

QCR HOLDINGS INC
Form 10-Q
November 10, 2008

Table of Contents

**U.S. SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q**

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

For the quarterly period ending September 30, 2008

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

For the transition period from _____ to _____

Commission file number 0-22208

QCR HOLDINGS, INC.

(Exact name of Registrant as specified in its charter)

Delaware

42-1397595

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer ID Number)

3551 7th Street, Suite 204, Moline, Illinois 61265

(Address of principal executive offices)

(309) 736-3580

(Registrant's telephone number, including area code)

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the latest practicable date: As of November 1, 2008, the Registrant had outstanding 4,630,883 shares of common stock, \$1.00 par value per share.

QCR HOLDINGS, INC. AND SUBSIDIARIES
INDEX

	Page Number
Part I FINANCIAL INFORMATION	
Item 1 Consolidated Financial Statements (Unaudited)	
<u>Consolidated Balance Sheets,</u> <u>September 30, 2008 and December 31, 2007</u>	2
<u>Consolidated Statements of Income,</u> <u>For the Three Months Ended September 30, 2008 and 2007</u>	3
<u>Consolidated Statements of Income,</u> <u>For the Nine Months Ended September 30, 2008 and 2007</u>	4
<u>Consolidated Statement of Changes in Stockholders' Equity,</u> <u>For the Nine Months Ended September 30, 2008</u>	5
<u>Consolidated Statements of Cash Flows,</u> <u>For the Nine Months Ended September 30, 2008 and 2007</u>	6
<u>Notes to Consolidated Financial Statements</u>	7-19
<u>Item 2 Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	20-40
<u>Item 3 Quantitative and Qualitative Disclosures About Market Risk</u>	41-42
<u>Item 4 Controls and Procedures</u>	43
Part II OTHER INFORMATION	
<u>Item 1 Legal Proceedings</u>	44
<u>Item 1.A. Risk Factors</u>	44
<u>Item 2 Unregistered Sales of Equity Securities and Use of Proceeds</u>	44
<u>Item 3 Defaults Upon Senior Securities</u>	44
<u>Item 4 Submission of Matters to a Vote of Security Holders</u>	44
<u>Item 5 Other Information</u>	44
<u>Item 6 Exhibits</u>	45

Signatures

46

Exhibit 31.1

Exhibit 31.2

Exhibit 32.1

Exhibit 32.2

Table of Contents

QCR HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS (UNAUDITED)
September 30, 2008 and December 31, 2007

	September 30, 2008	December 31, 2007
ASSETS		
Cash and due from banks	\$ 33,943,067	\$ 40,490,000
Federal funds sold	9,536,411	7,985,000
Interest-bearing deposits at financial institutions	1,282,987	5,096,048
Securities held to maturity, at amortized cost	350,000	350,000
Securities available for sale, at fair value	231,623,193	220,207,243
	231,973,193	220,557,243
Loans receivable held for sale	4,162,970	6,507,583
Loans/leases receivable held for investment	1,173,585,054	1,050,480,273
	1,177,748,024	1,056,987,856
Less: Allowance for estimated losses on loans/leases	(14,495,563)	(11,315,253)
	1,163,252,461	1,045,672,603
Premises and equipment, net	31,548,914	31,884,153
Goodwill	3,222,688	3,222,688
Intangible asset	89,250	
Accrued interest receivable	7,924,502	7,585,690
Bank-owned life insurance	27,336,830	26,549,614
Assets related to discontinued operations, held for sale	106,331,948	68,222,699
Other assets	24,973,874	19,298,604
Total assets	\$ 1,641,416,125	\$ 1,476,564,342
LIABILITIES AND STOCKHOLDERS EQUITY		
LIABILITIES		
Deposits:		
Noninterest-bearing	\$ 143,071,342	\$ 160,533,242
Interest-bearing	837,328,338	723,472,017
Total deposits	980,399,680	884,005,259
Short-term borrowings	127,094,449	170,204,021
Federal Home Loan Bank advances	214,695,000	168,815,006

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Other borrowings	76,605,144	47,690,122
Junior subordinated debentures	36,085,000	36,085,000
Liabilities related to discontinued operations, held for sale	94,789,085	59,061,550
Other liabilities	20,335,440	22,916,909
Total liabilities	1,550,003,798	1,388,777,867
Minority interest in consolidated subsidiaries	1,974,134	1,720,683
STOCKHOLDERS EQUITY		
Preferred stock, \$1 par value; shares authorized 250,000; September 2008 - 568 shares issued and outstanding, December 2007 - 568 shares issued and outstanding,	568	568
Common stock, \$1 par value; shares authorized 10,000,000 September 2008 - 4,625,088 shares issued and outstanding, December 2007 - 4,597,744 shares issued and outstanding,	4,625,088	4,597,744
Additional paid-in capital	42,902,685	42,317,374
Retained earnings	41,579,821	36,338,566
Accumulated other comprehensive income	330,031	2,811,540
Total stockholders equity	89,438,193	86,065,792
Total liabilities and stockholders equity	\$ 1,641,416,125	\$ 1,476,564,342

See Notes to Consolidated Financial Statements

Table of Contents

QCR HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)
Three Months Ended September 30,

	2008	2007
Interest and dividend income:		
Loans/leases, including fees	\$ 18,530,735	\$ 18,673,871
Securities:		
Taxable	2,742,291	2,385,165
Nontaxable	229,159	251,526
Interest-bearing deposits at financial institutions	10,391	70,931
Federal funds sold	28,492	40,758
 Total interest and dividend income	 21,541,068	 21,422,251
 Interest expense:		
Deposits	5,570,085	7,846,616
Short-term borrowings	656,039	1,471,588
Federal Home Loan Bank advances	2,248,559	1,859,131
Other borrowings	752,521	591,458
Junior subordinated debentures	572,822	660,690
 Total interest expense	 9,800,026	 12,429,483
 Net interest income	 11,741,042	 8,992,768
 Provision for loan/lease losses	 2,154,061	 956,967
 Net interest income after provision for loan/lease losses	 9,586,981	 8,035,801
 Non-interest income:		
Credit card issuing fees, net of processing costs	228,786	191,918
Trust department fees	781,182	924,464
Deposit service fees	816,019	672,288
Gains on sales of loans, net	200,499	277,265
Gains on sales of foreclosed assets	61,152	
Gains on sales of other assets		435,791
Earnings on bank-owned life insurance	241,190	242,534
Investment advisory and management fees, gross	480,587	369,239
Other	501,794	435,073
 Total non-interest income	 3,311,209	 3,548,572
 Non-interest expenses:		
Salaries and employee benefits	6,467,255	5,648,520

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Professional and data processing fees	1,143,404	805,640
Advertising and marketing	386,099	262,068
Occupancy and equipment expense	1,326,446	1,217,051
Stationery and supplies	116,589	129,811
Postage and telephone	222,931	235,247
Bank service charges	159,598	139,948
FDIC and other insurance	338,453	295,144
Other	415,508	358,501
Total non-interest expenses	10,576,283	9,091,930
Income from continuing operations before income taxes	2,321,907	2,492,443
Federal and state income tax expense from continuing operations	613,372	744,434
Income from continuing operations before minority interest in net income of consolidated subsidiaries	1,708,535	1,748,009
Minority interest in net income of consolidated subsidiaries	93,386	17,046
Income from continuing operations	\$ 1,615,149	\$ 1,730,963
Discontinued operations (Note 2):		
Gain on sale of merchant credit card acquiring business	4,645,213	
Operating income from merchant credit card acquiring business	119,483	112,937
Operating loss from First Wisconsin Bank & Trust	(582,307)	(348,244)
Income (loss) from discontinued operations before income taxes	4,182,389	(235,307)
Federal and state income tax expense (benefit) from discontinued operations	1,492,056	(98,153)
Income (loss) from discontinued operations	\$ 2,690,333	\$ (137,154)
Net income	\$ 4,305,482	\$ 1,593,809
Less preferred stock dividends	446,125	268,000
Net income available to common stockholders	\$ 3,859,357	\$ 1,325,809
Basic earnings per common share (Note 3):		
Income from continuing operations	0.25	0.32
Income (loss) from discontinued operations	0.58	(0.03)
Net income	\$ 0.83	\$ 0.29
Diluted earnings per common share (Note 3):		
Income from continuing operations	0.25	0.32
Income (loss) from discontinued operations	0.58	(0.03)
Net income	\$ 0.83	\$ 0.29

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Cash dividends declared per common share	\$ 0.00	\$ 0.00
Comprehensive income	\$ 3,150,057	\$ 3,324,477

See Notes to Consolidated Financial Statements

Table of Contents

QCR HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)
Nine Months Ended September 30,

	2008	2007
Interest and dividend income:		
Loans/leases, including fees	\$ 54,844,169	\$ 53,784,361
Securities:		
Taxable	8,017,862	6,445,213
Nontaxable	712,774	790,804
Interest-bearing deposits at financial institutions	157,590	294,561
Federal funds sold	70,440	214,329
 Total interest and dividend income	 63,802,835	 61,529,268
 Interest expense:		
Deposits	18,129,951	23,492,921
Short-term borrowings	2,723,254	3,865,000
Federal Home Loan Bank advances	6,188,099	5,370,203
Other borrowings	1,921,505	1,170,699
Junior subordinated debentures	1,770,728	1,965,959
 Total interest expense	 30,733,537	 35,864,782
 Net interest income	 33,069,298	 25,664,486
 Provision for loan/lease losses	 4,493,644	 2,083,959
 Net interest income after provision for loan/lease losses	 28,575,654	 23,580,527
 Non-interest income:		
Credit card issuing fees, net of processing costs	735,123	509,956
Trust department fees	2,549,856	2,783,795
Deposit service fees	2,319,958	1,918,389
Gains on sales of loans, net	863,146	965,680
Gains on sales of foreclosed assets	65,736	1,007
Gains on sales of other assets		435,791
Earnings on bank-owned life insurance	787,217	642,517
Investment advisory and management fees, gross	1,566,604	1,134,362
Other	1,491,681	1,361,348
 Total non-interest income	 10,379,321	 9,752,845
 Non-interest expenses:		
Salaries and employee benefits	19,301,094	16,114,688

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Professional and data processing fees	3,410,312	2,514,243
Advertising and marketing	980,942	769,424
Occupancy and equipment expense	3,791,235	3,522,896
Stationery and supplies	369,363	381,577
Postage and telephone	694,742	702,712
Bank service charges	430,614	419,526
FDIC and other insurance	971,037	697,301
Loss on sale of fixed assets		239,016
Other	1,183,168	985,239
Total non-interest expenses	31,132,507	26,346,622
Income from continuing operations before income taxes	7,822,468	6,986,750
Federal and state income tax expense from continuing operations	2,154,572	2,031,192
Income from continuing operations before minority interest in net income of consolidated subsidiaries	5,667,896	4,955,558
Minority interest in net income of consolidated subsidiaries	362,213	250,935
Income from continuing operations	\$ 5,305,683	\$ 4,704,623
Discontinued operations (Note 2):		
Gain on sale of merchant credit card acquiring business	4,645,213	
Operating income from merchant credit card acquiring business	361,160	305,939
Operating loss from First Wisconsin Bank & Trust	(2,790,363)	(1,182,758)
Income (loss) from discontinued operations before income taxes	2,216,010	(876,819)
Federal and state income tax expense (benefit) from discontinued operations	757,478	(339,296)
Income (loss) from discontinued operations	\$ 1,458,532	\$ (537,523)
Net income	\$ 6,764,215	\$ 4,167,100
Less preferred stock dividends	1,338,375	804,000
Net income available to common stockholders	\$ 5,425,840	\$ 3,363,100
Basic earnings per common share (Note 3):		
Income from continuing operations	0.86	0.85
Income (loss) from discontinued operations	0.32	(0.12)
Net income	\$ 1.18	\$ 0.73
Diluted earnings per common share (Note 3):		
Income from continuing operations	0.85	0.85
Income (loss) from discontinued operations	0.31	(0.12)

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Net income	\$	1.17	\$	0.73
Cash dividends declared per common share	\$	0.04	\$	0.04
Comprehensive income	\$	4,282,706	\$	5,262,567

See Notes to Consolidated Financial Statements

Table of Contents

QCR HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS EQUITY (UNAUDITED)
Nine Months Ended September 30, 2008

	Preferred Stock	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total
Balance December 31, 2007	\$ 568	\$ 4,597,744	\$ 42,317,374	\$ 36,338,566	\$ 2,811,540	\$ 86,065,792
Comprehensive income:						
Net income				686,444		686,444
Other comprehensive income, net of tax					1,808,101	1,808,101
Comprehensive income						2,494,545
Preferred cash dividends declared				(446,125)		(446,125)
Proceeds from issuance of 4,373 shares of common stock as a result of stock purchased under the Employee Stock Purchase Plan		4,373	45,686			50,059
Proceeds from issuance of 1,732 shares of common stock as a result of stock options exercised		1,732	15,839			17,571
Tax benefit of nonqualified stock options exercised				717		717
Stock compensation expense				99,922		99,922
Balance March 31, 2008	\$ 568	\$ 4,603,849	\$ 42,479,538	\$ 36,578,885	\$ 4,619,641	\$ 88,282,481
Comprehensive income:						
Net income				1,772,289		1,772,289
Other comprehensive loss, net of tax					(3,134,185)	(3,134,185)
Comprehensive loss						(1,361,896)
Common cash dividends declared \$0.04 per share				(184,585)		(184,585)
				(446,125)		(446,125)

Preferred cash dividends declared						
Proceeds from issuance of 7,501 shares of common stock as a result of stock purchased under the Employee Stock Purchase Plan	7,501		88,700			96,201
Proceeds from issuance of 5,499 shares of common stock as a result of stock options exercised	5,499		66,004			71,503
Exchange of 1,933 shares of common stock in connection with options exercised	(1,933)		(27,284)			(29,217)
Tax benefit of nonqualified stock options exercised			863			863
Stock compensation expense			117,576			117,576
Issuance of 5,000 shares of restricted stock	5,000		(5,000)			
Balance June 30, 2008	\$ 568	\$ 4,619,916	\$ 42,720,397	\$ 37,720,464	\$ 1,485,456	\$ 86,546,801
Comprehensive income:						
Net income				4,305,482		4,305,482
Other comprehensive income, net of tax					(1,155,425)	(1,155,425)
Comprehensive income						3,150,057
Preferred cash dividends declared				(446,125)		(446,125)
Proceeds from issuance of 5,098 shares of common stock as a result of stock purchased under the Employee Stock Purchase Plan	5,098		52,253			57,351
Proceeds from issuance of 74 shares of common stock as a result of stock options exercised	74		567			641
Tax benefit of nonqualified stock options exercised			31			31
Stock compensation expense			129,437			129,437

Balance September 30, 2008	\$ 568	\$ 4,625,088	\$ 42,902,685	\$ 41,579,821	\$ 330,031	\$ 89,438,193
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See Notes to Consolidated Financial Statements

Table of Contents

QCR HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
Nine Months Ended September 30,

	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$ 6,764,215	\$ 4,167,100
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	1,887,233	1,708,848
Provision for loan/lease losses related to continuing operations	4,493,644	2,083,959
Provision for loan/lease losses related to discontinued operations	1,727,000	184,384
Amortization of offering costs on subordinated debentures	10,738	10,738
Amortization of intangible asset	7,140	
Stock-based compensation expense	289,231	(30,538)
Minority interest in income of consolidated subsidiaries	362,213	250,935
Gain on sale of foreclosed assets	(65,736)	(1,007)
Gain on sale of other assets		(435,791)
Gain on sale of merchant credit card acquiring business	(4,645,213)	
Amortization of premiums (accretion of discount) on securities, net	31,918	(48,767)
Loans originated for sale	(68,882,999)	(81,123,640)
Proceeds on sales of loans	72,093,764	83,837,553
Net gains on sales of loans	(863,146)	(965,680)
Net loss on sale of premises and equipment		239,016
Increase in accrued interest receivable	(531,322)	(1,342,399)
Increase in other assets	(4,106,771)	(3,202,295)
(Decrease) increase in other liabilities	(2,338,195)	1,542,807
Net cash provided by operating activities	\$ 6,233,714	\$ 6,875,223
CASH FLOWS FROM INVESTING ACTIVITIES		
Net increase in federal funds sold	(2,916,411)	(4,830,000)
Net decrease (increase) in interest-bearing deposits at financial institutions	3,811,496	(476,982)
Proceeds from sale of foreclosed assets	661,268	93,901
Proceeds from sale of other assets		500,000
Proceeds from sale of merchant credit card acquiring business	5,200,000	
Activity in securities portfolio:		
Purchases	(94,236,370)	(94,049,814)
Calls, maturities and redemptions	75,312,251	61,291,150
Paydowns	633,222	435,831
Activity in bank-owned life insurance:		
Purchases		(9,121,488)
Increase in cash value	(872,543)	(661,356)
Net loans/leases originated and held for investment	(160,366,569)	(94,934,998)
Purchase of premises and equipment	(1,693,503)	(1,782,531)
Purchase of intangible asset	(96,390)	(887,542)
Net increase in cash related to discontinued operations, held for sale	(1,131,508)	(1,247,357)

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Net cash used in investing activities	\$ (175,695,057)	\$ (145,671,186)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net increase in deposit accounts	136,731,836	20,042,601
Net (decrease) increase in short-term borrowings	(47,349,417)	64,239,104
Activity in Federal Home Loan Bank advances:		
Advances	60,145,000	58,400,000
Payments	(14,265,006)	(50,381,685)
Net increase in other borrowings	28,915,022	43,955,759
Tax benefit of nonqualified stock options exercised	1,611	21,475
Payment of cash dividends	(1,528,745)	(1,066,013)
Costs from issuance of preferred stock, net		(10,671)
Proceeds from issuance of common stock, net	264,109	352,212
Net cash provided by financing activities	\$ 162,914,410	\$ 135,552,782
Net decrease in cash and due from banks	(6,546,933)	(3,243,181)
Cash and due from banks, beginning	40,490,000	42,502,770
Cash and due from banks, ending	\$ 33,943,067	\$ 39,259,589
Supplemental disclosure of cash flow information, cash payments for:		
Interest	\$ 32,950,020	\$ 36,499,392
Income/franchise taxes	\$ 2,283,927	\$ 767,932
Supplemental schedule of noncash investing activities:		
Change in accumulated other comprehensive income, unrealized gains (losses) on securities available for sale, net	\$ (2,481,509)	\$ 1,095,467
Transfers of loans to other real estate owned	\$ 2,228,613	\$

See Notes to Consolidated Financial Statements

Table of Contents

Part I
Item 1

QCR HOLDINGS, INC.
AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
SEPTEMBER 30, 2008

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation: The interim unaudited consolidated financial statements contained herein should be read in conjunction with the audited consolidated financial statements and accompanying notes to the consolidated financial statements for the fiscal year ended December 31, 2007, including QCR Holdings, Inc.'s (the "Company") Form 10-K filed with the Securities and Exchange Commission on March 5, 2008. Accordingly, footnote disclosures, which would substantially duplicate the disclosure contained in the audited consolidated financial statements, have been omitted.

The financial information of the Company included herein has been prepared in accordance with U.S. generally accepted accounting principles for interim financial reporting and has been prepared pursuant to the rules and regulations for reporting on Form 10-Q and Rule 10-01 of Regulation S-X. Such information reflects all adjustments (consisting of normal recurring adjustments) that are, in the opinion of management, necessary for a fair presentation of the financial position and results of operations for the periods presented. Any differences appearing between the numbers presented in financial statements and management's discussion and analysis are due to rounding. The results of the interim periods ended September 30, 2008, are not necessarily indicative of the results expected for the year ending December 31, 2008.

The consolidated financial statements include the accounts of the Company and its subsidiaries which includes four state-chartered commercial banks: Quad City Bank & Trust ("QCBT"), Cedar Rapids Bank & Trust ("CRBT"), Rockford Bank & Trust ("RB&T"), and First Wisconsin Bank & Trust ("FWBT"); and Quad City Bancard, Inc. ("Bancard") which provides merchant and cardholder credit card processing services. All material intercompany transactions and balances have been eliminated in consolidation.

Activities related to discontinued operations have been recorded separately with current and prior period amounts reclassified as assets and liabilities related to discontinued operations on the consolidated balance sheets and as discontinued operations on the consolidated statements of income and consolidated statement of cash flows. The notes to the consolidated financial statements have also been adjusted to eliminate the effect of discontinued operations.

Stock-based compensation plans: Please refer to Note 13 of our consolidated financial statements in our Annual Report on Form 10-K for the year ended December 31, 2007, for information related to the Company's stock option and incentive plans, stock appreciation rights ("SARs") and stock purchase plan.

During the third quarter of 2008, the Company granted to directors and certain employees nonqualified stock options to purchase 1,000 shares of common stock. The Company did not grant any shares of restricted stock during the third quarter of 2008.

Table of Contents

Part I

Item 1

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) continued

The Company accounts for stock-based compensation in accordance with the Statement of Financial Accounting Standards No. 123(R), Share-Based Payment (SFAS No. 123(R)). SFAS No. 123(R) requires measurement of compensation cost for all stock-based awards at fair value on the grant date and recognition of compensation expense over the requisite service period for awards expected to vest. Stock-based compensation expense totaled \$147 thousand and (\$38) thousand for the three months ended September 30, 2008 and 2007, and \$289 thousand and (\$31) thousand for the nine months ended September 30, 2008 and 2007, respectively. A key component in the calculation of stock-based compensation expense is the market price of the Company's stock.

NOTE 2 DISCONTINUED OPERATIONS**SALE OF MERCHANT CREDIT CARD ACQUIRING BUSINESS**

On August 29, 2008, the Company's subsidiary, Quad City Bancard, Inc., sold its merchant credit card acquiring business for \$5.2 million and recorded an after-tax gain of approximately \$3.0 million. Consequently, the business related to merchant credit card acquiring has been accounted for as discontinued operations. The assets and liabilities relating to the merchant credit card acquiring business were not significant as of September 30, 2008 and as of December 31, 2007.

The results from discontinued operations of the merchant credit card acquiring business for the three-month and nine-month periods ending September 30, 2008 and 2007 are presented in the following tables:

	Three Months Ended	
	September 30, 2008	September 30, 2007
Merchant credit card acquiring fees, net of processing costs	\$ 193,679	\$ 250,725
Non-interest expense	74,196	137,788
Income from discontinued operations, excluding gain on sale, before income taxes	119,483	112,937
Gain on sale of discontinued operations before income taxes	4,645,213	
Income from discontinued operations before income taxes	\$ 4,764,696	\$ 112,937
Income tax expense	1,689,652	39,391
Income from discontinued operations, net of tax	\$ 3,075,044	\$ 73,546

Table of ContentsPart I
Item 1

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) continued

	Nine Months Ended	
	September 30, 2008	September 30, 2007
Merchant credit card acquiring fees, net of processing costs	\$ 693,445	\$ 738,961
Non-interest expense	332,285	433,022
Income from discontinued operations, excluding gain on sale, before income taxes	361,160	305,939
Gain on sale of discontinued operations before income taxes	4,645,213	
Income from discontinued operations before income taxes	\$ 5,006,373	\$ 305,939
Income tax expense	1,775,716	110,015
Income from discontinued operations, net of tax	\$ 3,230,657	\$ 195,924

SALE OF FIRST WISCONSIN BANK & TRUST

Subsequent to September 30, 2008, the Company entered into a definitive agreement to sell First Wisconsin Bank & Trust, its wholly-owned commercial banking subsidiary which serves the Milwaukee, Wisconsin market. The transaction will involve the sale of stock of FWBT for approximately \$13.5 million and is anticipated to close by December 31, 2008, subject to various closing conditions, including regulatory approval. The Company expects to record a gain on the sale of approximately \$500 thousand, after taxes and related expenses. The activity related to FWBT is accounted for as discontinued operations.

Table of ContentsPart I
Item 1

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) continued

Presented in the following tables are condensed financial statements for First Wisconsin Bank & Trust:

CONDENSED BALANCE SHEETS DISCONTINUED OPERATIONS

(dollars in thousands)	As of September 30, 2008	As of December 31, 2007
ASSETS		
Cash and cash equivalents	\$ 1,838	\$ 706
Securities available for sale, at fair value	18,180	15,347
Loans receivable, net	81,197	49,204
Other assets	5,117	2,966
Assets related to discontinued operations, held for sale	\$ 106,332	\$ 68,223
LIABILITIES		
Deposits	\$ 85,760	\$ 45,422
Short-term borrowings	8,752	12,992
Other liabilities	277	648
Liabilities related to discontinued operations, held for sale	\$ 94,789	\$ 59,062

CONDENSED STATEMENTS OF INCOME DISCONTINUED OPERATIONS

	Three Months Ended	
	September 30, 2008	September 30, 2007
Interest income	\$ 1,449,144	\$ 680,203
Interest expense	795,359	361,210
Net interest income	653,785	318,993
Provision for loan losses	212,000	80,384
Net interest income after provision for loan losses	441,785	238,609
Non-interest income	119,273	59,193
Non-Interest expense	1,143,365	646,046
Net loss before income taxes	\$ (582,307)	\$ (348,244)
Income tax benefit	(197,596)	(137,544)
Net loss from discontinued operations	\$ (384,711)	\$ (210,700)

Table of ContentsPart I
Item 1**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) continued**
CONDENSED STATEMENTS OF INCOME - DISCONTINUED OPERATIONS (continued)

	Nine Months Ended	
	September 30, 2008	September 30, 2007
Interest income	\$ 3,763,240	\$ 1,560,985
Interest expense	2,011,921	766,366
Net interest income	1,751,319	794,619
Provision for loan losses	1,727,000	184,384
Net interest income after provision for loan losses	24,319	610,235
Non-interest income	330,082	93,256
Non-Interest expense	3,144,764	1,886,249
Net loss before income taxes	\$ (2,790,363)	\$ (1,182,758)
Income tax benefit	(1,018,238)	(449,311)
Net loss from discontinued operations	\$ (1,772,125)	\$ (733,447)

Table of Contents

Part I

Item 1

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) continued

NOTE 3 EARNINGS PER SHARE

The following information was used in the computation of earnings per share on a basic and diluted basis.

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2008	2007	2008	2007
Income from continuing operations	\$ 1,615,149	\$ 1,730,963	\$ 5,305,683	\$ 4,704,623
Income(loss) from discontinued operations	2,690,333	(137,154)	1,458,532	(537,523)
Net income	4,305,482	1,593,809	6,764,215	4,167,100
Less preferred stock dividends	446,125	268,000	1,338,375	804,000
Net income available to common stockholders, basic and diluted earnings	\$ 3,859,357	\$ 1,325,809	\$ 5,425,840	\$ 3,363,100
Weighted average common shares outstanding	4,624,056	4,591,576	4,612,658	4,576,963
Weighted average common shares issuable upon exercise of stock options, restricted stock awards, and under the employee stock purchase plan	22,443	7,830	32,074	19,828
Weighted average common and common equivalent shares outstanding	4,646,499	4,599,406	4,644,732	4,596,791

Table of Contents

Part I

Item 1

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) continued

NOTE 4 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 QCR Holdings, Inc. 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 three subsidiary banks wholly-owned by the Company: Quad City Bank & Trust, Cedar Rapids Bank & Trust, and Rockford Bank & Trust. 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.

First Wisconsin Bank & Trust is accounted for as discontinued bank operations and has been properly excluded where appropriate. FWBT's assets held for sale are reported in the ALL OTHER segment.

The Company's Credit Card Processing segment represents the continuing operations of Quad City Bancard, Inc. Bancard is a wholly-owned subsidiary of the Company that provides credit card processing for cardholders of the Company's three subsidiary banks and approximately one hundred agent banks.

As previously noted, Bancard sold its merchant credit card acquiring business and the Company has accounted for it as discontinued operations. The related financial information has been properly excluded.

The Company's Trust Management segment represents the trust and asset management 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 and for custodial services. No assets of the subsidiary banks have been allocated to the Trust Management segment.

The Company's All Other segment includes the operations of all other consolidated subsidiaries and/or defined operating segments that fall below the segment reporting thresholds. This segment includes the corporate operations of the parent and the real estate holding operations of Velie Plantation Holding Company.

Selected financial information on the Company's business segments is presented as follows for the three months and nine months ended September 30, 2008 and 2007.

Table of ContentsPart I
Item 1

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) continued

QCR HOLDINGS, INC. AND SUBSIDIARIES
SELECTED FINANCIAL DATA BUSINESS SEGMENTS
Three Months and Nine Months Ended September 30, 2008 and 2007

	Commercial Banking							
	Quad City Bank & Trust	Cedar Rapids Bank & Trust	Rockford Bank & Trust	Credit Card Processing	Trust Management	All other	Intercompany Eliminations	Consolidated Total
Three Months ended September 30, 2008								
Total Revenue	\$ 14,067,074	\$ 6,821,470	\$ 3,082,941	\$ 693,532	\$ 705,314	\$ 5,544,461	\$ (6,062,514)	\$ 24,852,277
Net Interest Income	\$ 7,527,971	\$ 3,497,061	\$ 1,354,700	\$ 115,860	\$	\$ (697,110)	\$ (57,440)	\$ 11,741,042
Income from continuing operations	\$ 1,865,998	\$ 837,737	\$ (58,510)	\$ 2,590	\$ 81,396	\$ 5,218,037	\$ (6,332,098)	\$ 1,615,143
Total Assets	\$ 886,113,521	\$ 444,211,934	\$ 216,133,770	\$ 955,869	\$	\$ 144,783,216	\$ (50,782,185)	\$ 1,641,416,125
Provision for Loan/Lease Losses	\$ 1,369,873	\$ 471,377	\$ 260,000	\$ 52,811	\$	\$	\$	\$ 2,154,061
Goodwill and Intangible Assets	\$ 3,311,938	\$	\$	\$	\$	\$	\$	\$ 3,311,938
Three Months ended September 30, 2007								
Total Revenue	\$ 14,767,072	\$ 6,412,504	\$ 2,334,069	\$ 626,424	\$ 924,465	\$ 4,935,235	\$ (5,028,945)	\$ 24,970,825
Net Interest Income	\$ 6,474,609	\$ 2,591,949	\$ 820,964	\$ 121,790	\$	\$ (876,718)	\$ (139,826)	\$ 8,992,769
Income from continuing operations	\$ 1,795,139	\$ 602,486	\$ (258,591)	\$ (15,671)	\$ 255,399	\$ 4,354,231	\$ (5,002,029)	\$ 1,730,964
Total Assets	\$ 860,477,760	\$ 367,714,176	\$ 138,899,065	\$ 980,836	\$	\$ 130,083,814	\$ (83,888,047)	\$ 1,414,267,603
Provision for Loan/Lease Losses	\$ 387,856	\$ 182,800	\$ 333,956	\$ 52,355	\$	\$	\$	\$ 956,967
Goodwill and Intangible Assets	\$ 3,222,688	\$	\$	\$	\$	\$	\$	\$ 3,222,688

**Three Months
ended**

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September 30, 2008										
Total Revenue	\$ 42,490,525	\$ 19,980,678	\$ 8,819,735	\$ 735,123	\$ 2,549,856	\$ 10,488,577	\$ (10,882,338)	\$ 74,182,15		
Net Interest Income	\$ 21,833,397	\$ 9,617,536	\$ 3,711,548	\$ 351,607	\$	\$ (2,109,158)	\$ (335,632)	\$ 33,069,29		
Income from Continuing Operations	\$ 6,016,789	\$ 2,357,705	\$ (146,039)	\$ 61,131	\$ 573,082	\$ 6,940,955	\$ (10,497,939)	\$ 5,305,68		
Total Assets	\$ 886,113,521	\$ 444,211,934	\$ 216,133,770	\$ 955,869	\$	\$ 144,783,216	\$ (50,782,185)	\$ 1,641,416,12		
Provision for Loan/Lease Losses	\$ 2,745,462	\$ 914,645	\$ 689,000	\$ 144,537	\$	\$	\$	\$ 4,493,64		
Goodwill and Intangible Assets	\$ 3,311,938	\$	\$	\$	\$	\$	\$	\$ 3,311,93		

Three Months Ended September 30, 2007										
Total Revenue	\$ 43,541,042	\$ 18,564,112	\$ 5,817,441	\$ 509,956	\$ 2,783,795	\$ 7,131,385	\$ (7,065,619)	\$ 71,282,11		
Net Interest Income	\$ 18,785,028	\$ 7,348,461	\$ 2,087,676	\$ 356,321	\$	\$ (2,481,096)	\$ (431,904)	\$ 25,664,48		
Income from Continuing Operations	\$ 5,357,784	\$ 1,757,569	\$ (766,540)	\$ (119,051)	\$ 811,589	\$ 4,309,021	\$ (6,645,749)	\$ 4,704,62		
Total Assets	\$ 860,477,760	\$ 367,714,176	\$ 138,899,065	\$ 980,836	\$	\$ 130,083,814	\$ (83,888,047)	\$ 1,414,267,60		
Provision for Loan/Lease Losses	\$ 746,867	\$ 533,401	\$ 579,956	\$ 223,735	\$	\$	\$	\$ 2,083,95		
Goodwill and Intangible Assets	\$ 3,222,688	\$	\$	\$	\$	\$	\$	\$ 3,222,68		

Table of Contents

Part I

Item 1

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) continued

NOTE 5 COMMITMENTS AND CONTINGENCIES

In the normal course of business, the Company's 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. As of September 30, 2008 and December 31, 2007, commitments to extend credit aggregated were \$472.4 million and \$464.9 million, respectively. As of September 30, 2008 and December 31, 2007, standby, commercial and similar letters of credit aggregated were \$13.7 million and \$14.1 million, respectively. Management does not expect that all of these commitments will be funded.

Contractual obligations and other commitments were presented in the Company's 2007 Annual Report on Form 10-K. There have been no material changes in the Company's contractual obligations and other commitments since that report was filed.

NOTE 6 RECENT ACCOUNTING DEVELOPMENTS

In September 2006, FASB issued Statement of Financial Accounting Standard No. 157 (SFAS No. 157), Fair Value Measurements, which defines fair value, establishes guidelines for measuring fair value and expands disclosures regarding fair value measurements. SFAS No. 157 does not require any new fair value measurements but rather eliminates inconsistencies in guidance found in various prior accounting pronouncements. The Company adopted the provisions of SFAS No. 157 for the quarter ended March 31, 2008. See NOTE 7 for additional information regarding fair value measurements.

In February of 2007, FASB issued Statement of Financial Accounting Standard No. 159 (SFAS No. 159), The Fair Value Option for Financial Assets and Financial Liabilities, which gives entities the option to measure eligible financial assets and financial liabilities at fair value on an instrument by instrument basis, that are otherwise not permitted to be accounted for at fair value under other accounting standards. The election to use the fair value option is available for eligible items that exist on the date that a company adopts SFAS No. 159 or when an entity first recognizes a financial asset or financial liability. The decision to elect the fair value option for an eligible item is irrevocable. Subsequent changes in fair value must be recorded in earnings. This statement is effective as of the beginning of a company's first fiscal year after November 15, 2007. The statement offered early adoption provisions that the Company elected not to exercise. There was no impact on the consolidated financial statements of the Company as a result of the adoption of SFAS No. 159 during the first nine months of 2008 since the Company has not elected the fair value option for any eligible items, as defined in SFAS No. 159.

Table of Contents

Part I

Item 1

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) continued

In December 2007, FASB issued Statement No. 141 (revised 2007), Business Combinations. Statement No. 141R fundamentally changes the manner in which the entity will account for a business combination. This Statement is effective for business combinations for which the acquisition date is on or before fiscal years beginning on or after December 15, 2008 and is predominantly prospective. The Company is currently evaluating the impact of the adoption of Statement No. 141R.

In December 2007, FASB issued Statement No. 160, Noncontrolling Interests in Consolidated Financial Statements. Statement No. 160 changes the measurement, recognition and presentation of minority interests in consolidated subsidiaries (now referred to as noncontrolling interests). This Statement is effective for fiscal years beginning on or after December 15, 2008 and is prospective for the change related to measurement and recognition and retrospective for the changes related to presentation. The Company is currently evaluating the impact of the adoption of Statement No. 160.

In March 2008, the FASB issued Statement of Financial Accounting Standard No. 161 (SFAS No. 161), which provides for enhanced disclosures about how and why an entity uses derivatives and how and where those derivatives and related hedged items are reported in the entity's financial statements. SFAS No. 161 applies to all entities and all derivative instruments and related hedged items accounted for under SFAS No. 133, and is effective for the 2009 fiscal year. Among other things, SFAS No. 161 requires disclosures of an entity's objectives and strategies for using derivatives by primary underlying risk and certain disclosures about the potential future collateral or cash requirements as a result of contingent credit-related features. The Company is currently evaluating the impact of the adoption of SFAS No. 161.

NOTE 7 FAIR VALUE MEASUREMENTS

As discussed in NOTE 6 above, on January 1, 2008, the Company adopted SFAS No. 157, *Fair Value Measurements*. There was no impact on the consolidated financial statements of the Company as a result of this adoption.

SFAS No. 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value. It also establishes a hierarchy for determining fair value measurement. The hierarchy includes three levels and is based upon the valuation techniques used to measure assets and liabilities. The three levels are as follows:

1. Level 1 Inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in markets;
2. 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
3. Level 3 Inputs to the valuation methodology are unobservable and significant to the fair value measurement

Table of ContentsPart I
Item 1

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) continued

Assets measured at fair value on a recurring basis comprise the following at September 30, 2008:

	Fair Value	Fair Value Measurements at Reporting Date Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
(dollars in thousands)				
Securities available for sale	\$ 231,623	\$ 597	\$ 231,026	\$
Total	\$ 231,623	\$ 597	\$ 231,026	\$

A small portion of the securities available for sale portfolio consists of common stocks issued by various unrelated bank holding companies. The fair values used by the Company are obtained from an independent pricing service, which represent quoted market prices for the identical securities (Level 1 inputs).

The large majority of the securities available for sale portfolio consist of U.S. government sponsored agency 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).

Certain financial assets are measured at fair value on a non-recurring basis; that is, the instruments 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). Financial assets measured at fair value on a non-recurring basis were not significant at September 30, 2008.

NOTE 8 RECENT INDUSTRY DEVELOPMENTS

In response to the current economic events, on October 3, 2008, the U.S. Congress passed, and the President signed into law, the Emergency Economic Stabilization Act of 2008 (the Stabilization Act). The Stabilization Act authorizes the Secretary of the U.S. Treasury and the Federal Deposit Insurance Corporation (the FDIC) to implement various temporary emergency programs designed to strengthen the capital positions of financial institutions and stimulate the availability of credit within the U.S. financial system. Pursuant to the Stabilization Act, the U.S. Treasury will have the authority to, among other things, purchase up to \$700 billion of mortgages, mortgage-backed securities and certain other financial instruments from financial institutions for the purpose of stabilizing and providing liquidity to the U.S. financial markets.

Table of Contents

Part I

Item 1

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) continued

On October 14, 2008, the U.S. Treasury announced that it will purchase equity stakes in eligible financial institutions that wish to participate. This program, known as the Capital Purchase Program, allocates \$250 billion from the \$700 billion authorized by the Stabilization Act to the U.S. Treasury for the purchase of senior preferred shares from qualifying financial institutions. Eligible institutions will be able to sell equity interests to the U.S. Treasury in amounts equal to between 1% and 3% of the institution's risk-weighted assets. In conjunction with the purchase of preferred stock, the U.S. Treasury will receive warrants to purchase common stock from the participating institutions with an aggregate market price equal to 15% of the preferred investment. Participating financial institutions will be required to adopt the U.S. Treasury's standards for executive compensation and corporate governance for the period during which the U.S. Treasury holds equity issued under the Capital Purchase Program. Many financial institutions have already announced that they will participate in the Capital Purchase Program. While the Company's management is confident that the Company is well positioned for growth, management is examining whether or not the Company will apply to participate in the Treasury Department's Capital Purchase Plan.

Also on October 14, 2008, using the systemic risk exception to the FDIC Improvement Act of 1991, the U.S. Treasury authorized the FDIC to provide a 100% guarantee of newly-issued senior unsecured debt and deposits in non-interest bearing accounts at FDIC insured institutions. Initially, all eligible financial institutions will automatically be covered under this program, known as the Temporary Liquidity Guarantee Program, without incurring any fees for a period of 30 days. Coverage under the Temporary Liquidity Guarantee Program after the initial 30-day period is available to insured financial institutions at a cost of 75 basis points per annum for senior unsecured debt and 10 basis points per annum for non-interest bearing deposits. After the initial 30-day period, institutions will continue to be covered under the Temporary Liquidity Guarantee Program unless they inform the FDIC that they have decided to opt out of the program. The Company is assessing its participation in the Temporary Liquidity Guarantee Program.

Under the Troubled Asset Auction Program, another initiative based on the authority granted by the Stabilization Act, the U.S. Treasury, through a newly-created Office of Financial Stability, will purchase certain troubled mortgage-related assets from financial institutions in a reverse-auction format. Troubled assets eligible for purchase by the Office of Financial Stability include residential and commercial mortgages originated on or before March 14, 2008, securities or obligations that are based on such mortgages, and any other financial instrument that the Secretary of the U.S. Treasury determines, after consultation with the Chairman of the Board of Governors of the Federal Reserve System, is necessary to promote financial market stability. The U.S. Treasury has not issued any definitive guidance regarding this program and the Company's management has not determined whether or not it will participate.

Table of Contents

Part I

Item 1

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) continued

Under the Stabilization Act, the U.S. Treasury is also required to establish a program that will guarantee principal of, and interest on, troubled assets originated or issued prior to March 14, 2008, including mortgage-backed securities. The program may take any form and may vary by asset class, but it must be voluntary and self-funding. The U.S. Treasury has the authority to set premiums to reflect the credit risk characteristics of the insured assets. The U.S. Treasury has solicited requests for comments on how the program should be structured but no program has been implemented to date. The Stabilization Act also temporarily increases the amount of insurance coverage of deposit accounts held at FDIC-insured depository institutions, including our bank subsidiaries, from \$100,000 to \$250,000. The increased coverage is effective during the period from October 3, 2008 until December 31, 2009.

It is not clear at this time what impact the Stabilization Act, the Capital Purchase Program, the Temporary Liquidity Guarantee Program, the Troubled Asset Auction Program, other liquidity and funding initiatives of the Federal Reserve and other agencies that have been previously announced, and any additional programs that may be initiated in the future will have on the Company's future financial condition and results of operations.

The preceding is a summary of recently enacted laws and regulations that could materially impact the Company's results of operations or financial condition. This discussion is qualified in its entirety by reference to such laws and regulations and should be read in conjunction with Supervision and Regulation discussion contained in the Company's 2007 Form 10-K.

Table of Contents

Part I
Item 2

MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

GENERAL

QCR Holdings, Inc. is the parent company of Quad City Bank & Trust, Cedar Rapids Bank & Trust, Rockford Bank & Trust, First Wisconsin Bank & Trust, and Quad City Bancard, Inc.

Quad City Bank & Trust and Cedar Rapids Bank & Trust are Iowa-chartered commercial banks, Rockford Bank & Trust is an Illinois-chartered commercial bank, and First Wisconsin Bank & Trust is a Wisconsin-chartered bank. All are members of the Federal Reserve System with depository accounts insured to the maximum amount permitted by law by the FDIC.

Quad City Bank & Trust commenced operations in 1994 and provides full-service commercial and consumer banking, and trust and asset management services to the Quad City area and adjacent communities through its five offices that are located in Bettendorf and Davenport, Iowa and Moline, Illinois. Quad City Bank & Trust also provides leasing services through its 80%-owned subsidiary, M2 Lease Funds, located in Brookfield, Wisconsin. During the first quarter of 2008, Quad City Bank & Trust acquired CMG Investment Advisors, LLC, which is an investment management and advisory company.

Cedar Rapids Bank & Trust commenced operations in 2001 and provides full-service commercial and consumer banking services to Cedar Rapids and adjacent communities through its main office located on First Avenue in downtown Cedar Rapids, Iowa and its branch facility located on Council Street in northern Cedar Rapids. Cedar Rapids Bank & Trust also provides residential real estate mortgage lending services through its 50%-owned joint venture, Cedar Rapids Mortgage Company.

Rockford Bank & Trust commenced operations in January 2005 and provides full-service commercial and consumer banking services to Rockford and adjacent communities through its main office located on Guilford Road at Alpine Road in Rockford, and its branch facility located in downtown Rockford.

First Wisconsin Bank & Trust is a wholly owned subsidiary of the Company providing full-service commercial and consumer banking services in the Milwaukee area through its main office located in Brookfield, Wisconsin. The Company has operated this charter since February, 2007. As discussed in the footnotes to the financial statements, in October, 2008 the Company entered into a definitive agreement to sell FWBT. The activity related to FWBT is accounted for as discontinued operations.

Bancard provides cardholder credit card processing services. Bancard currently provides credit card processing for its agent banks and for cardholders of the Company's subsidiary banks and agent banks. As discussed in the footnotes to the financial statements, the Company sold the merchant credit card acquiring business segment of Bancard during the third quarter of 2008. The activity related to the merchant credit card acquiring business is accounted for as discontinued operations.

Table of Contents

Part I

Item 2

MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

OVERVIEW

The Company reported earnings for the third quarter ended September 30, 2008 of \$4.3 million, which resulted in diluted earnings per share for common shareholders of \$0.83. During the third quarter of 2008, the Company's wholly owned subsidiary, Bancard, sold its merchant credit card acquiring business resulting in a gain on sale, net of taxes and related expenses, of approximately \$3.0 million or \$0.66 per share. Earnings from continuing operations for the third quarter ended September 30, 2008 were \$1.6 million, which resulted in diluted earnings per share of \$0.25. Earnings from continuing operations and diluted earnings per share for the third quarter of 2007 were \$1.7 million and \$0.32, respectively.

For the nine months ended September 30, 2008, earnings totaled \$6.8 million leading to diluted earnings per share of \$1.17. As mentioned above, the gain on sale of the merchant credit card acquiring business was the major contributor to the increase in earnings. Earnings from continuing operations and diluted earnings per share for the nine months ended September 30, 2008 were \$5.3 million and \$0.85, respectively. By comparison, for the nine months ended September 30, 2007, earnings from continuing operations totaled \$4.7 million which resulted in diluted earnings per share of \$0.85. The Company has experienced strong growth in net interest income over the first nine months. This growth has been partially offset by significant increases in the provision for loan/lease losses. Earnings from continuing operations before the provision for loan/lease losses and taxes for the nine months ended September 30, 2008 were \$11.9 million which represents an increase of \$3.1 million, or nearly 36%, from \$8.8 million for the nine months ended September 30, 2007.

When compared to the second quarter of 2008, earnings from continuing operations decreased from \$2.0 million to \$1.6 million, or 20%, for the third quarter of 2008. The primary reason for this decrease in earnings was a significant increase in the provision for loan/lease losses.

Table of Contents

Part I
Item 2

MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

NET INTEREST INCOME

The Company's operating results are derived largely from net interest income. Net interest income is the difference between interest income, principally from loans and investment securities, and interest expense, principally on borrowings and customer deposits. Changes in net interest income result from changes in volume, net interest spread and net interest margin. Volume refers to the average dollar levels of interest-earning assets and interest-bearing liabilities. Net interest spread refers to the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities. Net interest margin refers to net interest income divided by average interest-earning assets and is influenced by the level and relative mix of interest-earning assets and interest-bearing liabilities.

Net interest income increased \$2.7 million, or 30%, to \$11.9 million for the quarter ended September 30, 2008, from \$9.1 million for the third quarter of 2007. For the third quarter of 2008, average earning assets increased by \$159.2 million, or 13%, and average interest-bearing liabilities increased by \$127.2 million, or 11%, when compared with average balances for the third quarter of 2007. A comparison of yields, spread and margin from the third quarter of 2008 to the third quarter of 2007 is as follows:

The average yield on interest-earning assets decreased 78 basis points.

The average cost of interest-bearing liabilities decreased 129 basis points.

The net interest spread improved 51 basis points from 2.63% to 3.14%.

The net interest margin improved 45 basis points from 2.99% to 3.44%.

Net interest income increased \$7.4 million, or 28%, to \$33.4 million for the nine months ended September 30, 2008, from \$26.0 million for the first nine months of 2007. For the first nine months of 2008, average earning assets increased by \$151.9 million, or 13%, and average interest-bearing liabilities increased by \$136.5 million, or 13%, when compared with average balances for the first three quarters of 2007. A comparison of yields, spread and margin from the first nine months of 2008 to the first nine months of 2007 is as follows:

The average yield on interest-earning assets decreased 57 basis points.

The average cost of interest-bearing liabilities decreased 105 basis points.

The net interest spread improved 48 basis points from 2.55% to 3.03%.

The net interest margin improved 40 basis points from 2.92% to 3.32%.

Table of ContentsPart I
Item 2MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

The Company's average balances, interest income/expense, and rates earned/paid on major balance sheet categories, as well as the components of change in net interest income, are presented in the following tables:

	For the Three Months Ended September 30,					
	2008			2007		
	Average Balance	Interest Earned or Paid	Average Yield or Cost (dollars in thousands)	Average Balance	Interest Earned or Paid	Average Yield or Cost
ASSETS						
Interest earning assets:						
Federal funds sold	\$ 4,395	\$ 28	2.55%	\$ 3,837	\$ 41	4.27%
Interest-bearing deposits at financial institutions	1,041	10	3.84%	4,783	71	5.94%
Investment securities (1)	230,880	3,083	5.34%	209,802	2,759	5.26%
Gross loans/leases receivable (2)	1,143,273	18,531	6.48%	1,001,950	18,674	7.46%
Total interest earning assets	\$ 1,379,589	21,652	6.28%	\$ 1,220,372	21,545	7.06%
Noninterest-earning assets:						
Cash and due from banks	\$ 32,116			\$ 38,440		
Premises and equipment	31,506			31,695		
Less allowance for estimated losses on loans/leases	(13,987)			(11,410)		
Other	170,994			93,356		
Total assets	\$ 1,600,218			\$ 1,372,453		
LIABILITIES AND STOCKHOLDERS EQUITY						
Interest-bearing liabilities:						
Interest-bearing demand deposits	\$ 279,829	1,211	1.73%	\$ 310,877	2,806	3.61%
Savings deposits	67,193	231	1.38%	31,685	170	2.15%
Time deposits	442,058	4,128	3.74%	387,946	4,871	5.02%
Short-term borrowings	147,487	656	1.78%	160,429	1,472	3.67%
Federal Home Loan Bank advances	204,947	2,249	4.39%	161,344	1,859	4.61%
Junior subordinated debentures	36,085	573	6.35%	36,085	661	7.33%

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Other borrowings	71,933	752	4.18%	33,931	591	6.97%
Total interest-bearing liabilities	\$ 1,249,532	9,800	3.14%	\$ 1,122,297	12,430	4.43%
Noninterest-bearing demand	137,340			\$ 124,564		
Other noninterest-bearing liabilities	122,514			48,794		
Total liabilities	\$ 1,509,386			\$ 1,295,655		
Minority interest in consolidated subsidiaries	1,928			1,619		
Stockholders' equity	88,904			75,180		
Total liabilities and stockholders' equity	\$ 1,600,218			\$ 1,372,453		
Net interest income		\$ 11,852			\$ 9,115	
Net interest spread			3.14%			2.63%
Net interest margin			3.44%			2.99%
Ratio of average interest earning assets to average interest-bearing liabilities	110.41%			108.74%		

(1) Interest earned and yields on nontaxable investment securities are determined on a tax equivalent basis using a 34% tax rate for each period presented.

(2) Loan fees are not material and are included in interest income

from loans
receivable.

Table of ContentsPart I
Item 2

MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued
Analysis of Changes of Interest Income/Interest Expense
For the Three Months Ended September 30, 2008

	Inc./(Dec.) from Prior Period	Components of Change (1)	
		Rate	Volume
		2008 vs. 2007	
		(Dollars in Thousands)	
INTEREST INCOME			
Federal funds sold	\$ (13)	\$ (45)	\$ 32
Interest-bearing deposits at financial institutions	(61)	(19)	(42)
Investment securities (2)	324	43	281
Gross loans/leases receivable (3)	(143)	(10,188)	10,045
Total change in interest income	\$ 107	\$ (10,209)	\$ 10,316
INTEREST EXPENSE			
Interest-bearing demand deposits	\$ (1,595)	\$ (1,338)	\$ (257)
Savings deposits	61	(355)	416
Time deposits	(743)	(4,001)	3,258
Short-term borrowings	(816)	(706)	(110)
Federal Home Loan Bank advances	390	(544)	934
Junior subordinated debentures	(88)	(88)	
Other borrowings	161	(1,351)	1,512
Total change in interest expense	\$ (2,630)	\$ (8,383)	\$ 5,753
Total change in net interest income	\$ 2,737	\$ (1,826)	\$ 4,563

(1) The column increase/decrease from prior period 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 are determined on a tax equivalent basis using a 34% tax rate for each period presented.
- (3) Loan fees are not material and are included in interest income from loans/leases receivable.

Table of ContentsPart I
Item 2MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

	For the Nine Months Ended September 30,					
	2008			2007		
	Average Balance	Interest Earned or Paid	Average Yield or Cost (dollars in thousands)	Average Balance	Interest Earned or Paid	Average Yield or Cost
ASSETS						
Interest earnings assets:						
Federal funds sold	\$ 3,410	70	2.74%	\$ 6,163	214	4.63%
Interest-bearing deposits at financial institutions	6,572	158	3.21%	6,975	295	5.64%
Investment securities (1)	226,186	9,077	5.35%	197,461	7,620	5.15%
Gross loans receivable (2)	1,105,698	54,844	6.61%	979,414	53,784	7.32%
Total interest earning assets	\$ 1,341,866	64,149	6.37%	\$ 1,190,013	61,913	6.94%
Noninterest-earning assets:						