash quickly if needed to meet financial obligations. To remain viable, FDIC-insured institutions must have enough liquid assets to meet their near-term obligations, such as withdrawals by depositors. Because the global financial crisis was in part a liquidity crisis, Basel III also includes a liquidity framework that requires FDIC-insured institutions to measure their liquidity against specific liquidity tests. One test, referred to as the LCR, is designed to ensure that the banking entity has an adequate stock of unencumbered high-quality liquid assets that

Table of Contents

can be converted easily and immediately in private markets into cash to meet liquidity needs for a 30 calendar day liquidity stress scenario. The other test, known as the NSFR, is designed to promote more medium- and long-term funding of the assets and activities of FDIC-insured institutions over a one-year horizon. These tests provide an incentive for banks and holding companies to increase their holdings in Treasury securities and other sovereign debt as a component of assets, increase the use of long-term debt as a funding source and rely on stable funding like core deposits (in lieu of brokered deposits).

In addition to liquidity guidelines already in place, the federal bank regulatory agencies implemented the Basel III LCR in September 2014, which requires large financial firms to hold levels of liquid assets sufficient to protect against constraints on their funding during times of financial turmoil, and in 2016 proposed implementation of the NSFR. While these rules do not, and will not, apply to the Banks, they continue to review their liquidity risk management policies in light of the developments.

Liability of Commonly Controlled Institutions. Under federal law, institutions insured by the FDIC may be liable for any loss incurred by, or reasonably expected to be incurred by, the FDIC in connection with the default of commonly controlled FDIC-insured depository institutions or any assistance provided by the FDIC to commonly controlled FDIC-insured depository institutions in danger of default. Because the Company controls each of the Banks, the Banks are commonly-controlled for purposes of these provisions of federal law.

Dividend Payments. The primary source of funds for the Company is dividends from the Banks. In general, the Banks may only pay dividends either out of their historical net income after any required transfers to surplus or reserves have been made or out of their retained earnings. The Federal Reserve Act also imposes limitations on the amount of dividends that may be paid by state member banks, such as the Banks. Without prior Federal Reserve approval, a state member bank may not pay dividends in any calendar year that, in the aggregate, exceed the bank's calendar year-to-date net income plus the bank's retained net income for the two preceding calendar years.

The payment of dividends by any FDIC-insured institution is affected by the requirement to maintain adequate capital pursuant to applicable capital adequacy guidelines and regulations, and an FDIC-insured institution generally is prohibited from paying any dividends if, following payment thereof, the institution would be undercapitalized. As described above, each of the Banks exceeded its minimum capital requirements under applicable guidelines as of December 31, 2018. Notwithstanding the availability of funds for dividends, however, the Federal Reserve, the FDIC, the IDFPR, the Iowa Division of Banking or the Missouri Division of Finance, as applicable, may prohibit the payment of dividends by one of the Banks if it determines such payment would constitute an unsafe or unsound practice. In addition, under the Basel III Rule, institutions that seek the freedom to pay dividends have to maintain 2.5% in Common Equity Tier 1 Capital attributable to the capital conservation buffer. See "—The Role of Capital" above.

State Bank Investments and Activities. The Banks are permitted to make investments and engage in activities directly or through subsidiaries as authorized by Illinois, Iowa and Missouri law, as applicable. However, under federal law and FDIC regulations, FDIC-insured state banks are prohibited, subject to certain exceptions, from making or retaining equity investments of a type, or in an amount, that are not permissible for a national bank. Federal law and FDIC regulations also prohibit FDIC-insured state banks and their subsidiaries, subject to certain exceptions, from engaging as principal in any activity that is not permitted for a national bank unless the bank meets, and continues to meet, its minimum regulatory capital requirements and the FDIC determines that the activity would not pose a significant risk to the DIF. These restrictions have not had, and are not currently expected to have, a material impact on the operations of the Banks.

Insider Transactions. The Banks are subject to certain restrictions imposed by federal law on "covered transactions" between each Bank and its "affiliates." The Company is an affiliate of the Banks for purposes of these restrictions, and covered transactions subject to the restrictions include extensions of credit to the Company, investments in the stock

or other securities of the Company and the acceptance of the stock or other securities of the Company as collateral for loans made by any of the Banks. The Dodd-Frank Act enhanced the requirements for certain transactions with affiliates, including an expansion of the definition of “covered transactions” and an increase in the amount of time for which collateral requirements regarding covered transactions must be maintained.

Table of Contents

Certain limitations and reporting requirements are also placed on extensions of credit by each Bank to its directors and officers, to directors and officers of the Company and its subsidiaries, to principal stockholders of the Company and to "related interests" of such directors, officers and principal stockholders. In addition, federal law and regulations may affect the terms upon which any person who is a director or officer of the Company or the Banks, or a principal stockholder of the Company, may obtain credit from banks with which any of the Banks maintains a correspondent relationship.

Safety and Soundness Standards/Risk Management. The federal banking agencies have adopted operational and managerial standards to promote the safety and soundness of FDIC-insured institutions. The standards apply to internal controls, information systems, internal audit systems, loan documentation, credit underwriting, interest rate exposure, asset growth, compensation, fees and benefits, asset quality and earnings.

In general, the safety and soundness standards prescribe the goals to be achieved in each area, and each institution is responsible for establishing its own procedures to achieve those goals. While regulatory standards do not have the force of law, if an institution operates in an unsafe and unsound manner, the FDIC-insured institution's primary federal regulator may require the institution to submit a plan for achieving and maintaining compliance. If an FDIC-insured institution fails to submit an acceptable compliance plan, or fails in any material respect to implement a compliance plan that has been accepted by its primary federal regulator, the regulator is required to issue an order directing the institution to cure the deficiency. Until the deficiency cited in the regulator's order is cured, the regulator may restrict the FDIC-insured institution's rate of growth, require the FDIC-insured institution to increase its capital, restrict the rates the institution pays on deposits or require the institution to take any action the regulator deems appropriate under the circumstances. Noncompliance with safety and soundness may also constitute grounds for other enforcement action by the federal bank regulatory agencies, including cease and desist orders and civil money penalty assessments.

During the past decade, the bank regulatory agencies have increasingly emphasized the importance of sound risk management processes and strong internal controls when evaluating the activities of the FDIC-insured institutions they supervise. Properly managing risks has been identified as critical to the conduct of safe and sound banking activities and has become even more important as new technologies, product innovation, and the size and speed of financial transactions have changed the nature of banking markets. The agencies have identified a spectrum of risks facing a banking institution including, but not limited to, credit, market, liquidity, operational, legal, and reputational risk. In particular, recent regulatory pronouncements have focused on operational risk, which arises from the potential that inadequate information systems, operational problems, breaches in internal controls, fraud, or unforeseen catastrophes will result in unexpected losses. New products and services, third-party risk and cybersecurity are critical sources of operational risk that FDIC-insured institutions are expected to address in the current environment. Each Bank is expected to have active board and senior management oversight; adequate policies, procedures, and limits; adequate risk measurement, monitoring, and management information systems; and comprehensive internal controls.

Branching Authority. The Iowa Banks have the authority under Iowa law to establish branches anywhere in the State of Iowa, subject to receipt of all required regulatory approvals. In 1997, the Company formed a de novo Illinois bank that was merged into QCBT, resulting in QCBT establishing a branch office in Illinois. Under Illinois law, QCBT may continue to establish offices in Illinois to the same extent permitted for an Illinois bank (subject to certain conditions, including certain regulatory notice requirements). Similarly, RB&T has the authority under Illinois law to establish branches anywhere in the State of Illinois, subject to receipt of all required regulatory approvals. SFC Bank has the authority under Missouri law to establish branches anywhere in the State of Missouri, subject to receipt of all required regulatory approvals.

Federal law permits state and national banks to merge with banks in other states subject to: (i) regulatory approval; (ii) federal and state deposit concentration limits; and (iii) state law limitations requiring the merging bank to have been in existence for a minimum period of time (not to exceed five years) prior to the merger. The Dodd-Frank Act

permits well-capitalized and well-managed banks to establish new interstate branches or acquire individual branches of a bank in another state (rather than the acquisition of an out-of-state bank in its entirety) without impediments.

Transaction Account Reserves. Federal Reserve regulations require FDIC-insured institutions to maintain reserves against their transaction accounts (primarily NOW and regular checking accounts). For 2019: the first $16.3 million of otherwise reservable balances are exempt from reserves and have a zero-percent reserve requirement; for

Table of Contents

transaction accounts aggregating between $16.3 million to $124.2 million, the reserve requirement is 3% of those transaction account balances; and for net transaction accounts in excess of $124.2 million, the reserve requirement is 10% of the aggregate amount of total transaction account balances in excess of $124.2 million. These reserve requirements are subject to annual adjustment by the Federal Reserve.

Federal Home Loan Bank System. The Banks are each a member of the FHLB, which serves as a central credit facility for its members. The FHLB is funded primarily from proceeds from the sale of obligations of the FHLB system. It makes loans to member banks in the form of FHLB advances. All advances from the FHLB are required to be fully collateralized as determined by the FHLB.

Community Reinvestment Act Requirements. The Community Reinvestment Act requires the Banks to have a continuing and affirmative obligation in a safe and sound manner to help meet the credit needs of the entire community, including low- and moderate-income neighborhoods. Federal regulators regularly assess each Bank's record of meeting the credit needs of its communities. Applications for additional acquisitions would be affected by the evaluation of the Bank's effectiveness in meeting its Community Reinvestment Act requirements.

Anti-Money Laundering. The USA Patriot Act is designed to deny terrorists and criminals the ability to obtain access to the U.S. financial system and has significant implications for FDIC-insured institutions, brokers, dealers and other businesses involved in the transfer of money. The USA Patriot Act mandates financial services companies to have policies and procedures with respect to measures designed to address any or all of the following matters: (i) customer identification programs; (ii) money laundering; (iii) terrorist financing; (iv) identifying and reporting suspicious activities and currency transactions; (v) currency crimes; and (vi) cooperation between FDIC-insured institutions and law enforcement authorities.

Privacy and Cybersecurity. The Banks are subject to many U.S. federal and state laws and regulations governing requirements for maintaining policies and procedures to protect non-public confidential information of their customers. These laws require the Banks to periodically disclose their privacy policies and practices relating to sharing such information and permit consumers to opt out of their ability to share information with unaffiliated third parties under certain circumstances. They also impact the Banks' ability to share information with affiliates and non-affiliates for marketing and/or non-marketing purposes, or to contact customers with marketing offers. In addition, the Banks are required to implement a comprehensive information security program that includes administrative, technical, and physical safeguards to ensure the security and confidentiality of customer records and information. These security and privacy policies and procedures, for the protection of personal and confidential information, are in effect across all businesses and geographic locations.

Concentrations in Commercial Real Estate. Concentration risk exists when FDIC-insured institutions deploy too many assets to any one industry or segment. A concentration in commercial real estate is one example of regulatory concern. The interagency Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices guidance ("CRE Guidance") provides supervisory criteria, including the following numerical indicators, to assist bank examiners in identifying banks with potentially significant commercial real estate loan concentrations that may warrant greater supervisory scrutiny: (i) commercial real estate loans exceeding 300% of capital and increasing 50% or more in the preceding three years; or (ii) construction and land development loans exceeding 100% of capital. The CRE Guidance does not limit banks' levels of commercial real estate lending activities, but rather guides institutions in developing risk management practices and levels of capital that are commensurate with the level and nature of their commercial real estate concentrations. On December 18, 2015, the federal banking agencies issued a statement to reinforce prudent risk-management practices related to CRE lending, having observed substantial growth in many CRE asset and lending markets, increased competitive pressures, rising CRE concentrations in banks, and an easing of CRE underwriting standards. The federal bank agencies reminded FDIC-insured institutions to maintain underwriting discipline and exercise prudent risk-management practices to identify, measure, monitor, and manage the risks arising

from CRE lending. In addition, FDIC-insured institutions must maintain capital commensurate with the level and nature of their CRE concentration risk. As of December 31, 2018, QCBT, CRBT and RB&T were in compliance with the 300% guideline for commercial real estate loans. Although CSB's loan portfolio has historically been real estate dominated and its real estate portfolio levels exceed these policy limits, it has established a Credit Risk Committee to routinely monitor its real estate portfolio.

Table of Contents

Consumer Financial Services. The historical structure of federal consumer protection regulation applicable to all providers of consumer financial products and services changed significantly on July 21, 2011, when the CFPB commenced operations to supervise and enforce consumer protection laws. The CFPB has broad rulemaking authority for a wide range of consumer protection laws that apply to all providers of consumer products and services, including the Banks, as well as the authority to prohibit "unfair, deceptive or abusive" acts and practices. The CFPB has examination and enforcement authority over providers with more than $10 billion in assets. FDIC-insured institutions with $10 billion or less in assets, like the Banks, continue to be examined by their applicable bank regulators.

Because abuses in connection with residential mortgages were a significant factor contributing to the financial crisis, many new rules issued by the CFPB and required by the Dodd-Frank Act addressed mortgage and mortgage-related products, their underwriting, origination, servicing and sales. The Dodd-Frank Act significantly expanded underwriting requirements applicable to loans secured by 1-4 family residential real property and augmented federal law combating predatory lending practices. In addition to numerous disclosure requirements, the Dodd Frank Act imposed new standards for mortgage loan originations on all lenders, including banks and savings associations, in an effort to strongly encourage lenders to verify a borrower's ability to repay, while also establishing a presumption of compliance for certain "qualified mortgages." The Regulatory Relief Act provided relief in connection with mortgages for banks with assets of less than $10 billion, and, as a result, mortgages the Banks make are now considered to be qualified mortgages if they are held in portfolio for the life of the loan.

The Company does not expect the CFPB's rules to have a significant impact on its operations, except for higher compliance costs.

Regulation of the Bates Companies and QCIA

The Bates Companies and QCIA provide financial investment services as part of the wealth management operations of the Company. Bates Financial Advisors, Inc. and QCIA are investment advisers registered with the SEC. The SEC has supervisory, examination and enforcement authority over their respective operations. The SEC's focus is primarily for the protection of investors under the federal securities laws. Bates Securities, Inc. is a broker-dealer that executes trades in investment products primarily for customers of Bates Financial Advisors, Inc. It is a member of FINRA and is regulated by the SEC. FINRA is a non-governmental organization that regulates member brokerage firms with an emphasis on investor protection and market integrity.

Table of Contents

Appendix B

Guide 3 Information

The following tables and schedules show selected comparative financial information required by the SEC Securities Act Guide 3, regarding the business of the Company for the periods shown.

I. Distribution of Assets, Liabilities and Stockholders Equity; Interest Rates and Interest Differential

A. and B. Consolidated Average Balance Sheets and Analysis of Net Interest Earnings

The information requested is disclosed in the MD&A section of the Company's Form 10-K for the fiscal year ended December 31, 2018.

C. Analysis of Changes of Interest Income/Interest Expense

The information requested is disclosed in the MD&A section of the Company's Form 10-K for the fiscal year ended December 31, 2018.

Table of Contents

II. Investment Portfolio

A. Investment Securities

The following tables present the amortized cost and fair value of investment securities as of December 31, 2018, 2017, and 2016

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Fair Value
	(dollars in thousands)			
December 31, 2018				
Securities held to maturity:				
Municipal securities	$ 400,863	$ 5,661	$ (6,802)	$ 399,722
Other securities	1,050	—	(1)	1,049
Totals	$ 401,913	$ 5,661	$ (6,803)	$ 400,771
Securities available for sale:				
U.S. gov't.sponsored agency securities	$ 37,150	$ 39	$ (778)	$ 36,411
Residential mortgage-backed and related securities	163,699	181	(4,631)	159,249
Municipal securities	59,069	180	(703)	58,546
Other securities	6,754	101	(5)	6,850
Totals	$ 266,672	$ 501	$ (6,117)	$ 261,056
December 31, 2017				
Securities held to maturity:				
Municipal securities	$ 378,424	$ 2,764	$ (2,488)	$ 378,700
Other securities	1,050	—	—	1,050
Totals	$ 379,474	$ 2,764	$ (2,488)	$ 379,750
Securities available for sale:				
U.S. gov't.sponsored agency securities	$ 38,409	$ 37	$ (349)	$ 38,097
Residential mortgage-backed and related securities	165,460	155	(2,313)	163,301
Municipal securities	66,176	660	(211)	66,625
Other securities	4,014	897	(27)	4,885
Totals	$ 274,059	$ 1,749	$ (2,900)	$ 272,908
December 31, 2016				
Securities held to maturity:				
Municipal securities	$ 321,859	$ 2,201	$ (4,695)	$ 319,365
Other securities	1,050	—	—	1,050

Totals	$ 322,909	$ 2,201	$ (4,695)	$ 320,415
Securities available for sale:				
U.S. gov't.sponsored agency securities	$ 46,281	$ 133	$ (331)	$ 46,083
Residential mortgage-backed and related securities	150,465	175	(2,938)	147,702
Municipal securities	52,817	426	(638)	52,605
Other securities	4,046	704	(27)	4,723
Totals	$ 253,609	$ 1,438	$ (3,934)	$ 251,113

Table of Contents

NOTE: Stock of the Federal Home Loan Bank and Federal Reserve Bank are NOT included in the above. The Company carries these investments within restricted investment securities on the consolidated balance sheets. Following is a summary of the carrying value of all of the Company's restricted investment securities as of December 31, 2018, 2017, and 2016:

	As of December 31,		
	2018	2017	2016
	(dollars in thousands)		
Federal Home Loan Bank	$ 15,732	$ 11,697	$ 9,271
Federal Reserve Bank	9,903	8,032	5,672
Other	54	54	54
Totals	$ 25,689	$ 19,783	$ 14,997

B. Investment Securities, Maturities, and Yields

The following table presents the maturity of securities held on December 31, 2018 and the weighted average stated coupon rates by range of maturity:

	Amortized Cost	Weighted Average Yield	
	(dollars in thousands)		
U.S. gov't.sponsored agency securities:			
Within 1 year	$ 21	3.78	%
After 1 but within 5 years	13,274	2.00	%
After 5 but within 10 years	2,054	3.31	%
After 10 years	21,801	3.04	%
Total	$ 37,150	2.68	%
Residential mortgage-backed and related securities:			
After 1 but within 5 years	$ 19,639	2.10	%
After 5 but within 10 years	67,581	2.55	%
After 10 years	76,479	2.57	%
Total	$ 163,699	2.51	%
Municipal securities:			
Within 1 year	$ 4,878	2.85	%
After 1 but within 5 years	42,138	2.83	%
After 5 but within 10 years	86,585	3.32	%
After 10 years	326,331	3.71	%
Total	$ 459,932	3.55	%

Other securities:			
After 1 but within 5 years	$ 1,298	3.64	%
After 5 but within 10 years	6,506	5.42	%
Total	$ 7,804	5.12	%

NOTE: Yields above are NOT computed on a tax equivalent basis

Table of Contents

C. As of December 31, 2018, there were no securities with aggregate book value and market value purchased from a single issuer (as defined by Section 2(4) of the Securities Act of 1933) that exceeded 10% of stockholders' equity.

III. Loan/Lease Portfolio

A. Types of Loans/Leases

The information requested is disclosed in MD&A section of the Company's Form 10-K for the fiscal year ended December 31, 2018.

B. Maturities and Sensitivities of Loans/Leases to Changes in Interest Rates

The information requested is disclosed in MD&A section of the Company's Form 10-K for the fiscal year ended December 31, 2018.

C. Risk Elements

1. Nonaccrual, Past Due and Restructured Loans/Leases

The gross interest income that would have been recorded if nonaccrual loans/leases and performing troubled debt restructurings had been current in accordance with their original terms was $511,915 and $230 respectively, for the year ended December 31, 2018. The amount of interest collected on nonaccrual loans/leases and performing troubled debt restructurings that was included in interest income was none and $391,997, respectively, for the year ended December 31, 2018.

The remaining information requested is disclosed in MD&A section of the Company's Form 10-K for the fiscal year ended December 31, 2018.

2. Potential Problem Loans/Leases.

To management's best knowledge, there are no such significant loans/leases that have not been disclosed in the table presented in the MD&A section of the Company's Form 10-K for the fiscal year ended December 31, 2018.

3. Foreign Outstandings. None.

4. Loan/Lease Concentrations.

As of December 31, 2018, there were two concentrations of loans/leases exceeding 10% of total loans/leases, which is not otherwise disclosed in Item III. A. Those concentrations are Lessors of Non-Residential Buildings & Dwellings at 18% and Lessors of Residential Buildings & Dwellings at 17%.

D. Other Interest-Bearing Assets

As of December 31, 2018, there are no interest-bearing assets required to be disclosed in this Appendix.

IV. Summary of Loan/Lease Loss Experience

A. Analysis of the Allowance for Estimated Losses on Loans/Leases

The information requested is disclosed in MD&A section of the Company's Form 10-K for the fiscal year ended December 31, 2018.

B. Allocation of the Allowance for Estimated Losses on Loans/Leases

The information requested is disclosed in MD&A section of the Company's Form 10-K for the fiscal year ended December 31, 2018.

Table of Contents

V. Deposits.

The average amount of and average rate paid for the categories of deposits for the years ended December 31, 2018, 2017, and 2016 are included in the consolidated average balance sheets and can be found in the MD&A section of the Company's Form 10-K for the fiscal year ended December 31, 2018.

The Company has no deposits by foreign depositors in domestic offices as of December 31, 2018.

Included in interest bearing deposits at December 31, 2018, were certificates of deposit totaling $734,189,000 that were $100,000 or greater. Maturities of these certificates were as follows:

	December 31, 2018 (dollars in thousands)
One to three months	$ 257,957
Three to six months	170,203
Six to twelve months	187,552
Over twelve months	118,477
Total certificates of deposit greater than or equal to $100,000	$ 734,189

VI. Return on Equity and Assets.

The following tables present the return on assets and equity and the equity to assets ratio of the Company:

	Years ended December 31, 2018	2017	2016
	(dollars in thousands)		
Average total assets	$ 4,392,121	$ 3,519,848	$ 2,846,699
Average equity	405,973	310,210	262,075
Net income	43,120	35,707	27,687
Return on average assets	0.98 %	1.01 %	0.97 %
Return on average common equity	10.62 %	11.51 %	10.56 %
Return on average total equity	10.62 %	11.51 %	10.56 %
Dividend payout ratio	8.22 %	7.46 %	7.27 %
Average equity to average assets ratio	9.24 %	8.81 %	9.21 %

161

Table of Contents

VII. Short Term Borrowings.

The following tables present the information requested on short-term borrowings of the Company:

Short-term borrowings as of December 31, 2018, 2017, and 2016 are summarized as follows:

	2018	2017	2016
	(dollars in thousands)		
Overnight repurchase agreements with customers	$ 2,084	$ 7,003	$ 8,131
Federal funds purchased	26,690	6,990	31,840
	$ 28,774	$ 13,993	$ 39,971

Information concerning overnight repurchase agreements with customers is summarized as follows:

	2018		2017		2016	
	(dollars in thousands)					
Average daily balance during the period	$ 7,831		$ 7,476		$ 30,083	
Average daily interest rate during the period	0.38	%	0.08	%	0.07	%
Maximum month-end balance during the period	$ 10,392		$ 11,829		$ 59,833	
Weighted average rate as of end of period	0.90	%	0.15	%	0.18	%
Securities underlying the agreements as of end of period:						
Carrying value	$ 20,760		$ 20,894		$ 19,720	
Fair value	20,760		20,894		19,720	

Information concerning federal funds purchased is summarized as follows:

	2018		2017		2016	
	(dollars in thousands)					
Average daily balance during the period	$ 13,059		$ 13,486		$ 19,106	
Average daily interest rate during the period	2.18	%	1.31	%	0.56	%
Maximum month-end balance during the period	$ 32,330		$ 33,650		$ 51,750	
Weighted average rate as of end of period	2.46	%	1.24	%	0.70	%