

MidWestOne Financial Group, Inc.  
Form 10-Q  
April 30, 2015

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

FORM 10-Q

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

For the quarterly period ended March 31, 2015

OR

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 001-35968

MIDWESTONE FINANCIAL GROUP, INC.  
(Exact name of Registrant as specified in its charter)

Iowa 42-1206172  
(State or other jurisdiction of incorporation or (I.R.S. Employer Identification No.)  
organization)  
102 South Clinton Street  
Iowa City, IA 52240  
(Address of principal executive offices, including zip code)  
319-356-5800  
(Registrant's telephone number, including area code)

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

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

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

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

Edgar Filing: MidWestOne Financial Group, Inc. - Form 10-Q

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

As of April 29, 2015, there were 8,374,598 shares of common stock, \$1.00 par value per share, outstanding.

---

Table of Contents

MIDWESTONE FINANCIAL GROUP, INC.  
 Form 10-Q Quarterly Report  
 Table of Contents

	Page No.
PART I	
Item 1. <u>Financial Statements</u>	<u>1</u>
<u>Consolidated Balance Sheets</u>	<u>1</u>
<u>Consolidated Statements of Operations</u>	<u>2</u>
<u>Consolidated Statements of Comprehensive Income</u>	<u>3</u>
<u>Consolidated Statements of Shareholders' Equity</u>	<u>4</u>
<u>Consolidated Statements of Cash Flows</u>	<u>5</u>
<u>Notes to Consolidated Financial Statements</u>	<u>6</u>
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>31</u>
Item 3. <u>Quantitative and Qualitative Disclosures about Market Risk</u>	<u>47</u>
Item 4. <u>Controls and Procedures</u>	<u>49</u>
Part II	
Item 1. <u>Legal Proceedings</u>	<u>51</u>
Item 1A. <u>Risk Factors</u>	<u>51</u>
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>51</u>
Item 3. <u>Defaults Upon Senior Securities</u>	<u>51</u>
Item 4. <u>Mine Safety Disclosures</u>	<u>51</u>
Item 5. <u>Other Information</u>	<u>51</u>
Item 6. <u>Exhibits</u>	<u>52</u>
<u>Signatures</u>	<u>53</u>

---

Table of Contents

## PART I – FINANCIAL INFORMATION

## Item 1. Financial Statements.

MIDWESTONE FINANCIAL GROUP, INC. AND SUBSIDIARIES  
CONSOLIDATED BALANCE SHEETS

	March 31, 2015	December 31, 2014
(dollars in thousands, except per share amounts)	(unaudited)	
<b>ASSETS</b>		
Cash and due from banks	\$18,954	\$23,028
Interest-bearing deposits in banks	1,013	381
Federal funds sold	1,489	—
Cash and cash equivalents	21,456	23,409
Investment securities:		
Available for sale	408,950	474,942
Held to maturity (fair value of \$54,574 as of March 31, 2015 and \$51,253 as of December 31, 2014)	54,293	51,524
Loans held for sale	2,281	801
Loans	1,176,327	1,132,519
Allowance for loan losses	(16,526)	(16,363)
Net loans	1,159,801	1,116,156
Loan pool participations, net	18,230	19,332
Premises and equipment, net	39,443	37,770
Accrued interest receivable	9,358	10,898
Intangible assets, net	8,151	8,259
Bank-owned life insurance	38,437	38,142
Other real estate owned	1,652	1,916
Deferred income taxes	2,392	3,078
Other assets	13,533	14,075
Total assets	\$1,777,977	\$1,800,302
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Deposits:		
Non-interest-bearing demand	\$212,711	\$214,461
Interest-bearing checking	628,990	618,540
Savings	106,380	102,527
Certificates of deposit under \$100,000	229,543	235,395
Certificates of deposit \$100,000 and over	230,629	237,619
Total deposits	1,408,253	1,408,542
Federal funds purchased	8,900	17,408
Securities sold under agreements to repurchase	55,326	60,821
Federal Home Loan Bank borrowings	78,000	93,000
Deferred compensation liability	3,402	3,393
Long-term debt	15,464	15,464
Accrued interest payable	932	863
Other liabilities	10,308	8,080
Total liabilities	1,580,585	1,607,571
Shareholders' equity:	\$—	\$—

Edgar Filing: MidWestOne Financial Group, Inc. - Form 10-Q

Preferred stock, no par value; authorized 500,000 shares; no shares issued and outstanding at March 31, 2015 and December 31, 2014		
Common stock, \$1.00 par value; authorized 15,000,000 shares at March 31, 2015 and December 31, 2014; issued 8,690,398 shares at March 31, 2015 and December 31, 2014; outstanding 8,370,309 shares at March 31, 2015 and 8,355,666 shares at December 31, 2014	8,690	8,690
Additional paid-in capital	80,380	80,537
Treasury stock at cost, 320,089 shares as of March 31, 2015 and 334,732 shares at December 31, 2014	(6,651	) (6,945
Retained earnings	108,667	105,127
Accumulated other comprehensive income	6,306	5,322
Total shareholders' equity	197,392	192,731
Total liabilities and shareholders' equity	\$1,777,977	\$1,800,302

See accompanying notes to consolidated financial statements.

Table of ContentsMIDWESTONE FINANCIAL GROUP, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF OPERATIONS

(unaudited) (dollars in thousands, except per share amounts)	Three Months Ended	
	March 31, 2015	2014
Interest income:		
Interest and fees on loans	\$12,577	\$11,940
Interest and discount on loan pool participations	620	280
Interest on bank deposits	1	4
Interest on investment securities:		
Taxable securities	1,894	2,316
Tax-exempt securities	1,390	1,381
Total interest income	16,482	15,921
Interest expense:		
Interest on deposits:		
Interest-bearing checking	535	545
Savings	36	36
Certificates of deposit under \$100,000	626	697
Certificates of deposit \$100,000 and over	526	445
Total interest expense on deposits	1,723	1,723
Interest on federal funds purchased	12	1
Interest on securities sold under agreements to repurchase	30	30
Interest on Federal Home Loan Bank borrowings	399	562
Interest on other borrowings	4	6
Interest on long-term debt	72	72
Total interest expense	2,240	2,394
Net interest income	14,242	13,527
Provision for loan losses	600	450
Net interest income after provision for loan losses	13,642	13,077
Noninterest income:		
Trust, investment, and insurance fees	1,581	1,518
Service charges and fees on deposit accounts	733	628
Mortgage origination and loan servicing fees	238	437
Other service charges, commissions and fees	603	619
Bank-owned life insurance income	295	229
Gain on sale or call of available for sale securities (Includes \$555 and \$783 reclassified from accumulated other comprehensive income for net gains on available for sale securities for the three months ended March 31, 2015 and 2014, respectively)	555	783
Gain on sale of premises and equipment	3	3
Total noninterest income	4,008	4,217
Noninterest expense:		
Salaries and employee benefits	6,869	6,134
Net occupancy and equipment expense	1,524	1,605
Professional fees	680	575
Data processing expense	432	424
FDIC insurance expense	239	243
Amortization of intangible assets	108	137
Other operating expense	1,327	1,274

Edgar Filing: MidWestOne Financial Group, Inc. - Form 10-Q

Total noninterest expense	11,179	10,392
Income before income tax expense	6,471	6,902
Income tax expense (Includes \$216 and \$305 income tax expense reclassified from accumulated other comprehensive income for the three months ended March 31, 2015 and 2014, respectively)	1,675	1,929
Net income	\$4,796	\$4,973
Share and per share information:		
Ending number of shares outstanding	8,370,309	8,471,761
Average number of shares outstanding	8,363,861	8,475,593
Diluted average number of shares	8,394,026	8,507,973
Earnings per common share - basic	\$0.57	\$0.59
Earnings per common share - diluted	0.57	0.58
Dividends paid per common share	0.150	0.145
See accompanying notes to consolidated financial statements.		

Table of ContentsMIDWESTONE FINANCIAL GROUP, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(unaudited) (dollars in thousands)	Three Months Ended March 31,	
	2015	2014
Net income	\$4,796	\$4,973
Other comprehensive income, available for sale securities:		
Unrealized holding gains arising during period	2,156	3,888
Reclassification adjustment for gains included in net income	(555 )	(783 )
Income tax expense	(617 )	(1,177 )
Other comprehensive income on available for sale securities	984	1,928
Other comprehensive income, net of tax	984	1,928
Comprehensive income	\$5,780	\$6,901
See accompanying notes to consolidated financial statements.		



Table of ContentsMIDWESTONE FINANCIAL GROUP, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(unaudited) (dollars in thousands, except per share amounts)	Preferred Stock	Common Stock	Additional Paid-in Capital	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Income (loss)	Total
Balance at December 31, 2013	\$ —	\$ 8,690	\$ 80,506	\$(3,702)	\$91,473	\$ 1,049	\$178,016
Net income	—	—	—	—	4,973	—	4,973
Dividends paid on common stock (\$0.145 per share)	—	—	—	—	(1,228)	—	(1,228)
Stock options exercised (2,310 shares)	—	—	(1)	42	—	—	41
Release/lapse of restriction on RSUs (19,111 shares)	—	—	(276)	296	—	—	20
Repurchase of common stock (29,466 shares)	—	—	—	(716)	—	—	(716)
Stock compensation	—	—	109	—	—	—	109
Other comprehensive income, net of tax	—	—	—	—	—	1,928	1,928
Balance at March 31, 2014	\$ —	\$ 8,690	\$ 80,338	\$(4,080)	\$95,218	\$ 2,977	\$183,143
Balance at December 31, 2014	\$ —	\$ 8,690	\$ 80,537	\$(6,945)	\$105,127	\$ 5,322	\$192,731
Net income	—	—	—	—	4,796	—	4,796
Dividends paid on common stock (\$0.15 per share)	—	—	—	—	(1,256)	—	(1,256)
Release/lapse of restriction on RSUs (15,853 shares)	—	—	(283)	294	—	—	11
Stock compensation	—	—	126	—	—	—	126
Other comprehensive income, net of tax	—	—	—	—	—	984	984
Balance at March 31, 2015	\$ —	\$ 8,690	\$ 80,380	\$(6,651)	\$108,667	\$ 6,306	\$197,392

See accompanying notes to consolidated financial statements.

Table of ContentsMIDWESTONE FINANCIAL GROUP, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited) (dollars in thousands)	Three Months Ended March 31,	
	2015	2014
Cash flows from operating activities:		
Net income	\$4,796	\$4,973
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	600	450
Depreciation, amortization and accretion	929	1,149
Loss on sale of premises and equipment	(3	) (3
Deferred income taxes	69	2,852
Stock-based compensation	126	109
Net gain on sale or call of available for sale securities	(555	) (783
Net gain on sale of other real estate owned	(16	) (5
Net gain on sale of loans held for sale	(80	) (76
Origination of loans held for sale	(13,791	) (4,184
Proceeds from sales of loans held for sale	12,391	4,528
Decrease in accrued interest receivable	1,540	1,120
Increase in cash surrender value of bank-owned life insurance	(295	) (229
(Increase) decrease in other assets	542	(1,370
Increase (decrease) in deferred compensation liability	9	(22
Increase (decrease) in accrued interest payable, accounts payable, accrued expenses, and other liabilities	2,297	(2,772
Net cash provided by operating activities	8,559	5,737
Cash flows from investing activities:		
Proceeds from sales of available for sale securities	48,261	3,250
Proceeds from maturities and calls of available for sale securities	19,581	13,368
Purchases of available for sale securities	(7	) (11,529
Proceeds from maturities and calls of held to maturity securities	257	228
Purchase of held to maturity securities	(3,034	) (1,564
(Increase) decrease in loans	(44,245	) 15,029
Decrease in loan pool participations, net	1,102	2,133
Purchases of premises and equipment	(2,180	) (2,775
Proceeds from sale of other real estate owned	280	7
Proceeds from sale of premises and equipment	10	3
Net cash provided by investing activities	20,025	18,150
Cash flows from financing activities:		
Net increase (decrease) in deposits	(289	) 734
Decrease in federal funds purchased	(8,508	) (5,482
Decrease in securities sold under agreements to repurchase	(5,495	) (8,890
Proceeds from Federal Home Loan Bank borrowings	—	12,000
Repayment of Federal Home Loan Bank borrowings	(15,000	) (10,000
Stock options exercised	11	61
Dividends paid	(1,256	) (1,228
Repurchase of common stock	—	(716
Net cash used in financing activities	(30,537	) (13,521
Net increase (decrease) in cash and cash equivalents	(1,953	) 10,366

Edgar Filing: MidWestOne Financial Group, Inc. - Form 10-Q

Cash and cash equivalents at beginning of period	23,409	24,890
Cash and cash equivalents at end of period	\$21,456	\$35,256
Supplemental disclosures of cash flow information:		
Cash paid during the period for interest	\$2,171	\$2,459
Cash paid during the period for income taxes	\$200	\$150
Supplemental schedule of non-cash investing activities:		
Transfer of loans to other real estate owned	\$—	\$228
See accompanying notes to consolidated financial statements.		

Table of Contents

MidWestOne Financial Group, Inc. and Subsidiaries  
Notes to Consolidated Financial Statements  
(Unaudited)

1. Principles of Consolidation and Presentation

MidWestOne Financial Group, Inc. (the "Company," which is also referred to herein as "we," "our" or "us") is an Iowa corporation incorporated in 1983, a bank holding company under the Bank Holding Company Act of 1956 and a financial holding company under the Gramm-Leach-Bliley Act of 1999. Our principal executive offices are located at 102 South Clinton Street, Iowa City, Iowa 52240.

The Company owns 100% of the outstanding common stock of MidWestOne Bank, an Iowa state non-member bank chartered in 1934 with its main office in Iowa City, Iowa (the "Bank"), and 100% of the common stock of MidWestOne Insurance Services, Inc., Oskaloosa, Iowa. We operate primarily through our bank subsidiary, MidWestOne Bank, and MidWestOne Insurance Services, Inc., our wholly-owned subsidiary that operates an insurance agency business through six offices located in central and east-central Iowa.

The accompanying unaudited consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and, therefore, do not include all the information and notes necessary for complete financial statements in conformity with U.S. Generally Accepted Accounting Principles ("GAAP"). The information in this Quarterly Report on Form 10-Q is written with the presumption that the users of the interim financial statements have read or have access to the most recent Annual Report on Form 10-K of the Company, which contains the latest audited financial statements and notes thereto, together with Management's Discussion and Analysis of Financial Condition and Results of Operations as of December 31, 2014 and for the year then ended. Management believes that the disclosures are adequate to make the information presented not misleading. In the opinion of management, the accompanying consolidated financial statements contain all adjustments (consisting of only normal recurring accruals) necessary to present fairly the Company's financial position as of March 31, 2015, and the results of operations and cash flows for the three months ended March 31, 2015 and 2014. All significant intercompany accounts and transactions have been eliminated in consolidation.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect: (1) the reported amounts of assets and liabilities, (2) the disclosure of contingent assets and liabilities at the date of the financial statements, and (3) the reported amounts of revenues and expenses during the reporting period. These estimates are based on information available to management at the time the estimates are made. Actual results could differ from those estimates. The results for the three months ended March 31, 2015 may not be indicative of results for the year ending December 31, 2015, or for any other period.

All significant accounting policies followed in the preparation of the quarterly financial statements are disclosed in the Annual Report on Form 10-K for the year ended December 31, 2014. In the consolidated statements of cash flows, cash and cash equivalents include cash and due from banks and interest-bearing deposits in banks.

On April 23, 2015, the Company held a special meeting of shareholders, at which the Company's shareholders voted to approve the merger agreement with Central Bancshares, Inc., a Minnesota corporation ("Central Bancshares"), pursuant to which Central Bancshares will merge with and into the Company. In connection with the merger, Central Bank, a Minnesota-chartered commercial bank and wholly-owned subsidiary of Central Bancshares, will become a wholly-owned subsidiary of the Company. The corporate headquarters of the combined company will be in Iowa City, Iowa.

Subject to the terms and conditions of the merger agreement, each share of common stock of Central Bancshares will automatically be converted into the right to receive a pro rata portion of (i) 2,723,083 shares of common stock of the Company and (ii) \$64.0 million in cash, subject to certain adjustments as described in the merger agreement. The transaction is expected to be completed in May 2015.

2. Shareholders' Equity

Preferred Stock: The number of authorized shares of preferred stock for the Company is 500,000. As of March 31, 2015, none were issued or outstanding.

Common Stock: As of March 31, 2015, the number of authorized shares of common stock for the Company was 15,000,000. As of March 31, 2015, 8,370,309 shares were outstanding.

On July 17, 2014, the board of directors of the Company approved a new share repurchase program, allowing for the repurchase of up to \$5.0 million of stock through December 31, 2016. The new repurchase program replaced the Company's prior repurchase program, pursuant to which the Company had repurchased approximately \$3.7 million of

Table of Contents

common stock since January 1, 2013. Pursuant to the new program, the Company may continue to repurchase shares from time to time in the open market, and the method, timing and amounts of repurchase will be solely in the discretion of the Company's management. The repurchase program does not require the Company to acquire a specific number of shares. Therefore, the amount of shares repurchased pursuant to the program will depend on several factors, including market conditions, capital and liquidity requirements, and alternative uses for cash available. During the first quarter 2015 the Company repurchased no common stock. Of the \$5.0 million of stock authorized under the repurchase plan, \$3.8 million remained available for possible future repurchases as of March 31, 2015.

### 3. Earnings per Common Share

Basic per-share amounts are computed by dividing net income (the numerator) by the weighted-average number of common shares outstanding (the denominator). Diluted per share amounts assume issuance of all common stock issuable upon conversion or exercise of other securities, unless the effect is to reduce the loss or increase the income per common share from continuing operations.

The following table presents the computation of earnings per common share for the respective periods:

	Three Months Ended March 31,	
(dollars in thousands, except per share amounts)	2015	2014
Basic earnings per common share computation		
Numerator:		
Net income	\$4,796	\$4,973
Denominator:		
Weighted average shares outstanding	8,363,861	8,475,593
Basic earnings per common share	\$0.57	\$0.59
Diluted earnings per common share computation		
Numerator:		
Net income	\$4,796	\$4,973
Denominator:		
Weighted average shares outstanding, including all dilutive potential shares	8,394,026	8,507,973
Diluted earnings per common share	\$0.57	\$0.58

### 4. Investment Securities

The amortized cost and fair value of investment securities available for sale, with gross unrealized gains and losses, are as follows:

	As of March 31, 2015			
(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
U.S. Government agencies and corporations	\$26,766	\$229	\$28	\$26,967
State and political subdivisions	182,978	8,558	114	191,422
Mortgage-backed securities	28,971	1,522	—	30,493
Collateralized mortgage obligations	115,443	808	1,191	115,060
Corporate debt securities	43,392	373	24	43,741
Total debt securities	397,550	11,490	1,357	407,683
Other equity securities	1,243	46	22	1,267
Total	\$398,793	\$11,536	\$1,379	\$408,950



Table of Contents

	As of December 31, 2014			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
(in thousands)				
U.S. Government agencies and corporations	\$49,392	\$248	\$265	\$49,375
State and political subdivisions	187,276	8,113	190	195,199
Mortgage-backed securities	30,965	1,498	—	32,463
Collateralized mortgage obligations	147,412	813	2,093	146,132
Corporate debt securities	48,656	188	103	48,741
Total debt securities	463,701	10,860	2,651	471,910
Other equity securities	2,686	380	34	3,032
Total	\$466,387	\$11,240	\$2,685	\$474,942

The amortized cost and fair value of investment securities held to maturity, with gross unrealized gains and losses, are as follows:

	As of March 31, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
(in thousands)				
State and political subdivisions	\$42,252	\$654	\$147	\$42,759
Mortgage-backed securities	21	3	—	24
Collateralized mortgage obligations	8,288	—	91	8,197
Corporate debt securities	3,732	—	138	3,594
Total	\$54,293	\$657	\$376	\$54,574

	As of December 31, 2014			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
(in thousands)				
State and political subdivisions	\$39,704	\$370	\$252	\$39,822
Mortgage-backed securities	22	3	—	25
Collateralized mortgage obligations	8,531	—	233	8,298
Corporate debt securities	3,267	—	159	3,108
Total	\$51,524	\$373	\$644	\$51,253

Investment securities with a carrying value of \$182.1 million and \$200.7 million at March 31, 2015 and December 31, 2014, respectively, were pledged on public deposits, securities sold under agreements to repurchase and for other purposes, as required or permitted by law.

The summary of investment securities shows that some of the securities in the available for sale and held to maturity investment portfolios had unrealized losses, or were temporarily impaired, as of March 31, 2015 and December 31, 2014. This temporary impairment represents the estimated amount of loss that would be realized if the securities were sold on the valuation date.



Table of Contents

The following presents information pertaining to securities with gross unrealized losses as of March 31, 2015 and December 31, 2014, aggregated by investment category and length of time that individual securities have been in a continuous loss position:

		As of March 31, 2015					
		Number of Securities	Less than Fair Value	12 Months Unrealized Losses	12 Months or More Fair Value	Total Fair Value	Unrealized Losses
Available for Sale (in thousands, except number of securities)							
U.S. Government agencies and corporations	1	\$—	\$—	\$7,726	\$ 28	\$7,726	\$ 28
State and political subdivisions	26	3,209	31	2,946	83	6,155	114
Collateralized mortgage obligations	10	11,952	81	48,729	1,110	60,681	1,191
Corporate debt securities	3	5,117	3	3,308	21	8,425	24
Other equity securities	1	—	—	978	22	978	22
Total	41	\$20,278	\$ 115	\$63,687	\$ 1,264	\$83,965	\$ 1,379
		As of December 31, 2014					
		Number of Securities	Less than Fair Value	12 Months Unrealized Losses	12 Months or More Fair Value	Total Fair Value	Unrealized Losses
(in thousands, except number of securities)							
U.S. Government agencies and corporations	4	\$9,946	\$ 11	\$15,018	\$ 254	\$24,964	\$ 265
State and political subdivisions	46	3,024	18	10,728	172	13,752	190
Collateralized mortgage obligations	14	14,971	123	68,370	1,970	83,341	2,093
Corporate debt securities	7	23,024	50	3,400	53	26,424	103
Other equity securities	1	—	—	966	34	966	34
Total	72	\$50,965	\$ 202	\$98,482	\$ 2,483	\$149,447	\$ 2,685
		As of March 31, 2015					
		Number of Securities	Less than Fair Value	12 Months Unrealized Losses	12 Months or More Fair Value	Total Fair Value	Unrealized Losses
Held to Maturity (in thousands, except number of securities)							
State and political subdivisions	19	\$4,375	\$ 135	\$1,687	\$ 12	\$6,062	\$ 147
Collateralized mortgage obligations	1	8,197	91	—	—	8,197	91
Corporate debt securities	2	2,379	5	750	133	3,129	138
Total	22	\$14,951	\$ 231	\$2,437	\$ 145	\$17,388	\$ 376
		As of December 31, 2014					
		Number of Securities	Less than Fair Value	12 Months Unrealized Losses	12 Months or More Fair Value	Total Fair Value	Unrealized Losses
(in thousands, except number of securities)							
State and political subdivisions	29	\$5,322	\$ 190	\$9,144	\$ 62	\$14,466	\$ 252

Collateralized mortgage obligations	1	—	—	8,298	233	8,298	233
Corporate debt securities	2	2,358	27	750	132	3,108	159
Total	32	\$7,680	\$ 217	\$18,192	\$ 427	\$25,872	\$ 644

The Company's assessment of other-than-temporary impairment ("OTTI") is based on its reasonable judgment of the specific facts and circumstances impacting each individual security at the time such assessments are made. The Company reviews and considers factual information, including expected cash flows, the structure of the security, the creditworthiness of the issuer, the type of underlying assets, if any, and the current and anticipated market conditions. At March 31, 2015 and December 31, 2014, the Company's mortgage-backed securities and collateralized mortgage obligations portfolios consisted of securities predominantly backed by one- to four-family mortgage loans and underwritten to the standards of and guaranteed by the following government-sponsored agencies: the Federal Home Loan Mortgage Corporation ("FHLMC"), the Federal National Mortgage Association ("FNMA"), and the Government

Table of Contents

National Mortgage Association ("GNMA"). The receipt of principal, at par, and interest on mortgage-backed securities is guaranteed by the respective government-sponsored agency guarantor, such that the Company believes that its mortgage-backed securities do not expose the Company to credit-related losses.

At March 31, 2015, approximately 60% of the municipal bonds held by the Company were Iowa-based. The Company does not intend to sell these municipal obligations, and it is not more likely than not that the Company will be required to sell them before the recovery of their cost. Due to the issuers' continued satisfaction of their obligations under the securities in accordance with their contractual terms and the expectation that they will continue to do so, management's intent and ability to hold these securities for a period of time sufficient to allow for any anticipated recovery in fair value, as well as the evaluation of the fundamentals of the issuers' financial conditions and other objective evidence, the Company believes that the municipal obligations identified in the tables above were temporarily depressed as of March 31, 2015 and December 31, 2014.

As of March 31, 2015, the Company also owned \$0.3 million of equity securities in banks and financial service-related companies, and \$1.0 million of mutual funds invested in debt securities and other debt instruments that will cause units of the fund to be deemed to be qualified under the Community Reinvestment Act. Equity securities are considered to have OTTI whenever they have been in a loss position, compared to current book value, for twelve consecutive months, and the Company does not expect them to recover to their original cost basis. For the three months ended March 31, 2015 and the full year of 2014, no impairment charges were recorded, as the affected equity securities were not deemed impaired due to stabilized market prices in relation to the Company's original purchase price.

The following table provides a roll forward of credit losses on fixed maturity securities recognized in net income:

	For the Three Months Ended March 31,	
	2015	2014
(in thousands)		
Beginning balance	\$—	\$6,639
Additional credit losses:		
Reductions to credit losses:		
Securities with other than temporary impairment, due to liquidation	—	—
Securities with other than temporary impairment, due to sale	—	(6,639)
Ending balance	\$—	\$—

It is reasonably possible that the fair values of the Company's investment securities could decline in the future if the overall economy or the financial conditions of the issuers deteriorate. As a result, there is a risk that additional OTTI may be recognized in the future and any such amounts could be material to the Company's consolidated statements of operations.

The contractual maturity distribution of investment debt securities at March 31, 2015, is summarized as follows:

	Available For Sale		Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
(in thousands)				
Due in one year or less	\$25,853	\$26,079	\$190	\$190
Due after one year through five years	91,538	93,854	3,030	3,026
Due after five years through ten years	102,394	107,758	20,111	20,410
Due after ten years	33,351	34,439	22,653	22,727
Debt securities without a single maturity date	144,414	145,553	8,309	8,221
Total	\$397,550	\$407,683	\$54,293	\$54,574

Mortgage-backed securities and collateralized mortgage obligations are collateralized by mortgage loans and guaranteed by U.S. government agencies. Experience has indicated that principal payments will be collected sooner

than scheduled because of prepayments. Therefore, these securities are not scheduled in the maturity categories indicated above. Equity securities available for sale with an amortized cost of \$1.2 million and a fair value of \$1.3 million are also excluded from this table.

Other investment securities include investments in Federal Home Loan Bank (“FHLB”) stock. The carrying value of the FHLB stock at March 31, 2015 was \$8.0 million and at December 31, 2014 was \$8.6 million, which is included in the Other Assets line of the consolidated balance sheets. This security is not readily marketable and ownership of FHLB

Table of Contents

stock is a requirement for membership in the FHLB-Des Moines. The amount of FHLB stock the Bank is required to hold is directly related to the amount of FHLB advances borrowed. Because there are no available market values, this security is carried at cost and evaluated for potential impairment each quarter. Redemption of this investment is at the option of the FHLB.

Realized gains and losses on sales are determined on the basis of specific identification of investments based on the trade date. Realized gains on investments for the three months ended March 31, 2015 and 2014 are as follows:

	Three Months Ended March 31,	
	2015	2014
(in thousands)		
Available for sale fixed maturity securities:		
Gross realized gains	\$441	\$929
Gross realized losses	(74 )	(146 )
Other-than-temporary impairment	—	—
	367	783
Equity securities:		
Gross realized gains	188	—
Gross realized losses	—	—
Other-than-temporary impairment	—	—
	188	—
Total net realized gains and losses	\$555	\$783

## 5. Loans Receivable and the Allowance for Loan Losses

The composition of allowance for loan losses, loans, and loan pool participations by portfolio segment are as follows:

## Allowance for Loan Losses and Recorded Investment in Loan Receivables

As of March 31, 2015 and December 31, 2014

(in thousands)	Agricultural land Industrial	Commercial Real Estate	Commercial Real Estate	Residential Real Estate	Consumer	Unallocated	Total
March 31, 2015							
Allowance for loan losses:							
Individually evaluated for impairment	\$78	\$261	\$185	\$323	\$1	\$—	\$848
Collectively evaluated for impairment	1,534	5,257	5,571	2,760	284	272	15,678
Total	\$1,612	\$5,518	\$5,756	\$3,083	\$285	\$272	\$16,526
Loans acquired with deteriorated credit quality (loan pool participations)	\$—	\$62	\$637	\$77	\$2	\$1,356	\$2,134
Loans receivable							
Individually evaluated for impairment	\$2,901	\$2,850	\$3,941	\$2,692	\$31	\$—	\$12,415
Collectively evaluated for impairment	108,058	319,271	439,508	272,374	24,701	—	1,163,912
Total	\$110,959	\$322,121	\$443,449	\$275,066	\$24,732	\$—	\$1,176,327
Loans acquired with deteriorated credit quality (loan pool participations)	\$3	\$806	\$13,397	\$3,131	\$4	\$3,023	\$20,364



Table of Contents

(in thousands)	Agricultural	Commercial and Industrial	Commercial Real Estate	Residential Real Estate	Consumer	Unallocated	Total
December 31, 2014							
Allowance for loan losses:							
Individually evaluated for impairment	\$ 88	\$ 206	\$ 226	\$ 623	\$ 2	\$ —	\$ 1,145
Collectively evaluated for impairment	1,418	5,574	4,173	2,544	321	1,188	15,218
Total	\$ 1,506	\$ 5,780	\$ 4,399	\$ 3,167	\$ 323	\$ 1,188	\$ 16,363
Loans acquired with deteriorated credit quality (loan pool participations)	\$ —	\$ 70	\$ 669	\$ 82	\$ 9	\$ 1,304	\$ 2,134
Loans receivable							
Individually evaluated for impairment	\$ 3,027	\$ 3,168	\$ 3,916	\$ 3,341	\$ 34	\$ —	\$ 13,486
Collectively evaluated for impairment	101,782	301,732	422,605	269,270	23,644	—	1,119,033
Total	\$ 104,809	\$ 304,900	\$ 426,521	\$ 272,611	\$ 23,678	\$ —	\$ 1,132,519
Loans acquired with deteriorated credit quality (loan pool participations)	\$ 4	\$ 935	\$ 14,246	\$ 3,340	\$ 12	\$ 2,929	\$ 21,466

Loans with unpaid principal in the amount of \$401.7 million and \$404.4 million at March 31, 2015 and December 31, 2014, respectively, were pledged to the FHLB as collateral for borrowings.

The changes in the allowance for loan losses by portfolio segment are as follows:

(in thousands)	Allowance for Loan Loss Activity						
	For the Three Months Ended March 31, 2015 and 2014						
	Agricultural	Commercial and Industrial	Commercial Real Estate	Residential Real Estate	Consumer	Unallocated	Total
2015							
Beginning balance	\$ 1,506	\$ 5,780	\$ 4,399	\$ 3,167	\$ 323	\$ 1,188	\$ 16,363
Charge-offs	—	(247 )	—	(510 )	(33 )	—	(790 )
Recoveries	—	339	—	4	10	—	353
Provision	106	(354 )	1,357	422	(15 )	(916 )	600
Ending balance	\$ 1,612	\$ 5,518	\$ 5,756	\$ 3,083	\$ 285	\$ 272	\$ 16,526
2014							
Beginning balance	\$ 1,358	\$ 4,980	\$ 5,294	\$ 3,185	\$ 275	\$ 1,087	\$ 16,179
Charge-offs	—	(170 )	(73 )	(62 )	(23 )	—	(328 )
Recoveries	5	113	—	3	3	—	124
Provision	(329 )	481	(731 )	(137 )	39	1,127	450
Ending balance	\$ 1,034	\$ 5,404	\$ 4,490	\$ 2,989	\$ 294	\$ 2,214	\$ 16,425

**Loan Portfolio Segment Risk Characteristics**

**Agricultural** - Agricultural loans, most of which are secured by crops, livestock, and machinery, are provided to finance capital improvements and farm operations as well as acquisitions of livestock and machinery. The ability of the borrower to repay may be affected by many factors outside of the borrower's control including adverse weather

conditions, loss of livestock due to disease or other factors, declines in market prices for agricultural products and the impact of government regulations. The ultimate repayment of agricultural loans is dependent upon the profitable operation or management of the agricultural entity. 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. The collateral securing these loans may depreciate over time, may be difficult to appraise and may fluctuate in value based on the success of the business.

Commercial and Industrial - Commercial and industrial loans are primarily made based on the reported cash flow of the borrower and secondarily on the underlying collateral provided by the borrower. The collateral support provided by the borrower for most of these loans and the probability of repayment are based on the liquidation of the pledged collateral and enforcement of a personal guarantee, if any exists. The primary repayment risks of commercial and industrial loans are that the cash flows of the borrower may be unpredictable, and the collateral securing these loans may fluctuate in value. The size of the loans the Company can offer to commercial customers is less than the size of the loans that competitors with larger lending limits can offer. This may limit the Company's ability to establish relationships with the largest businesses in the areas in which the Company operates. As a result, the Company may assume greater lending risks than financial institutions that have a lesser concentration of such loans and tend to make loans to larger businesses. Collateral for these loans generally includes accounts receivable, inventory, equipment and real estate. However,



## Table of Contents

depending on the overall financial condition of the borrower, some loans are made on an unsecured basis. The collateral securing these loans may depreciate over time, may be difficult to appraise and may fluctuate in value based on the success of the business. In addition, if the U.S. economy does not continue to improve, this could harm or continue to harm the businesses of the Company's commercial and industrial customers and reduce the value of the collateral securing these loans.

**Commercial Real Estate** - The Company offers mortgage loans to commercial and agricultural customers for the acquisition of real estate used in their businesses, such as offices, warehouses and production facilities, and to real estate investors for the acquisition of apartment buildings, retail centers, office buildings and other commercial buildings. The market value of real estate securing commercial real estate 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 the Company's markets could increase the credit risk associated with its loan portfolio. Additionally, real estate lending typically involves higher loan principal amounts than other loans, 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 Company's control or that of the borrower could negatively impact the future cash flow and market values of the affected properties.

**Residential Real Estate** - The Company generally retains short-term residential mortgage loans that are originated for its own portfolio but sells most long-term loans to other parties while retaining servicing rights on the majority of those loans. The market value of real estate securing residential real estate loans can fluctuate 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 the Company's markets could increase the credit risk associated with its loan portfolio. Additionally, real estate lending typically involves higher loan principal amounts than other loans, and the repayment of the loans generally is dependent, in large part, on the borrower's continuing financial stability, and is therefore more likely to be affected by adverse personal circumstances.

**Consumer** - Consumer loans typically have shorter terms, lower balances, higher yields and higher risks of default than real estate-related loans. Consumer loan collections are dependent on the borrower's continuing financial stability, and are therefore more likely to be affected by adverse personal circumstances. Collateral for these loans generally includes automobiles, boats, recreational vehicles, mobile homes, and real estate. However, depending on the overall financial condition of the borrower, some loans are made on an unsecured basis. The collateral securing these loans may depreciate over time, may be difficult to recover and may fluctuate in value based on condition. In addition, a decline in the United States economy could result in reduced employment, impacting the ability of customers to repay their obligations.

**Loans acquired with deteriorated credit quality (loan pool participations)** - The underlying loans in the loan pool participations include both fixed-rate and variable-rate instruments. No amounts for interest due are reflected in the carrying value of the loan pool participations. Based on historical experience, the average period of collectibility for loans underlying loan pool participations, many of which have exceeded contractual maturity dates, is approximately three to five years. Loan pool balances are affected by the payment and refinancing activities of the borrowers resulting in pay-offs of the underlying loans and reduction in the balances. Collections from the individual borrowers are managed by the loan pool servicer and are affected by the borrower's financial ability and willingness to pay, foreclosure and legal action, collateral value, and the economy in general.

### **Charge-off Policy**

The Company requires a loan to be charged-off as soon as it becomes apparent that some loss will be incurred, or when its collectability is sufficiently questionable that it no longer is considered a bankable asset. The primary considerations when determining if and how much of a loan should be charged-off are as follows: (1) the potential for future cash flows; (2) the value of any collateral; and (3) the strength of any co-makers or guarantors.

When it is determined that a loan requires a partial or full charge-off, a request for approval of a charge-off is submitted to the Bank's President, Executive Vice President and Chief Credit Officer, and the Senior Regional Loan officer. The Bank's board of directors formally approves all loan charge-offs. Once a loan is charged-off, it cannot be restructured and returned to the Bank's books.

**The Allowance for Loan and Lease Losses - Bank Loans**

The Company requires the maintenance of an adequate allowance for loan and lease losses ("ALLL") in order to cover estimated probable losses without eroding the Company's capital base. Calculations are done at each quarter end, or more frequently if warranted, to analyze the collectability of loans and to ensure the adequacy of the allowance. In line with Federal Deposit Insurance Corporation (the "FDIC") directives, the ALLL calculation does not include consideration of

Table of Contents

loans held for sale or off-balance-sheet credit exposures (such as unfunded letters of credit). Determining the appropriate level for the ALLL relies on the informed judgment of management, and as such, is subject to inaccuracy. Given the inherently imprecise nature of calculating the necessary ALLL, the Company's policy permits an "unallocated" allowance between 15% above and 5% below the "indicated reserve." These unallocated amounts are due to those overall factors impacting the ALLL that are not captured in detailed loan category calculations.

**Loans Reviewed Individually for Impairment**

The Company identifies loans to be reviewed and evaluated individually for impairment based on current information and events and the probability that the borrower will be unable to repay all amounts due according to the contractual terms of the loan agreement. Specific areas of consideration include: size of credit exposure, risk rating, delinquency, nonaccrual status, and loan classification.

The level of individual impairment is measured using one of the following methods: (1) the fair value of the collateral less costs to sell; (2) the present value of expected future cash flows, discounted at the loan's effective interest rate; or (3) the loan's observable market price. Loans that are deemed fully collateralized or have been charged down to a level corresponding with any of the three measurements require no assignment of reserves from the ALLL.

All loans deemed troubled debt restructure or "TDR" are considered impaired. A loan is considered a TDR when the Bank, for economic or legal reasons related to a borrower's financial difficulties, grants a concession to the borrower that the Bank would not otherwise consider. The following factors are potential indicators that the Bank has granted a concession (one or multiple items may be present):

- The borrower receives a reduction of the stated interest rate for the remaining original life of the debt.
- The borrower receives an extension of the maturity date or dates at a stated interest rate lower than the current market interest rate for new debt with similar risk characteristics.
- The borrower receives a reduction of the face amount or maturity amount of the debt as stated in the instrument or other agreement.
- The borrower receives a deferral of required payments (principal and/or interest).
- The borrower receives a reduction of the accrued interest.

The following table sets forth information on the Company's TDRs<sup>(1)</sup> by class of financing receivable occurring during the stated periods:

	Three Months Ended March 31, 2015			2014		
	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
(dollars in thousands)						
Total	—	\$ —	\$ —	—	\$ —	\$ —

(1) TDRs may include multiple concessions and the disclosure classifications are based on the primary concession provided to the borrower.

Loans by class of financing receivable modified as TDRs<sup>(1)</sup> within the previous 12 months and for which there was a payment default during the stated periods were:

Three Months Ended March 31,			
2015		2014	
Number of Investment	Recorded of	Number of Investment	Recorded of

(dollars in thousands)

Total

Contracts

— \$ —

Contracts

— \$ —

(1) TDRs may include multiple concessions and the disclosure classifications are based on the primary concession provided to the borrower.

**Loans Reviewed Collectively for Impairment**

All loans not evaluated individually for impairment are grouped together by type (i.e. commercial, agricultural, consumer, etc.) and further segmented within each subset by risk classification (i.e. pass, special mention, and substandard). Homogeneous loans past due 60-89 days and 90 days and over are classified special mention and substandard, respectively, for allocation purposes.

## Table of Contents

The Company's historical loss experience for each loan type is calculated using the fiscal quarter-end data for the most recent 20 quarters as a starting point for estimating losses. In addition, other prevailing qualitative or environmental factors likely to cause probable losses to vary from historical data are incorporated in the form of adjustments to increase or decrease the loss rate applied to each group. These adjustments are documented and fully explain how the current information, events, circumstances, and conditions impact the historical loss measurement assumptions.

Although not a comprehensive list, the following are considered key factors and are evaluated with each calculation of the ALLL to determine if adjustments to historical loss rates are warranted:

- Changes in lending policies and procedures, including changes in underwriting standards and collection, charge-off, and recovery practices not considered elsewhere in estimating credit losses.
- Changes in international, national, regional, and local economic and business conditions and developments that affect the collectability of the portfolio, including the condition of various market segments.
- Changes in the nature and volume of the portfolio and in the terms of loans.
- Changes in the experience, ability and depth of lending management and other relevant staff.
- Changes in the volume and severity of past due loans, the volume of nonaccrual loans, and the volume and severity of adversely classified or graded loans.
- Changes in the quality of our loan review system.
- Changes in the value of underlying collateral for collateral-dependent loans.
- The existence and effect of any concentrations of credit, and changes in the level of such concentrations.
- The effect of other external factors, such as competition and legal and regulatory requirements, on the level of estimated credit losses in the Bank's existing portfolio.

The items listed above are used to determine the pass percentage for loans evaluated collectively and, as such, are applied to the loans risk rated pass. Due to the inherent risks associated with special mention risk rated loans (i.e. early stages of financial deterioration, technical exceptions, etc.), this subset is reserved at two times the pass allocation factor to reflect this increased risk exposure. In addition, non-impaired loans classified as substandard loans carry greater risk than special mention loans, and as such, this subset is reserved at six times the pass allocation. Further, non-impaired loans less than \$0.2 million that are past due 60 - 89 days or 90 days and over, are respectively classified as special mention or substandard. They are given an increased loan loss allocation of 25% or 50%, respectively, above the five-year historical loss rate of the specific loan type.

### The Allowance for Loan and Lease Losses - Loan Pool Participations

The Company requires the maintenance of an adequate allowance for loan pool participation losses in order to cover estimated probable losses. Currently, charge-offs are netted against the income the Company receives, so the balance in the loan pool reserve is not affected and remains stable. In essence, a provision for loan losses is made that is equal to the quarterly charge-offs, which is deducted from income received from the loan pools. By maintaining a sufficient reserve to cover the next quarter's charge-offs, the Company will have sufficient reserves in place should no income be collected from the loan pools during the quarter. In the event the estimated charge-offs provided by the servicer are greater than the loan pool ALLL, an additional provision is made to cover the difference between the current ALLL and the estimated charge-offs provided by the servicer.

### Loans Reviewed Individually for Impairment

The loan servicer reviews the portfolio quarterly on a loan-by-loan basis, and loans that are deemed to be impaired are charged-down to their estimated value during the next calendar quarter. All loans that are to be charged-down are reserved against in the ALLL adequacy calculation. Loans that continue to have an investment basis and that have been charged-down are monitored, and, if additional impairment is noted, the reserve requirement is increased on the individual loan.

### Loans Reviewed Collectively for Impairment

The Company utilizes the annualized average of portfolio loan (not loan pool participation) historical loss per risk category over a two year period of time. Supporting documentation for the technique used to develop the historical

loss rate for each group of loans is required to be maintained. It is management's assessment that the two year rate is most reflective of the estimated credit losses in the current loan pool portfolio.

Table of Contents

The following table sets forth the composition of each class of the Company's loans by internally assigned credit quality indicators at March 31, 2015 and December 31, 2014:

	Pass	Special Mention/ Watch	Substandard	Doubtful	Loss	Total
(in thousands)						
March 31, 2015						
Agricultural	\$102,694	\$6,732	\$1,533	\$—	\$—	\$110,959
Commercial and industrial	295,655	5,627	19,245	—	—	320,527
Credit cards	1,309	8	—	—	—	1,317
Overdrafts	264	169	88	—	—	521
Commercial real estate:						
Construction and development	66,811	945	1,499	—	—	69,255
Farmland	82,767	1,716	2,232	—	—	86,715
Multifamily	54,050	177	—	—	—	54,227
Commercial real estate-other	213,778	11,405	8,069	—	—	233,252
Total commercial real estate	417,406	14,243	11,800	—	—	443,449
Residential real estate:						
One- to four- family first liens	214,703	3,649	3,474	—	—	221,826
One- to four- family junior liens	53,030	—	210	—	—	53,240
Total residential real estate	267,733	3,649	3,684	—	—	275,066
Consumer	24,438	16	34	—	—	24,488
Total	\$1,109,499	\$30,444	\$36,384	\$—	\$—	\$1,176,327
Loans acquired with deteriorated credit quality (loan pool participations)	\$9,446	\$—	\$10,917	\$—	\$1	\$20,364
	Pass	Special Mention/ Watch	Substandard	Doubtful	Loss	Total
(in thousands)						
December 31, 2014						
Agricultural	\$98,096	\$5,032	\$1,681	\$—	\$—	\$104,809
Commercial and industrial	273,290	7,468	22,350	—	—	303,108
Credit cards	1,240	6	—	—	—	1,246
Overdrafts	373	262	109	—	—	744
Commercial real estate:						
Construction and development	56,963	1,151	1,269	—	—	59,383
Farmland	79,629	1,778	2,293	—	—	83,700
Multifamily	54,708	178	—	—	—	54,886
Commercial real estate-other	215,268	11,216	2,068	—	—	228,552
Total commercial real estate	406,568	14,323	5,630	—	—	426,521
Residential real estate:						
One- to four- family first liens	211,390	3,933	3,991	—	—	219,314
One- to four- family junior liens	53,039	48	210	—	—	53,297
Total residential real estate	264,429	3,981	4,201	—	—	272,611
Consumer	23,431	8	41	—	—	23,480
Total	\$1,067,427	\$31,080	\$34,012	\$—	\$—	\$1,132,519

Loans acquired with deteriorated credit quality (loan \$10,256 pool participations)	\$—	\$11,202	\$—	\$8	\$21,466
-------------------------------------------------------------------------------------------	-----	----------	-----	-----	----------

Special Mention/Watch - A special mention/watch asset has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in the Company's credit position at some future date. Special mention/watch assets are not adversely classified and do not expose the Company to sufficient risk to warrant adverse classification.

Substandard - Substandard loans are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected.



Table of Contents

Doubtful - Loans classified doubtful have all the weaknesses inherent in those classified substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently known facts, conditions and values, highly questionable and improbable.

Loss - Loans classified loss are considered uncollectible and of such little value that their continuance as bankable assets is not warranted. This classification does not mean that the loan has absolutely no recovery or salvage value but rather it is not practical or desirable to defer writing off this basically worthless asset even though partial recovery may be effected in the future.

Table of Contents

The following table sets forth the amounts and categories of the Company's impaired loans as of March 31, 2015 and December 31, 2014:

	March 31, 2015			December 31, 2014		
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Recorded Investment	Unpaid Principal Balance	Related Allowance
(in thousands)						
With no related allowance recorded:						
Agricultural	\$1,340	\$1,840	\$—	\$1,410	\$1,910	\$—
Commercial and industrial	1,865	1,865	—	2,169	2,270	—
Credit cards	—	—	—	—	—	—
Overdrafts	—	—	—	—	—	—
Commercial real estate:						
Construction and development	49	176	—	49	176	—
Farmland	2,211	2,374	—	2,270	2,433	—
Multifamily	—	—	—	—	—	—
Commercial real estate-other	1,030	1,155	—	939	1,064	—
Total commercial real estate	3,290	3,705	—	3,258	3,673	—
Residential real estate:						
One- to four- family first liens	1,421	1,997	—	535	773	—
One- to four- family junior liens	134	157	—	134	157	—
Total residential real estate	1,555	2,154	—	669	930	—
Consumer	22	38	—	6	22	—
Total	\$8,072	\$9,602	\$—	\$7,512	\$8,805	\$—
With an allowance recorded:						
Agricultural	\$1,561	\$1,561	\$78	\$1,617	\$1,617	\$88
Commercial and industrial	985	1,015	261	999	999	206
Credit cards	—	—	—	—	—	—
Overdrafts	—	—	—	—	—	—
Commercial real estate:						
Construction and development	34	34	34	34	34	34
Farmland	69	69	3	74	74	4
Multifamily	—	—	—	—	—	—
Commercial real estate-other	548	548	148	550	550	188
Total commercial real estate	651	651	185	658	658	226
Residential real estate:						
One- to four- family first liens	1,066	1,066	294	2,600	2,600	594
One- to four- family junior liens	71	71	29	72	72	29
Total residential real estate	1,137	1,137	323	2,672	2,672	623
Consumer	9	9	1	28	28	2
Total	\$4,343	\$4,373	\$848	\$5,974	\$5,974	\$1,145
Total:						
Agricultural	\$2,901	\$3,401	\$78	\$3,027	\$3,527	\$88
Commercial and industrial	2,850	2,880	261	3,168	3,269	206
Credit cards	—	—	—	—	—	—
Overdrafts	—	—	—	—	—	—
Commercial real estate:						
Construction and development	83	210	34	83	210	34

Edgar Filing: MidWestOne Financial Group, Inc. - Form 10-Q

Farmland	2,280	2,443	3	2,344	2,507	4
Multifamily	—	—	—	—	—	—
Commercial real estate-other	1,578	1,703	148	1,489	1,614	188
Total commercial real estate	3,941	4,356	185	3,916	4,331	226
Residential real estate:						
One- to four- family first liens	2,487	3,063	294	3,135	3,373	594
One- to four- family junior liens	205	228	29	206	229	29
Total residential real estate	2,692	3,291	323	3,341	3,602	623
Consumer	31	47	1	34	50	2
Total	\$12,415	\$13,975	\$848	\$13,486	\$14,779	\$1,145

18

---

Table of Contents

The following table sets forth the average recorded investment and interest income recognized for each category of the Company's impaired loans during the stated periods:

	Three Months Ended March 31,			
	2015		2014	
	Average Recorded Investment	Interest Recognized	Average Recorded Investment	Interest Recognized
(in thousands)				
With no related allowance recorded:				
Agricultural	\$1,375	\$ 14	\$1,416	\$ 14
Commercial and industrial	1,872	29	1,874	20
Credit cards	—	—	—	—
Overdrafts	—	—	—	—
Commercial real estate:				
Construction and development	49	—	90	1
Farmland	2,241	27	91	2
Multifamily	—	—	—	—
Commercial real estate-other	1,036	—	551	(7 )
Total commercial real estate	3,326	27	732	(4 )
Residential real estate:				
One- to four- family first liens	1,417	—	645	4
One- to four- family junior liens	134	—	85	—
Total residential real estate	1,551	—	730	4
Consumer	23	—	9	—
Total	\$8,147	\$ 70	\$4,761	\$ 34
With an allowance recorded:				
Agricultural	\$1,589	\$ 12	\$1,738	\$ 12
Commercial and industrial	1,022	9	1,910	17
Credit cards	—	—	—	—
Overdrafts	—	—	—	—
Commercial real estate:				
Construction and development	34	—	—	—
Farmland	72	1	2,440	26
Multifamily	—	—	—	—
Commercial real estate-other	549	4	1,852	8
Total commercial real estate	655	5	4,292	34
Residential real estate:				
One- to four- family first liens	1,068	9	1,005	1
One- to four- family junior liens	72	—	89	—
Total residential real estate	1,140	9	1,094	1
Consumer	10	—	20	1
Total	\$4,416	\$ 35	\$9,054	\$ 65
Total:				
Agricultural	\$2,964	\$ 26	\$3,154	\$ 26
Commercial and industrial	2,894	38	3,784	37
Credit cards	—	—	—	—
Overdrafts	—	—	—	—
Commercial real estate:				
Construction and development	83	—	90	1

Edgar Filing: MidWestOne Financial Group, Inc. - Form 10-Q

Farmland	2,313	28	2,531	28
Multifamily	—	—	—	—
Commercial real estate-other	1,585	4	2,403	1
Total commercial real estate	3,981	32	5,024	30
Residential real estate:				
One- to four- family first liens	2,485	9	1,650	5
One- to four- family junior liens	206	—	174	—
Total residential real estate	2,691	9	1,824	5
Consumer	33	—	29	1
Total	\$12,563	\$ 105	\$13,815	\$ 99

Table of Contents

The following table sets forth the composition and past due status of the Company's loans at March 31, 2015 and December 31, 2014:

	30 - 59 Days Past Due	60 - 89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans Receivable	Recorded Investment > 90 Days Past Due and Accruing
(in thousands)							
March 31, 2015							
Agricultural	\$285	\$—	\$—	\$285	\$110,674	\$110,959	\$—
Commercial and industrial	1,091	77	408	1,576	318,951	320,527	—
Credit cards	3	5	—	8	1,309	1,317	—
Overdrafts	85	—	4	89	432	521	—
Commercial real estate:							
Construction and development	—	—	83	83	69,172	69,255	—
Farmland	123	—	—	123	86,592	86,715	—
Multifamily	—	—	—	—	54,227	54,227	—
Commercial real estate-other	—	76	2,214	2,290	230,962	233,252	924
Total commercial real estate	123	76	2,297	2,496	440,953	443,449	924
Residential real estate:							
One- to four- family first liens	1,831	137	1,541	3,509	218,317	221,826	111
One- to four- family junior liens	351	—	192	543	52,697	53,240	—
Total residential real estate	2,182	137	1,733	4,052	271,014	275,066	111
Consumer	82	16	16	114	24,374	24,488	2
Total	\$3,851	\$311	\$4,458	\$8,620	\$1,167,707	\$1,176,327	\$1,037
December 31, 2014							
Agricultural	\$58	\$30	\$—	\$88	\$104,721	\$104,809	\$—
Commercial and industrial	897	603	515	2,015	301,093	303,108	66
Credit cards	3	3	—	6	1,240	1,246	—
Overdrafts	104	2	4	110	634	744	—
Commercial real estate:							
Construction and development	—	—	83	83	59,300	59,383	—
Farmland	503	—	—	503	83,197	83,700	—
Multifamily	—	—	—	—	54,886	54,886	—
Commercial real estate-other	168	57	1,200	1,425	227,127	228,552	—
Total commercial real estate	671	57	1,283	2,011	424,510	426,521	—
Residential real estate:							
One- to four- family first liens	1,481	581	2,023	4,085	215,229	219,314	780
One- to four- family junior liens	105	48	192	345	52,952	53,297	—
Total residential real estate	1,586	629	2,215	4,430	268,181	272,611	780

Edgar Filing: MidWestOne Financial Group, Inc. - Form 10-Q

Consumer	35	8	23	66	23,414	23,480	2
Total	\$3,354	\$1,332	\$4,040	\$8,726	\$1,123,793	\$1,132,519	\$848

Non-accrual and Delinquent Loans

Loans are placed on non-accrual when (1) payment in full of principal and interest is no longer expected or (2) principal or interest has been in default for 90 days or more (unless the loan is both well secured with marketable collateral and in the process of collection). All loans rated doubtful or worse, and certain loans rated substandard, are placed on non-accrual.

A non-accrual asset may be restored to an accrual status when (1) all past due principal and interest has been paid (excluding renewals and modifications that involve the capitalizing of interest) or (2) the loan becomes well secured with marketable collateral and is in the process of collection. An established track record of performance is also considered when determining accrual status.

Delinquency status of a loan is determined by the number of days that have elapsed past the loan's payment due date, using the following classification groupings: 30-59 days, 60-89 days and 90 days or more. Loans shown in the 30-59 days and 60-89 days columns in the table above reflect contractual delinquency status of loans not considered nonperforming due to classification as a TDR or being placed on non-accrual.

Table of Contents

The following table sets forth the composition of the Company's recorded investment in loans on nonaccrual status as of March 31, 2015 and December 31, 2014:

	March 31, 2015	December 31, 2014
(in thousands)		
Agricultural	\$—	\$—
Commercial and industrial	430	479
Credit cards	—	—
Overdrafts	—	—
Commercial real estate:		
Construction and development	83	83
Farmland	23	24
Multifamily	—	—
Commercial real estate-other	1,291	1,200
Total commercial real estate	1,397	1,307
Residential real estate:		
One- to four- family first liens	1,430	1,261
One- to four- family junior liens	192	192
Total residential real estate	1,622	1,453
Consumer	14	16
Total	\$3,463	\$3,255

As of March 31, 2015, the Company had no commitments to lend additional funds to any borrowers who have had a TDR.

**Loan Pool Participations**

ASC Topic 310 addresses accounting for differences between contractual cash flows and cash flows expected to be collected from an investor's initial investment in loans or debt securities acquired in a transfer if those differences are attributable, at least in part, to credit quality. The loans underlying the loan pool participations were evaluated individually when purchased for application of ASC Topic 310, utilizing various criteria including: past-due status, late payments, legal status of the loan (not in foreclosure, judgment against the borrower, or referred to legal counsel), frequency of payments made, collateral adequacy and the borrower's financial condition. If all the criteria were met, the individual loan utilized the accounting treatment required by ASC Topic 310 with the accretible yield difference between the expected cash flows and the purchased basis accreted into income on the level yield basis over the anticipated life of the loan. If any of the six criteria were not met at the time of purchase, the loan was accounted for on the cash basis of accounting.

The loan servicer reviews the portfolio quarterly on a loan-by-loan basis, and loans that are deemed to be impaired are charged down to their estimated value. As of March 31, 2015, approximately 71% of the loans were contractually current or less than 90 days past due, while 29% were contractually past due 90 days or more. Many of the loans were acquired in a contractually past due status, which was reflected in the discounted purchase price of the loans. Performance status is monitored on a monthly basis. The 29% of loans contractually past due includes loans in litigation and foreclosed property.

**6. Income Taxes**

Federal income tax expense for the three months ended March 31, 2015 and 2014 was computed using the consolidated effective federal tax rate. The Company also recognized income tax expense pertaining to state franchise taxes payable by the subsidiary bank.

**7. Fair Value Measurements**



Fair value is the price that would be received in selling an asset or paid in transferring a liability in an orderly transaction between market participants. A fair value measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. The price in the principal (or most advantageous) market used to measure the fair value of the asset or liability is not adjusted for transaction costs. An orderly transaction is a transaction that assumes exposure to the market for a period prior to the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets and liabilities; it is not a forced transaction. Market participants are buyers and sellers in the principal market that are (i) independent, (ii) knowledgeable, (iii) able to transact and (iv) willing to transact.

Table of Contents

GAAP requires the use of valuation techniques that are consistent with the market approach, the income approach and/or the cost approach. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets and liabilities. The income approach uses valuation techniques to convert future amounts, such as cash flows or earnings, to a single present amount on a discounted basis. The cost approach is based on the amount that currently would be required to replace the service capacity of an asset (replacement cost). Valuation techniques should be consistently applied. Inputs to valuation techniques refer to the assumptions that market participants would use in pricing the asset or liability. Inputs may be observable, meaning those that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from independent sources, or unobservable, meaning those that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. In that regard, GAAP establishes a fair value hierarchy for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy is as follows:

Level 1 Inputs – Unadjusted quoted prices for identical assets or liabilities in active markets that the reporting entity has the ability to access at the measurement date.

Level 2 Inputs – Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These might include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset (such as interest rates, volatilities, prepayment speeds, credit risks, etc.) or inputs that are derived principally from or corroborated by market data by correlation or other means.

Level 3 Inputs – Unobservable inputs for determining the fair values of assets or liabilities that reflect an entity's own assumptions about the assumptions that market participants would use in pricing the assets or liabilities.

It is the Company's policy to maximize the use of observable inputs and minimize the use of unobservable inputs when developing fair value measurements. The Company is required to use observable inputs, to the extent available, in the fair value estimation process unless that data results from forced liquidations or distressed sales. A description of the valuation methodologies used for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below.

Valuation methods for instruments measured at fair value on a recurring basis.

Securities Available for Sale - The Company's investment securities classified as available for sale include: debt securities issued by the U.S. Treasury and other U.S. Government agencies and corporations, debt securities issued by state and political subdivisions, mortgage-backed securities, collateralized mortgage obligations, corporate debt securities, and equity securities. Quoted exchange prices are available for equity securities, which are classified as Level 1. The Company utilizes an independent pricing service to obtain the fair value of debt securities. On a quarterly basis, the Company selects a sample of 30 securities from its primary pricing service and compares them to a secondary independent pricing service to validate value. In addition, the Company periodically reviews the pricing methodology utilized by the primary independent service for reasonableness. Debt securities issued by the U.S. Treasury and other U.S. Government agencies and corporations and mortgage-backed obligations are priced utilizing industry-standard models that consider various assumptions, including time value, yield curves, volatility factors, prepayment speeds, default rates, loss severity, current market and contractual prices for the underlying financial instruments, as well as other relevant economic measures. Substantially all of these assumptions are observable in the marketplace, can be derived from observable data, or are supported by observable levels at which transactions are executed in the marketplace and are classified as Level 2. Municipal securities are valued using a type of matrix, or grid, pricing in which securities are benchmarked against the treasury rate based on credit rating. These model and matrix measurements are classified as Level 2 in the fair value hierarchy. On an annual basis, a group of selected municipal securities are priced by a securities dealer and that price is used to verify the primary independent service's valuation.

Mortgage Servicing Rights - The Company recognizes the rights to service mortgage loans for others on residential real estate loans internally originated and then sold. Mortgage servicing rights are recorded at fair value based on

assumptions through a third-party valuation service. The valuation model incorporates assumptions that market participants would use in estimating future net servicing income, such as the servicing cost per loan, the discount rate, the escrow float rate, an inflation rate, ancillary income, prepayment speeds and default rates and losses. Because many of these inputs are unobservable, the valuations are classified as Level 3.

Table of Contents

The following table summarizes assets measured at fair value on a recurring basis as of March 31, 2015 and December 31, 2014. There were no liabilities subject to fair value measurement as of these dates. The assets are segregated by the level of valuation inputs within the fair value hierarchy utilized to measure fair value:

Fair Value Measurement at March 31, 2015 Using				
(in thousands)	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Available for sale debt securities:				
U.S. Government agencies and corporations	\$26,967	\$ —	\$26,967	\$ —
State and political subdivisions	191,422	—	191,422	—
Mortgage-backed securities	30,493	—	30,493	—
Collateralized mortgage obligations	115,060	—	115,060	—
Corporate debt securities	43,741	—	43,741	—
Total available for sale debt securities	407,683	—	407,683	—
Available for sale equity securities:				
Other equity securities	1,267	1,267	—	—
Total available for sale equity securities	1,267	1,267	—	—
Total securities available for sale	\$408,950	\$ 1,267	\$407,683	\$ —
Mortgage servicing rights	\$2,181	\$ —	\$ —	\$ 2,181
Fair Value Measurement at December 31, 2014 Using				
(in thousands)	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Available for sale debt securities:				
U.S. Government agencies and corporations	\$49,375	\$ —	\$ 49,375	\$ —
State and political subdivisions	195,199	—	195,199	—
Mortgage-backed securities	32,463	—	32,463	—
Collateralized mortgage obligations	146,132	—	146,132	—
Corporate debt securities	48,741	—	48,741	—
Total available for sale debt securities	471,910	—	471,910	—
Available for sale equity securities:				
Other equity securities	3,032	3,032	—	—
Total available for sale equity securities	3,032	3,032	—	—
Total securities available for sale	\$474,942	\$ 3,032	\$ 471,910	\$ —
Mortgage servicing rights	\$2,308	\$ —	\$ —	\$ 2,308

There were no transfers of assets between levels of the fair value hierarchy during the three months ended March 31, 2015 or the year ended December 31, 2014.

There have been no changes in valuation techniques used for any assets measured at fair value during the three months ended March 31, 2015 or the year ended December 31, 2014.



Table of Contents

The following table presents additional information about assets measured at fair market value on a recurring basis for which the Company has utilized Level 3 inputs to determine fair value for the three months ended March 31, 2015 and 2014:

	For the Three Months Ended March 31,			
	2015		2014	
	Collateralized Debt Obligations	Mortgage Servicing Rights	Collateralized Debt Obligations	Mortgage Servicing Rights
(in thousands)				
Beginning balance	\$—	\$2,308	\$1,317	\$2,298
Transfers into Level 3	—	—	—	—
Transfers out of Level 3	—	—	—	—
Total gains (losses):				
Included in earnings	—	(172 )	782	51
Included in other comprehensive income	—	—	794	—
Purchases, issuances, sales, and settlements:				
Purchases	—	—	—	—
Issuances	—	45	—	40
Sales	—	—	(2,893 )	—
Settlements	—	—	—	—
Ending balance	\$—	\$2,181	\$—	\$2,389

The following table presents the amount of gains and losses on Level 3 assets noted above which were included in earnings and other comprehensive income for the three months ended March 31, 2015 and 2014 that are attributable to the change in unrealized gains and losses relating to those assets still held, and the line item in the consolidated financial statements in which they are included:

	For the Three Months Ended March 31,			
	2015		2014	
	Collateralized Debt Obligations	Mortgage Servicing Rights	Collateralized Debt Obligations	Mortgage Servicing Rights
(in thousands)				
Total gains (losses) for the period in earnings*	\$—	\$(127 )	\$782	\$91
Change in unrealized gains for the period included in other comprehensive income	—	—	794	—

\* Gains on collateralized debt obligations are included in gain on sale or call of available for sale securities, while gains on mortgage servicing rights are included in mortgage origination and loan servicing fees, both in the consolidated statements of operations.

Changes in the fair value of available for sale securities are included in other comprehensive income to the extent the changes are not considered OTTI. OTTI tests are performed on a quarterly basis and any decline in the fair value of an individual security below its cost that is deemed to be other-than-temporary results in a write-down that is reflected directly in the Company's consolidated statements of operations.

Valuation methods for instruments measured at fair value on a nonrecurring basis

Collateral Dependent Impaired Loans - From time to time, a loan is considered impaired and an allowance for credit losses is established. The specific reserves for collateral dependent impaired loans are based on the fair value of the collateral less estimated costs to sell. The fair value of collateral is determined based on appraisals. In some cases, adjustments are made to the appraised values due to various factors, including age of the appraisal, age of comparables included in the appraisal, and known changes in the market and in the collateral. Because many of these inputs are unobservable, the valuations are classified as Level 3.

Other Real Estate Owned ("OREO") - OREO represents property acquired through foreclosures and settlements of loans. Property acquired through or in lieu of foreclosure are initially recorded at fair value less estimated selling cost at the date of foreclosure, establishing a new cost basis. The Company considers third party appraisals as well as independent fair value assessments from real estate brokers or persons involved in selling OREO in determining the fair value of particular properties. Accordingly, the valuation of OREO is subject to significant external and internal judgment. The Company also periodically reviews OREO to determine whether the property continues to be carried at the lower of its

Table of Contents

recorded book value or fair value of the property, less disposal costs. Because many of these inputs are unobservable, the valuations are classified as Level 3.

The following table discloses the Company's estimated fair value amounts of its assets recorded at fair value on a nonrecurring basis. It is management's belief that the fair values presented below are reasonable based on the valuation techniques and data available to the Company as of March 31, 2015 and December 31, 2014, as more fully described above.

(in thousands)	Fair Value Measurement at March 31, 2015 Using			
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Collateral dependent impaired loans:				
Agricultural	\$—	\$—	\$—	\$—
Commercial and industrial	725	—	—	725
Commercial real estate:				
Construction and development	49	—	—	49
Farmland	48	—	—	48
Multifamily	—	—	—	—
Commercial real estate-other	1,037	—	—	1,037
Total commercial real estate	1,134	—	—	1,134
Residential real estate:				
One- to four- family first liens	1,334	—	—	1,334
One- to four- family junior liens	47	—	—	47
Total residential real estate	1,381	—	—	1,381
Consumer	8	—	—	8
Collateral dependent impaired loans	\$3,248	\$—	\$—	\$ 3,248
Other real estate owned	\$1,652	\$—	\$—	\$ 1,652
(in thousands)	Fair Value Measurement at December 31, 2014 Using			
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Collateral dependent impaired loans:				
Agricultural	\$—	\$—	\$—	\$—
Commercial and industrial	793	—	—	793
Commercial real estate:				
Construction and development	49	—	—	49
Farmland	52	—	—	52
Multifamily	—	—	—	—
Commercial real estate-other	1,012	—	—	1,012
Total commercial real estate	1,113	—	—	1,113
Residential real estate:				
One- to four- family first liens	1,427	—	—	1,427
One- to four- family junior liens	47	—	—	47
Total residential real estate	1,474	—	—	1,474



Edgar Filing: MidWestOne Financial Group, Inc. - Form 10-Q

Consumer	32	—	—	32
Collateral dependent impaired loans	\$3,412	\$ —	\$—	\$ 3,412
Other real estate owned	\$1,916	\$ —	\$—	\$ 1,916

25

---

Table of Contents

The following presents the carrying amount and estimated fair value of the financial instruments held by the Company at March 31, 2015 and December 31, 2014. The information presented is subject to change over time based on a variety of factors. The operations of the Company are managed on a going concern basis and not a liquidation basis. As a result, the ultimate value realized from the financial instruments presented could be substantially different when actually recognized over time through the normal course of operations. Additionally, a substantial portion of the Company's inherent value is the Bank's capitalization and franchise value. Neither of these components has been given consideration in the presentation of fair values below.

	March 31, 2015				
	Carrying Amount	Estimated Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
(in thousands)					
Financial assets:					
Cash and cash equivalents	\$21,456	\$ 21,456	\$21,456	\$ —	\$ —
Investment securities:					
Available for sale	408,950	408,950	1,267	407,683	—
Held to maturity	54,293	54,574	—	54,574	—
Total investment securities	463,243	463,524	1,267	462,257	—
Loans held for sale	2,281	2,297	—	—	2,297
Loans, net:					
Agricultural	109,321	108,979	—	—	108,979
Commercial and industrial	314,978	314,021	—	—	314,021
Credit cards	1,274	1,274	—	—	1,274
Overdrafts	439	439	—	—	439
Commercial real estate:					
Construction and development	68,455	68,530	—	—	68,530
Farmland	85,910	86,101	—	—	86,101
Multifamily	53,873	53,717	—	—	53,717
Commercial real estate-other	229,352	229,703	—	—	229,703
Total commercial real estate	437,590	438,051	—	—	438,051
Residential real estate:					
One- to four- family first liens	219,111	218,990	—	—	218,990
One- to four- family junior liens	52,809	53,604	—	—	53,604
Total residential real estate	271,920	272,594	—	—	272,594
Consumer	24,279	24,339	—	—	24,339
Total loans, net	1,159,801	1,159,697	—	—	1,159,697
Loan pool participations, net	18,230	18,230	—	—	18,230
Accrued interest receivable	9,358	9,358	9,358	—	—
Federal Home Loan Bank stock	8,000	8,000	—	8,000	—
Mortgage servicing rights	2,349	2,349	—	—	2,349
Financial liabilities:					
Deposits:					
Non-interest bearing demand	212,711	212,711	212,711	—	—
Interest-bearing checking	628,990	628,990	628,990	—	—

Edgar Filing: MidWestOne Financial Group, Inc. - Form 10-Q

Savings	106,380	106,380	106,380	—	—
Certificates of deposit under \$100,000	229,543	229,827	—	229,827	—
Certificates of deposit \$100,000 and over	230,629	231,621	—	231,621	—
Total deposits	1,408,253	1,409,529	948,081	461,448	—
Federal funds purchased and securities sold under agreements to repurchase	64,226	64,226	64,226	—	—
Federal Home Loan Bank borrowings	78,000	78,505	—	—	78,505
Long-term debt	15,464	10,064	—	—	10,064
Accrued interest payable	932	932	932	—	—

Table of Contents

	December 31, 2014				
	Carrying Amount	Estimated Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
(in thousands)					
Financial assets:					
Cash and cash equivalents	\$23,409	\$ 23,409	\$23,409	\$ —	\$ —
Investment securities:					
Available for sale	474,942	474,942	3,032	471,910	—
Held to maturity	51,524	51,253	—	51,253	—
Total investment securities	526,466	526,195	3,032	523,163	—
Loans held for sale	801	812	—	—	812
Loans, net:					
Agricultural	103,193	102,927	—	—	102,927
Commercial and industrial	297,048	295,886	—	—	295,886
Credit cards	1,206	1,206	—	—	1,206
Overdrafts	610	610	—	—	610
Commercial real estate:					
Construction and development	58,665	58,764	—	—	58,764
Farmland	82,888	83,285	—	—	83,285
Multifamily	54,516	54,356	—	—	54,356
Commercial real estate-other	225,605	225,899	—	—	225,899
Total commercial real estate	421,674	422,304	—	—	422,304
Residential real estate:					
One- to four- family first liens	216,338	216,326	—	—	216,326
One- to four- family junior liens	52,821	53,664	—	—	53,664
Total residential real estate	269,159	269,990	—	—	269,990
Consumer	23,266	23,362	—	—	23,362
Total loans, net	1,116,156	1,116,285	—	—	1,116,285
Loan pool participations, net	19,332	19,332	—	—	19,332
Accrued interest receivable	10,898	10,898	10,898	—	—
Federal Home Loan Bank stock	8,582	8,582	—	8,582	—
Mortgage servicing rights	2,308	2,308	—	—	2,308
Financial liabilities:					
Deposits:					
Non-interest bearing demand	214,461	214,461	214,461	—	—
Interest-bearing checking	618,540	618,540	618,540	—	—
Savings	102,527	102,527	102,527	—	—
Certificates of deposit under \$100,000	235,395	235,401	—	235,401	—
Certificates of deposit \$100,000 and over	237,619	238,480	—	238,480	—
Total deposits	1,408,542	1,409,409	935,528	473,881	—
Federal funds purchased and securities sold under agreements to repurchase	78,229	78,229	78,229	—	—
Federal Home Loan Bank borrowings	93,000	93,051	—	—	93,051

Edgar Filing: MidWestOne Financial Group, Inc. - Form 10-Q

Long-term debt	15,464	10,021	—	—	10,021
Accrued interest payable	863	863	863	—	—

• Cash and cash equivalents, federal funds purchased, securities sold under repurchase agreements, and accrued interest are instruments with carrying values that approximate fair value.

Investment securities available for sale are measured at fair value on a recurring basis. Held to maturity securities are carried at amortized cost. Fair value is based upon quoted prices, if available. If a quoted price is not available, the fair value is obtained from benchmarking the security against similar securities by using a third-party pricing service.

• Loans held for sale are carried at the lower of cost or fair value, with fair value being based on recent observable loan sales. The portfolio has historically consisted primarily of residential real estate loans.

Table of Contents

For variable-rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values. The fair values for other loans are determined using estimated future cash flows, discounted at the interest rates currently being offered for loans with similar terms to borrowers with similar credit quality. The Company does record nonrecurring fair value adjustments to loans to reflect (1) partial write-downs and allowances that are based on the observable market price or appraised value of the collateral or (2) the full charge-off of the loan carrying value.

Loan pool participation carrying values represent the discounted price paid by us to acquire our participation interests in the various loan pool participations purchased, which approximates fair value.

The fair value of FHLB stock is estimated at its carrying value and redemption price of \$100 per share.

Deposit liabilities are carried at historical cost. The fair value of demand deposits, savings accounts and certain money market account deposits is the amount payable on demand at the reporting date. The fair value of fixed maturity certificates of deposit is estimated using the rates currently offered for deposits of similar remaining maturities. If the fair value of the fixed maturity certificates of deposit is calculated at less than the carrying amount, the carrying value of these deposits is reported as the fair value.

FHLB borrowings and long-term debt are recorded at historical cost. The fair value of these items is estimated using discounted cash flow analysis, based on the Company's current incremental borrowing rates for similar types of borrowing arrangements.

The following presents the valuation technique(s), observable inputs, and quantitative information about the unobservable inputs used for fair value measurements of the financial instruments held by the Company at March 31, 2015, categorized within Level 3 of the fair value hierarchy:

Quantitative Information About Level 3 Fair Value Measurements						
(dollars in thousands)	Fair Value at March 31, 2015	Valuation Techniques(s)	Unobservable Input	Range of Inputs		Weighted Average
Collateral dependent impaired loans:						
Commercial and industrial	725	Modified appraised value	Third party appraisal	NM *	NM *	NM *
			Appraisal discount	NM *	NM *	NM *
Construction & development	49	Modified appraised value	Third party appraisal	NM *	NM *	NM *
			Appraisal discount	NM *	NM *	NM *
Farmland	48	Modified appraised value	Third party appraisal	NM *	NM *	NM *
			Appraisal discount	NM *	NM *	NM *
Commercial real estate-other	1,037	Modified appraised value	Third party appraisal	NM *	NM *	NM *
			Appraisal discount	NM *	NM *	NM *
Residential real estate one-to four-family first liens	1,334	Modified appraised value	Third party appraisal	NM *	NM *	NM *
			Appraisal discount	NM *	NM *	NM *
	47			NM *	NM *	NM *

Edgar Filing: MidWestOne Financial Group, Inc. - Form 10-Q

Residential real estate one-to four-family junior liens		Modified appraised value	Third party appraisal			
			Appraisal discount	NM *	NM *	NM *
Consumer	8	Modified appraised value	Third party appraisal	NM *	NM *	NM *
			Appraisal discount	NM *	NM *	NM *
Mortgage servicing rights	2,181	Discounted cash flows	Constant prepayment rate	9.47 %-	16.95 %	9.98 %
			Pretax discount rate	10.00 %-	13.00 %	10.16 %
Other real estate owned	1,652	Modified appraised value	Third party appraisal	NM *	NM *	NM *
			Appraisal discount	NM *	NM *	NM *

\* Not Meaningful. Third party appraisals are obtained as to the value of the underlying asset, but disclosure of this information would not provide meaningful information, as the range will vary widely from loan to loan. Types of discounts considered include age of the appraisal, local market conditions, current condition of the property, and estimated sales costs. These discounts will also vary from loan to loan, thus providing a range would not be meaningful.

Changes in assumptions or estimation methodologies may have a material effect on these estimated fair values.

Table of Contents

8. Variable Interest Entities

Loan Pool Participations

The Company has invested in certain participation certificates of loan pools which are purchased, held and serviced by a third-party independent servicing corporation. The Company's portfolio holds approximately 95% of the participation interests in the pools of loans owned and serviced by States Resources Corporation ("SRC"), a third-party loan servicing organization located in Omaha, Nebraska, in which the Company participates. SRC's owner holds the remaining interest. The Company does not have any ownership interest in or exert any control over SRC, and thus it is not included in the consolidated financial statements.

These pools of loans were purchased from large nonaffiliated banking organizations and from the FDIC acting as receiver of failed banks and savings associations. As loan pools were put out for bid (generally in a sealed bid auction), SRC's due diligence teams evaluated the loans and determined their interest in bidding on the pool. After the due diligence, the Company's management reviewed the status and decided if it wished to continue in the process. If the decision to consider a bid was made, SRC conducted additional analysis to determine the appropriate bid price. This analysis involved discounting loan cash flows with adjustments made for expected losses, changes in collateral values as well as targeted rates of return. A cost or investment basis was assigned to each individual loan on a cents-per-dollar (discounted price) basis based on SRC's assessment of the recovery potential of each loan.

Once a bid was awarded to SRC, the Company assumed the risk of profit or loss but on a non-recourse basis so the risk is limited to its initial investment. The extent of the risk is also dependent upon: the debtor or guarantor's financial condition, the possibility that a debtor or guarantor may file for bankruptcy protection, SRC's ability to locate any collateral and obtain possession, the value of such collateral, and the length of time it takes to realize the recovery either through collection procedures, legal process, or resale of the loans after a restructure.

Loan pool participations are shown on the Company's consolidated balance sheets as a separate asset category. The original carrying value or investment basis of loan pool participations is the discounted price paid by the Company to acquire its interests, which, as noted, is less than the face amount of the underlying loans. The Company's investment basis is reduced as SRC recovers principal on the loans and remits its share to the Company or as loan balances are written off as uncollectible.

9. Effect of New Financial Accounting Standards

In January 2014, the FASB issued Accounting Standards Update No. 2014-01, Investments—Equity Method and Joint Ventures (Topic 323): Accounting for Investments in Qualified Affordable Housing Projects. The objective of this update is to provide guidance on accounting for investments by a reporting entity in flow-through limited liability entities that manage or invest in affordable housing projects that qualify for the low-income housing tax credit. The low-income housing tax credit program is designed to encourage private capital investment in the construction and rehabilitation of low-income housing. This program is an indirect tax subsidy that allows investors in a flow-through limited liability entity, such as limited partnerships or limited liability companies that manage or invest in qualified affordable housing projects, to receive the benefits of the tax credits allocated to the entity that owns the qualified affordable housing project. The tax credits are allowable on the tax return each year over a 10-year period as a result of a sufficient number of units being rented to qualifying tenants and are subject to restrictions on gross rentals paid by those tenants. Those credits are subject to recapture over a 15-year period starting with the first year tax credits are earned. The amendments in this update permit reporting entities to make an accounting policy election to account for their investments in qualified affordable housing projects using the proportional amortization method if certain conditions are met. For public entities, the amendments are to be applied retrospectively to all annual periods and interim reporting periods presented within those annual periods, beginning after December 15, 2014. The adoption of this amendment did not have a material effect on the Company's consolidated financial statements.

In January 2014, the FASB issued Accounting Standards Update No. 2014-04, Receivables—Troubled Debt Restructurings by Creditors (Subtopic 310-40): Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure. The objective of this update is to reduce diversity by clarifying when an in-substance repossession or foreclosure occurs, that is, when a creditor should be considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan such that the loan



receivable should be derecognized and the real estate property recognized. For public entities, the amendments are effective for reporting periods beginning after December 31, 2014, with early adoption permitted. The adoption of this amendment did not have a material effect on the Company's consolidated financial statements.

In May 2014, the FASB issued Accounting Standards Update No. 2014-09, Revenue from Contract with Customers (Topic 606). The guidance in this update affects any entity that either enters into contracts with customers to transfer goods or

Table of Contents

services or enters into contracts for the transfer of nonfinancial assets unless those contracts are within the scope of other standards (for example, insurance contracts or lease contracts). The core principle of the guidance 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 five steps: 1) identify the contract(s) with the customer; 2) identify the performance obligations in the contract; 3) determine the transaction price; 4) allocate the transaction price to the performance obligations in the contract; and 5) recognize revenue when (or as) the entity satisfies a performance obligation. The guidance also specifies the accounting for some costs to obtain or fulfill a contract with a customer. For a public entity, the amendments in this update are effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. Early application is not permitted. The adoption of this amendment is not expected to have a material effect on the Company's consolidated financial statements.

In June 2014, the FASB issued Accounting Standards Update No. 2014-11, Transfers and Servicing (Topic 860): Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures. The guidance in this update changes the accounting for repurchase-to-maturity transactions and repurchase financing arrangements. It also requires enhanced disclosures about repurchase agreements and other similar transactions. The accounting changes in this update are effective for public companies for the first interim or annual period beginning after December 15, 2014. In addition, for public companies, the disclosure for certain transactions accounted for as a sale is effective for the first interim or annual period beginning on or after December 15, 2014, and the disclosure for transactions accounted for as secured borrowings is required to be presented for annual periods beginning after December 15, 2014, and interim periods beginning after March 15, 2015. Early application is not permitted. The adoption of this amendment did not have a material effect on the Company's consolidated financial statements.

In August 2014, the FASB issued Accounting Standards Update No. 2014-14, Receivables - Troubled Debt Restructurings by Creditors (Subtopic 310-40): Classification of Certain Government-Guaranteed Mortgage Loans upon Foreclosure. This update provides guidance on how to classify and measure certain government-guaranteed mortgage loans upon foreclosure, most commonly those offered by the Federal Housing Administration ("FHA") of the U.S. Department of Housing and Urban Development ("HUD"), and the U.S. Department of Veterans Affairs ("VA"). The ASU requires that a mortgage loan be derecognized and that a separate other receivable be recognized upon foreclosure if the following conditions are met: 1) the loan has a government guarantee that is not separable from the loan before foreclosure; 2) at the time of foreclosure, the creditor has the intent to convey the real estate property to the guarantor and make a claim on the guarantee, and the creditor has the ability to recover under the claim; and 3) at the time of foreclosure, an amount of the claim that is determined on the basis of the fair value of the real estate is fixed. Upon foreclosure, the separate other receivable should be measured based on the amount of the loan balance (principal and interest) expected to be recovered from the guarantor. The accounting changes in this update are effective for public companies for annual periods, and the interim periods within those annual periods, beginning after December 15, 2014. Early application is permitted under certain circumstances. The adoption of this amendment did not have a material effect on the Company's consolidated financial statements.

In August 2014, the FASB issued Accounting Standards Update No. 2014-15, Presentation of Financial Statements - Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern. The amendments in this update provide guidance in GAAP about management's responsibility to evaluate whether there is substantial doubt about an entity's ability to continue as a going concern and to provide related footnote disclosures. In doing so, the amendment should reduce diversity in the timing and content of footnote disclosures. Disclosures are required if it is probable an entity will be unable to meet its obligations within the look-forward period of twelve months after the financial statements are made available. Incremental substantial doubt disclosure is required if the probability is not mitigated by management's plans. The new standard applies to all entities for the first annual period ending after December 15, 2016, and interim periods thereafter. The adoption of this

standard is not expected to have a material effect on the Company's consolidated financial statements.

10. Subsequent Events

Management evaluated subsequent events through the date the consolidated financial statements were issued. Events or transactions occurring after March 31, 2015, but prior to the date the consolidated financial statements were issued, that provided additional evidence about conditions that existed at March 31, 2015 have been recognized in the consolidated financial statements for the period ended March 31, 2015. Events or transactions that provided evidence about conditions that did not exist at March 31, 2015, but arose before the consolidated financial statements were issued, have not been recognized in the consolidated financial statements for the period ended March 31, 2015.

## Table of Contents

On April 16, 2015, the board of directors of the Company declared a cash dividend of \$0.15 per share payable on June 15, 2015 to shareholders of record as of the close of business on June 1, 2015.

On April 17, 2015, the Company announced that the necessary regulatory approval had been received related to the proposed merger with Central Bancshares, Inc., a Minnesota corporation ("Central Bancshares") and parent company of Central Bank, Golden Valley, Minnesota.

On April 23, 2015, the Company held a special meeting of shareholders, at which the Company's shareholders voted to approve the merger agreement with Central Bancshares, pursuant to which Central Bancshares will merge with and into the Company. In connection with the merger, Central Bank, a Minnesota-chartered commercial bank and wholly-owned subsidiary of Central Bancshares, will become a wholly-owned subsidiary of the Company. The transaction is expected to be completed in May 2015.

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

### OVERVIEW

The Company provides financial services to individuals, businesses, governmental units and institutional customers in central and east-central Iowa. The Bank has office locations in Belle Plaine, Burlington, Cedar Falls, Conrad, Coralville, Davenport, Fairfield, Fort Madison, Iowa City, Melbourne, North English, North Liberty, Oskaloosa, Ottumwa, Parkersburg, Pella, Sigourney, Waterloo and West Liberty, Iowa. MidWestOne Insurance Services, Inc. provides personal and business insurance services in Cedar Falls, Conrad, Melbourne, Oskaloosa, Parkersburg, and Pella, Iowa. The Bank is actively engaged in many areas of commercial banking, including: acceptance of demand, savings and time deposits; making commercial, real estate, agricultural and consumer loans; and other banking services tailored for its individual customers. The Wealth Management Division of the Bank administers estates, personal trusts, conservatorships, and pension and profit-sharing accounts along with providing brokerage and other investment management services to customers.

We operate as an independent community bank that offers a broad range of customer-focused financial services as an alternative to large regional and multi-state banks in our market area. Management has invested in infrastructure and staffing to support our strategy of serving the financial needs of businesses, individuals and municipalities in our market area. We focus our efforts on core deposit generation, especially transaction accounts, and quality loan growth with an emphasis on growing commercial loan balances. We seek to maintain a disciplined pricing strategy on deposit generation that will allow us to compete for high quality loans while maintaining an appropriate spread over funding costs.

Our results of operations depend primarily on our net interest income, which is the difference between the interest income on our earning assets, such as loans and securities, and the interest expense paid on our deposits and borrowings. Results of operations are also affected by non-interest income and expense, the provision for loan losses and income tax expense. Significant external factors that impact our results of operations include general economic and competitive conditions, as well as changes in market interest rates, government policies, and actions of regulatory authorities.

The following discussion and analysis should be read in conjunction with the consolidated financial statements and related notes and with the statistical information and financial data appearing in this report as well as our 2014 Annual Report on Form 10-K. Results of operations for the three month period ended March 31, 2015 are not necessarily indicative of results to be attained for any other period.

### Critical Accounting Estimates

Critical accounting estimates are those which are both most important to the portrayal of our financial condition and results of operations, and require our management's most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain. Our critical accounting estimates relate to the allowance for loan losses, participation interests in loan pools, intangible assets, and fair value of available for sale investment securities, all of which involve significant judgment by our management. Information about our critical accounting estimates is included under Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" in our Annual Report on Form 10-K for the year ended December 31, 2014.

Pending Merger with Central Bancshares

On April 23, 2015, the Company held a special meeting of shareholders, at which the Company's shareholders voted to approve the merger agreement with Central Bancshares, pursuant to which Central Bancshares will merge with and into the Company. In connection with the merger, Central Bank, a Minnesota-chartered commercial bank and wholly-owned subsidiary of Central Bancshares, will become a wholly-owned subsidiary of the Company. The corporate headquarters of the combined company will be in Iowa City, Iowa.

Table of Contents

Subject to the terms and conditions of the merger agreement, each share of common stock of Central Bancshares will automatically be converted into the right to receive a pro rata portion of (i) 2,723,083 shares of common stock of the Company and (ii) \$64.0 million in cash, subject to certain adjustments as described in the merger agreement. The transaction is expected to close in May 2015.

## Comparison of Operating Results for the Three Months Ended March 31, 2015 and March 31, 2014

## Summary

For the three months ended March 31, 2015, we earned net income of \$4.8 million, compared with \$5.0 million for the three months ended March 31, 2014, a decrease of 3.6%. Basic and diluted earnings per common share for the first three months of 2015 were \$0.57, versus \$0.59 and \$0.58, respectively, in the first three months of 2014. After excluding the effects of \$0.5 million of expenses related to the previously announced merger with Central Bancshares, adjusted diluted earnings per share for the first quarter of 2015 were \$0.62. Our annualized return on average assets for the first three months of 2015 was 1.10% compared with 1.15% for the same period in 2014. Our annualized return on average shareholders' equity was 9.99% for the three months ended March 31, 2015 versus 11.13% for the three months ended March 31, 2014. The annualized return on average tangible equity ("ROATE") was 10.58% for the first three months of 2015 compared with 11.90% for the same period in 2014.

The following table presents selected financial results and measures for the first three months of 2015 and 2014.

(\$ amounts in thousands)	As of and for the Three Months Ended	
	March 31, 2015	2014
Net Income	\$4,796	\$4,973
Average Assets	1,773,129	1,747,027
Average Shareholders' Equity	194,761	181,274
Return on Average Assets* (ROAA)	1.10	1.15
Return on Average Shareholders' Equity* (ROAE)	9.99	11.13
Return on Average Tangible Equity* (ROATE)	10.58	11.90
Total Equity to Assets (end of period)	11.10	10.49
Tangible Equity to Tangible Assets (end of period)	10.69	10.04

\* Annualized

We have traditionally disclosed certain non-GAAP ratios, including our ROATE and the ratio of our tangible equity to tangible assets. We believe these ratios provide investors with information regarding our financial condition and results of operations and how we evaluate them internally.

Table of Contents

The following tables provide a reconciliation of the non-GAAP measures to the most comparable GAAP equivalents.

(in thousands)	For the Three Months Ended March 31,			
	2015		2014	
Net Income:				
Net income	\$4,796		\$4,973	
Plus: Intangible amortization, net of tax <sup>(1)</sup>	70		89	
Adjusted net income	\$4,866		\$5,062	
Average Tangible Equity:				
Average total shareholders' equity	\$194,761		\$181,274	
Less: Average intangibles	(8,193	)	(8,723	)
Average tangible equity	\$186,568		\$172,551	
ROATE (annualized)	10.58	%	11.90	%
Net Income:				
Net income	\$4,796		\$4,973	
Plus: Merger-related expenses	510		—	
Net tax effect of merger-related expenses <sup>(2)</sup>	(113	)	—	
Net income exclusive of merger-related expenses	\$5,193		\$4,973	
Diluted average number of shares	8,394,026		8,507,973	
Earnings Per Common Share-Diluted	\$0.57		\$0.58	
Earnings Per Common Share-Diluted, exclusive of merger-related expenses	\$0.62		\$0.58	

(1) Computed on a tax-equivalent basis, assuming a federal income tax rate of 35%.

(2) Computed based on qualifying tax deductible expenses, assuming a federal income tax rate of 35%

(in thousands)	As of March 31,			
	2015		2014	
Tangible Equity:				
Total shareholders' equity	\$197,392		\$183,143	
Less: Intangibles	(8,151	)	(8,669	)
Tangible equity	\$189,241		\$174,474	
Tangible Assets:				
Total assets	\$1,777,977		\$1,745,913	
Less: Intangibles	(8,151	)	(8,669	)
Tangible assets	\$1,769,826		\$1,737,244	
Tangible Equity/Tangible Assets	10.69	%	10.04	%

## Net Interest Income

Our net interest income for the three months ended March 31, 2015 was \$14.2 million, \$0.7 million, or 5.3%, greater than our net interest income reported for the three months ended March 31, 2014. Our total interest income of \$16.5 million was \$0.6 million higher in the first three months of 2015 compared with the same period in 2014. The increase in total interest income was driven by increases in interest and fees on loans and loan pool participation income, partially offset by lower income on investment securities. Income from loans increased from \$11.9 million in the first three months of 2014 to \$12.6 million in the first three months of 2015 due to a higher average loan balance and despite a lower yield. Income from loan pool participations increased from \$0.3 million for the three months ended March 31, 2014 to \$0.6 million for the three months ended March 31, 2015. Loan pool participation income is accounted for on a cash basis when actual payments are received, which can cause income related to this item to vary widely from period to period. Interest income on investment securities decreased \$0.4 million, or 11.2%, to \$3.3

million for the first three months of 2015 compared to the first three months of 2014. The decrease was primarily due to a lower average balance of investment securities during the first three months of 2015 compared to the same period of 2014, as the yield on these instruments remained steady. Net interest income was further augmented by reduced total interest expense. Total interest expense for the first three months of 2015 decreased \$0.2 million, or 6.4%, compared with the same period in 2014, due primarily to the lower average balance of FHLB borrowings. Our net interest margin on a tax-equivalent basis for the first three months of 2015 improved to 3.72% compared with 3.55% for the first three months of 2014. Net interest margin is a measure of the net return on interest-earning assets and is computed by dividing annualized net interest income on a tax-equivalent basis by the average of total interest-earning assets for the period. Our overall yield on earning assets increased to 4.26% for the first three



Table of Contents

months of 2015 from 4.14% for the first three months of 2014. This improvement was due primarily to increased average loan volumes along with higher yields on loan pool participations. The average cost of interest-bearing liabilities decreased in the first three months of 2015 to 0.67% from 0.72% for the first three months of 2014, due to the maturity and repayment of higher rate FHLB borrowings.

The following table shows the consolidated average balance sheets, detailing the major categories of assets and liabilities, the interest income earned on interest-earning assets, the interest expense paid for interest-bearing liabilities, and the related yields and interest rates for the three months ended March 31, 2015 and 2014. Dividing annualized income or expense by the average balances of assets or liabilities results in average yields or costs. Average information is provided on a daily average basis.

	Three Months Ended March 31, 2015			2014		
	Average Balance	Interest Income/ Expense	Average Rate/ Yield	Average Balance	Interest Income/ Expense	Average Rate/ Yield
(dollars in thousands)						
Average Earning Assets:						
Loans <sup>(1)(2)(3)</sup>	\$1,154,218	\$12,899	4.53 %	\$1,082,467	\$12,213	4.58 %
Loan pool participations <sup>(4)</sup>	20,974	620	11.99	27,061	280	4.20
Investment securities:						
Taxable investments	313,837	1,894	2.45	372,166	2,316	2.52
Tax exempt investments <sup>(2)</sup>	178,695	2,124	4.82	168,360	2,110	5.08
Total investment securities	492,532	4,018	3.31	540,526	4,426	3.32
Federal funds sold and interest-bearing balances	1,198	1	0.34	6,803	4	0.24
Total interest-earning assets	\$1,668,922	\$17,538	4.26 %	\$1,656,857	\$16,923	4.14 %
Cash and due from banks	19,035			19,585		
Premises and equipment	38,784			28,812		
Allowance for loan losses	(18,632 )			(18,491 )		
Other assets	65,020			60,264		
Total assets	\$1,773,129			\$1,747,027		
Average Interest-Bearing Liabilities:						
Savings and interest-bearing demand deposits	\$717,294	\$571	0.32 %	\$700,697	\$581	0.34 %
Certificates of deposit	465,772	1,152	1.00	453,911	1,142	1.02
Total deposits	1,183,066	1,723	0.59	1,154,608	1,723	0.61
Federal funds purchased and repurchase agreements	68,172	42	0.25	60,354	31	0.21
Federal Home Loan Bank borrowings	85,278	399	1.90	108,389	562	2.10
Long-term debt and other	15,773	76	1.95	15,941	78	1.98
Total borrowed funds	169,223	517	1.24	184,684	671	1.47
Total interest-bearing liabilities	\$1,352,289	\$2,240	0.67 %	\$1,339,292	\$2,394	0.72 %
Net interest spread <sup>(2)</sup>			3.59 %			3.42 %
Demand deposits	213,418			215,092		
Other liabilities	12,661			11,369		
Shareholders' equity	194,761			181,274		

Edgar Filing: MidWestOne Financial Group, Inc. - Form 10-Q

Total liabilities and shareholders' equity	\$ 1,773,129				\$ 1,747,027			
Interest income/earning assets <sup>(2)</sup>	\$ 1,668,922	\$ 17,538	4.26	%	\$ 1,656,857	\$ 16,923	4.14	%
Interest expense/earning assets	\$ 1,668,922	\$ 2,240	0.54	%	\$ 1,656,857	\$ 2,394	0.59	%
Net interest margin <sup>(2)(5)</sup>		\$ 15,298	3.72	%		\$ 14,529	3.55	%

Non-GAAP to GAAP Reconciliation:

Tax Equivalent Adjustment:

Loans	\$ 322	\$ 273
Securities	734	729
Total tax equivalent adjustment	1,056	1,002
Net Interest Income	\$ 14,242	\$ 13,527

34

---

Table of Contents

- (1) Loan fees included in interest income are not material.
- (2) Computed on a tax-equivalent basis, assuming a federal income tax rate of 35%.
- (3) Non-accrual loans have been included in average loans, net of unearned discount.
- (4) Includes interest income and discount realized on loan pool participations.
- (5) Net interest margin is tax-equivalent net interest income as a percentage of average earning assets.

The following table sets forth an analysis of volume and rate changes in interest income and interest expense on our average earning assets and average interest-bearing liabilities during the three months ended March 31, 2015, compared to the same period in 2014, reported on a fully tax-equivalent basis assuming a 35% tax rate. The table distinguishes between the changes related to average outstanding balances (changes in volume holding the initial interest rate constant) and the changes related to average interest rates (changes in average rate holding the initial outstanding balance constant). The change in interest due to both volume and rate has been allocated to volume and rate changes in proportion to the relationship of the absolute dollar amounts of the change in each.

	Three Months Ended March 31, 2015 Compared to 2014 Change due to		
	Volume	Rate/Yield	Net
(in thousands)			
Increase (decrease) in interest income:			
Loans, tax equivalent	\$1,518	\$(832 )	\$686
Loan pool participations	(419 )	759	340
Investment securities:			
Taxable investments	(358 )	(64 )	(422 )
Tax exempt investments	485	(471 )	14
Total investment securities	127	(535 )	(408 )
Federal funds sold and interest-bearing balances	(11 )	8	(3 )
Change in interest income	1,215	(600 )	615
Increase (decrease) in interest expense:			
Savings and interest-bearing demand deposits	78	(88 )	(10 )
Certificates of deposit	109	(99 )	10
Total deposits	187	(187 )	—
Federal funds purchased and repurchase agreements	4	7	11
Federal Home Loan Bank borrowings	(113 )	(50 )	(163 )
Other long-term debt	(1 )	(1 )	(2 )
Total borrowed funds	(110 )	(44 )	(154 )
Change in interest expense	77	(231 )	(154 )
Change in net interest income	\$1,138	\$(369 )	\$769
Percentage change in net interest income over prior period			5.3 %

Interest income and fees on loans on a tax-equivalent basis increased \$0.7 million, or 5.6%, in the first three months of 2015 compared to the same period in 2014. The increase is mainly due to an increase in average loans balances of \$71.8 million, or 6.6%, in the first three months of 2015 compared to the same period in 2014. This increase was partially offset by a slight decrease in the yield of loans from 4.58% in the first three months of 2014 to 4.53% in the same period of 2015, as new and renewing loans were made at lower interest rates than those paying down. We believe the increase in average loan balances was attributable to a continued improvement in general economic conditions, resulting in the willingness of borrowers to incur more debt to support growth in their businesses. The yield on our loan portfolio is affected by the amount of nonaccrual loans (which do not earn interest income), the mix of the portfolio (real estate loans generally have a lower overall yield than commercial and agricultural loans), the effects of competition and the interest rate environment on the amounts and volumes of new loan originations, and the mix of variable-rate versus fixed-rate loans in our portfolio.

Interest and discount income on loan pool participations was \$0.6 million for the first three months of 2015 compared with \$0.3 million for the first three months of 2014, an increase of \$0.3 million. Average loan pool participations were \$6.1 million, or 22.5%, lower in the first three months of 2015 compared to the same period in 2014. The decrease in average loan pool volume was due to loan pay downs and charge-offs, and is expected to continue as the Company exits this line of business.

The net “all-in” yield on loan pool participations was 11.99% for the first three months of 2015, up from 4.20% for the same period of 2014. Loan pool participation income is accounted for on a cash basis when actual payments are received, which can

Table of Contents

cause income related to this item to vary widely from period to period. As the percentage of creditworthy borrowers in the portfolio continues to decrease, we expect returns to generally trend lower.

Interest income on investment securities on a tax-equivalent basis totaled \$4.0 million in the first three months of 2015 compared with \$4.4 million for the same period of 2014, mainly due to lower average balances of investment securities. The average balance of investments in the first three months of 2015 was \$492.5 million compared with \$540.5 million in the first three months of 2014, a decrease of \$48.0 million, or 8.9%. The decrease in average balance resulted primarily from the use of proceeds from maturing investment securities to originate loans, to reduce FHLB borrowings, and to fund the net outflow of federal funds purchased and repurchase agreements. The tax-equivalent yield on our investment portfolio for the first three months of 2015 decreased to 3.31% from 3.32% in the comparable period of 2014.

Interest expense on deposits was unchanged for the first three months of 2015 compared with the same period in 2014. The weighted average rate paid on interest-bearing deposits was 0.59% for the first three months of 2015 compared with 0.61% for the first three months of 2014. This decline reflects the overall reduction in interest rates on deposits throughout the markets in which we operate and the gradual downward repricing of time deposits as higher rate certificates mature. Average interest-bearing deposits for the first three months of 2015 increased \$28.5 million, or 2.5%, compared with the same period in 2014, due primarily to increases in personal fund deposits in the first quarter of 2015 than in the comparable period of 2014.

Interest expense on borrowed funds was \$0.2 million lower in the first three months of 2015 compared with the same period in 2014, due to both lower average balances and lower rates. Interest on borrowed funds totaled \$0.5 million for the first three months of 2015. Average borrowed funds for the first three months of 2015 were \$15.5 million lower compared with the same period in 2014. This decrease was due primarily to a decrease in the level of FHLB borrowings. The weighted average rate on borrowed funds decreased to 1.24% for the first three months of 2015 compared with 1.47% for the first three months of 2014, reflecting the repayment of higher-rate borrowings.

**Provision for Loan Losses**

We recorded a provision for loan losses of \$0.6 million in the first three months of 2015, \$0.2 million, or 33.3%, more than the \$0.4 million provision in the first three months of 2014. Net loans charged off in the first three months of 2015 totaled \$0.4 million compared with \$0.2 million in the first three months of 2014. The increased provision reflects the increase in outstanding loan balances.

**Noninterest Income**

	Three Months Ended March			
	2015	2014	\$ Change	% Change
(dollars in thousands)				
Trust, investment, and insurance fees	\$1,581	\$1,518	\$63	4.2 %
Service charges and fees on deposit accounts	733	628	105	16.7
Mortgage origination and loan servicing fees	238	437	(199)	(45.5)
Other service charges, commissions and fees	603	619	(16)	(2.6)
Bank-owned life insurance income	295	229	66	28.8
Gain on sale or call of available for sale securities	555	783	(228)	(29.1)
Loss on sale of premises and equipment	3	3	—	—
Total noninterest income	\$4,008	\$4,217	\$(209)	(5.0)%
Noninterest income as a % of total revenue*	19.5 %	20.2 %		

\* Total revenue is net interest income plus noninterest income excluding gain/loss on securities and premises and equipment and impairment of investment securities.

Total noninterest income decreased \$0.2 million for the first three months of 2015 compared with the same period for 2014. The decrease was primarily due to a \$0.2 million, or 29.1%, decrease in gains on sale of investment securities combined with a decrease in mortgage origination and loan servicing fees of \$0.2 million, or 45.5%, from \$0.4 million in the first quarter of 2014 compared to \$0.2 million for the first quarter of 2015. The decline in mortgage origination and loan servicing fees was primarily due to a downward adjustment in the value of mortgage servicing rights of \$0.1

million.

These decreases were partially offset by an increase in service charges and fees on deposit accounts of \$0.1 million, or 16.7%, to \$0.7 million for the first quarter of 2015, compared to \$0.6 million for the same quarter of 2014, due primarily to increased service charges on demand deposit accounts, a trend we expect to continue. Income from trust, investment and insurance fees increased slightly to \$1.6 million for the first quarter of 2015. Management's strategic goal is for noninterest income to constitute 25% of total revenues (net interest income plus noninterest income excluding gain/loss on securities and premises and

36

---

Table of Contents

equipment and impairment of investment securities) over time. For the three months ended March 31, 2015, noninterest income comprised 19.5% of total revenues, compared with 20.2% for the same period in 2014. While our emphasis on trust, investment, and insurance fees, as well as service charges and fees on deposit accounts, has shown some improvement in these categories of noninterest income, the effects of decreased origination of mortgage loans for sale on the secondary market have significantly inhibited material improvement, a trend we expect to continue in the near-term. Management continues to evaluate options for increasing noninterest income, particularly in connection with the post-acquisition company and its new market areas.

## Noninterest Expense

	Three Months Ended			
	March 31, 2015	2014	\$ Change	% Change
(dollars in thousands)				
Salaries and employee benefits	\$6,869	\$6,134	\$735	12.0 %
Net occupancy and equipment expense	1,524	1,605	(81)	(5.0)
Professional fees	680	575	105	18.3
Data processing expense	432	424	8	1.9
FDIC insurance expense	239	243	(4)	(1.6)
Amortization of intangible assets	108	137	(29)	(21.2)
Other operating expense	1,327	1,274	53	4.2
Total noninterest expense	\$11,179	\$10,392	\$787	7.6 %

Noninterest expense for the first three months of 2015 was \$11.2 million, up \$0.8 million, or 7.6%, from the first quarter of 2014. The increase was mainly due to expenses paid of \$0.5 million (\$0.4 million after tax) related to the previously announced pending merger with Central Bancshares. The majority of the increase in noninterest expense was salaries and employee benefits, which increased \$0.7 million, or 12.0%, between the first quarter of 2015 and the first quarter of 2014. This increase in salaries and employee benefits includes \$0.3 million of incentive compensation expense associated with the pending merger with Central Bancshares, with the balance of the merger expenses reflected in professional fees expense, which increased \$0.1 million, or 18.3%, for the first quarter of 2015, compared with the first quarter of 2014. These increases were partially offset by a slight decrease in net occupancy and equipment expense for the first quarter of 2015 of \$0.1 million, or (5.0)%, compared with the first quarter of 2014. Noninterest expense is expected to increase in the second quarter of 2015 as a result of the consummation of the merger.

## Income Tax Expense

Our effective tax rate, or income taxes divided by income before taxes, was 25.9% for the first three months of 2015, and 27.9% for the first three months of 2014. Income tax expense decreased to \$1.7 million in the first three months of 2015 compared with \$1.9 million for the same period of 2014, primarily due to decreased taxable net income.

## FINANCIAL CONDITION

Our total assets decreased slightly to \$1.78 billion at March 31, 2015 from \$1.80 billion at December 31, 2014, resulting primarily from decreased balances in investment securities available for sale, cash and cash equivalents, and accrued interest receivable. These decreases were partially offset by increased balances in loans, investment securities held to maturity, and premises and equipment, net. Total deposits at March 31, 2015, were \$1.41 billion, a decrease of \$0.3 million, from December 31, 2014. The deposit decrease was concentrated in jumbo certificates of deposit accounts (accounts \$100,000 and over), which decreased by \$7.0 million, or 2.9%, and certificates of deposit under \$100,000, which decreased by \$5.9 million, or 2.5%. Interest bearing demand deposits increased \$10.5 million, or 1.7%, to \$629.0 million at March 31, 2015, from \$618.5 million at December 31, 2014, and savings deposits increased \$3.9 million, or 3.8%, from December 31, 2014 to March 31, 2015. Federal funds purchased decreased by \$8.5 million, to \$8.9 million. FHLB borrowings decreased by \$15.0 million, or 16.1%, to \$78.0 million.

## Investment Securities

Investment securities available for sale totaled \$409.0 million as of March 31, 2015. This was a decrease of \$66.0 million, or 13.9%, from December 31, 2014. Investment securities serve as a source of liquidity, and investment balances vary along with fluctuations in levels of deposits and loans. Investment securities classified as held to maturity increased to \$54.3 million as of March 31, 2015 from \$51.5 million at December 31, 2014. The \$2.8 million, or 5.4%, increase in held to maturity investments was due to a strategic decision to increase our holdings in this classification to mitigate any volatility in capital levels that may result from future increases in interest rates. The investment portfolio consisted mainly of obligations of states and political subdivisions (50.4%), mortgage-backed securities and collateralized mortgage obligations (33.2%), and U.S. government agencies (5.8%).



Table of Contents

## Loans

The composition of bank loans (before deducting the allowance for loan losses) was as follows:

(dollars in thousands)	March 31, 2015		December 31, 2014	
	Balance	% of Total	Balance	% of Total
Agricultural	\$ 110,959	9.4 %	\$ 104,809	9.3 %
Commercial and industrial	320,527	27.2	303,108	26.7
Credit cards	1,317	0.1	1,246	0.1
Overdrafts	521	0.1	744	0.1
Commercial real estate:				
Construction and development	69,255	5.9	59,383	5.2
Farmland	86,715	7.4	83,700	7.4
Multifamily	54,227	4.6	54,886	4.8
Commercial real estate-other	233,252	19.8	228,552	20.2
Total commercial real estate	443,449	37.7	426,521	37.6
Residential real estate:				
One- to four- family first liens	221,826	18.9	219,314	19.4
One- to four- family junior liens	53,240	4.5	53,297	4.7
Total residential real estate	275,066	23.4	272,611	24.1
Consumer	24,488	2.1	23,480	2.1
Total loans	\$ 1,176,327	100.0 %	\$ 1,132,519	100.0 %

Total bank loans (excluding loan pool participations and loans held for sale) increased by \$43.8 million to \$1.18 billion as of March 31, 2015 as compared to December 31, 2014. While most loan categories saw increased balances, the increase was primarily in commercial and industrial loans, construction and development loans, and agricultural loans. Increases in these categories were slightly offset by a decrease in multifamily commercial real estate loans. As of March 31, 2015, our bank loan (excluding loan pool participations) to deposit ratio was 83.5% compared with a bank loan to deposit ratio of 80.4% at December 31, 2014. We anticipate that the loan to deposit ratio will remain relatively stable or increase in future periods, with loans showing overall measured growth and deposits remaining steady or decreasing with interest rates remaining at record lows.

We have minimal direct exposure to subprime mortgages in our loan portfolio. Our loan policy provides a guideline that real estate mortgage borrowers have a Beacon score of 640 or greater. Exceptions to this guideline have been noted but the overall exposure is deemed minimal by management. Mortgages we originate and sell on the secondary market are typically underwritten according to the guidelines of secondary market investors. These mortgages are sold on a non-recourse basis.

## Loan Pool Participations

As of March 31, 2015, we had loan pool participations, net, totaling \$18.2 million, down from \$19.3 million at December 31, 2014. Loan pool participations are participation interests in performing, subperforming and nonperforming loans that have been purchased from various non-affiliated banking organizations. The Company entered into this business upon consummation of its merger with Former MidWestOne in March 2008. As previously announced, the Company has decided to exit this line of business as current balances pay down. The loan pool investment balances shown as an asset on our consolidated balance sheets represent the discounted purchase cost of the loan pool participations. As of March 31, 2015, the categories of loans by collateral type in the loan pool participations were commercial real estate - 66%, commercial loans - 4%, single-family residential real estate - 15% and other loans - 15%. We have minimal exposure in the loan pool participations to consumer real estate subprime credit or to construction and real estate development loans.

Our overall cost basis in the loan pool participations represents a discount from the aggregate outstanding principal amount of the loans underlying the pools. For example, as of March 31, 2015, such cost basis was \$20.4 million, while the contractual outstanding principal amount of the underlying loans as of such date was approximately \$66.2 million, resulting in an investment basis of 30.8% of the "face amount" of the underlying loans. The discounted cost

basis inherently reflects the assessed collectability of the underlying loans. We do not include any amounts related to the loan pool participations in our totals of nonperforming loans.

As of March 31, 2015, loans in the southeast region of the United States represented approximately 44% of our loan pool participations. The northeast was the next largest area with 33%, and the central region represented 22%. The southwest and the northwest regions represented a minimal amount of the portfolio at less than 1% combined. The highest concentration of assets was in Florida at approximately 19% of the basis total, with the next highest state levels being Ohio at approximately 13% and New Jersey at approximately 8%. As of March 31, 2015, approximately 71% of the loans were contractually current or less than

Table of Contents

90 days past due, while 29% were contractually past due 90 days or more. It should be noted that many of the loans were acquired in a contractually past due status, which is reflected in the discounted purchase price of the loans. Performance status is monitored on a monthly basis. The 29% of loans contractually past due includes loans in litigation and foreclosed property. As of March 31, 2015, loans in litigation totaled approximately \$1.2 million, while foreclosed property was approximately \$2.9 million.

**Premises and Equipment**

As of March 31, 2015, premises and equipment totaled \$39.4 million, an increase of \$1.7 million, or 4.4%, from \$37.8 million at December 31, 2014. This increase was primarily due to two ongoing major construction projects, both in our Iowa City market. In August 2013, we entered into a contract for the restoration and remodeling of the building which serves as the main office of the Bank and headquarters of the Company. The estimated cost of the restoration and remodeling is \$13.8 million, and it is anticipated that the project will be completed in April 2016. In December 2013, we entered into a contract for the construction of a new Home Mortgage Center with an estimated cost of design and construction of \$16.0 million, and with completion anticipated in the second quarter of 2015. As of March 31, 2015, an estimated \$13.3 million remained to be paid on these contracts. We expect the balance of premises and equipment to continue rising in the future as these projects progress towards completion in the remainder of 2015 and 2016, and as a result of our pending merger with Central Bancshares.

**Intangible Assets**

Intangible assets decreased to \$8.2 million as of March 31, 2015 from \$8.3 million as of December 31, 2014 as a result of normal amortization. Amortization of intangible assets is recorded using an accelerated method based on the estimated life of the intangible.

The following table summarizes the amounts and carrying values of intangible assets as of March 31, 2015.

	Gross Carrying Amount	Accumulated Amortization	Unamortized Intangible Assets
(in thousands)			
March 31, 2015			
Intangible assets:			
Insurance agency intangible	\$ 1,320	\$ 978	\$ 342
Core deposit premium	5,433	4,822	611
Trade name intangible	7,040	—	7,040
Customer list intangible	330	172	158
Total	\$14,123	\$ 5,972	\$ 8,151

**Deposits**

Total deposits as of March 31, 2015 were \$1.41 billion, the same as of December 31, 2014. Interest-bearing checking deposits were the largest category of deposits at March 31, 2015, representing approximately 44.7% of total deposits. Total interest-bearing checking deposits were \$629.0 million at March 31, 2015, an increase of \$10.5 million, or 1.7%, from \$618.5 million at December 31, 2014. Included in interest-bearing checking deposits at March 31, 2015 was \$17.8 million of brokered deposits in the Insured Cash Sweep (ICS) program, a decrease of \$9.8 million, or 35.5%, from the \$27.6 million at December 31, 2014, due primarily to a withdrawal by one account holder.

Non-interest bearing demand deposits were \$212.7 million at March 31, 2015, a decrease of \$1.8 million, or 0.8%, from \$214.5 million at December 31, 2014. The decreased balances in non-interest bearing deposit accounts were primarily in commercial accounts. Savings deposits increased \$3.9 million, or 3.8%, from December 31, 2014 to March 31, 2015, primarily in personal savings. Total certificates of deposit were \$460.2 million at March 31, 2015, down \$12.8 million, or 2.7%, from \$473.0 million at December 31, 2014, as public fund and individual depositors moved balances from certificates of deposit to interest-bearing checking. Included in total certificates of deposit at March 31, 2015 was \$5.2 million of brokered deposits in the Certificate of Deposit Account Registry Service (CDARS) program, a decrease of \$0.8 million, or 13.7%, from the \$6.1 million at December 31, 2014. Based on recent experience, management anticipates that many of the maturing certificates of deposit will not be renewed upon maturity due to the current low interest rate environment. Approximately 83.6% of our total deposits were considered

“core” deposits as of March 31, 2015.

Federal Home Loan Bank Borrowings

FHLB borrowings totaled \$78.0 million as of March 31, 2015 compared with \$93.0 million as of December 31, 2014.

We utilize FHLB borrowings as a supplement to customer deposits to fund earning assets and to assist in managing interest rate risk. Thus, if deposits decline, FHLB borrowing may increase to provide necessary liquidity.

39

---

Table of Contents

## Long-term Debt

Long-term debt in the form of junior subordinated debentures that have been issued to a statutory trust that issued trust preferred securities was \$15.5 million as of March 31, 2015, unchanged from December 31, 2014. These junior subordinated debentures were assumed by us from Former MidWestOne in the merger in 2008. Former MidWestOne had issued these junior subordinated debentures on September 20, 2007, to MidWestOne Capital Trust II. The junior subordinated debentures supporting the trust preferred securities have a maturity date of December 15, 2037, and do not require any principal amortization. They became callable on December 15, 2012 at par, and are callable, in whole or in part, on any interest payment date, at the Company's option. The interest rate on the debt is a variable rate based on the three-month LIBOR rate plus 1.59% with interest payable quarterly. At March 31, 2015, the interest rate on the debt was 1.86%.

## Nonperforming Assets

The following tables set forth information concerning nonperforming loans by class of financing receivable at March 31, 2015 and December 31, 2014:

	90 Days or More Past Due and Still Accruing Interest	Restructured	Nonaccrual	Total
(in thousands)				
March 31, 2015				
Agricultural	\$—	\$2,901	\$—	\$2,901
Commercial and industrial	—	1,954	430	2,384
Credit cards	—	—	—	—
Overdrafts	—	—	—	—
Commercial real estate:				
Construction and development	—	—	83	83
Farmland	—	2,209	23	2,232
Multifamily	—	—	—	—
Commercial real estate-other	924	—	1,291	2,215
Total commercial real estate	924	2,209	1,397	4,530
Residential real estate:				
One- to four- family first liens	111	990	1,430	2,531
One- to four- family junior liens	—	13	192	205
Total residential real estate	111	1,003	1,622	2,736
Consumer	2	17	14	33
Total	\$1,037	\$8,084	\$3,463	\$12,584

Table of Contents

	90 Days or More Past Due and Still Accruing Interest	Restructured	Nonaccrual	Total
(in thousands)				
December 31, 2014				
Agricultural	\$—	\$3,027	\$—	\$3,027
Commercial and industrial	66	2,217	479	2,762
Credit cards	—	—	—	—
Overdrafts	—	—	—	—
Commercial real estate:				
Construction and development	—	—	83	83
Farmland	—	2,268	24	2,292
Multifamily	—	—	—	—
Commercial real estate-other	—	255	1,200	1,455
Total commercial real estate	—	2,523	1,307	3,830
Residential real estate:				
One- to four- family first liens	780	1,119	1,261	3,160
One- to four- family junior liens	—	14	192	206
Total residential real estate	780	1,133	1,453	3,366
Consumer	2	18	16	36
Total	\$848	\$8,918	\$3,255	\$13,021

Our nonperforming assets totaled \$14.2 million as of March 31, 2015, a decrease of \$0.7 million, or 4.7%, from December 31, 2014. The balance of OREO at March 31, 2015 was \$1.7 million, down from \$1.9 million of OREO at December 31, 2014. All of the OREO property was acquired through foreclosures, and we are actively working to sell all properties held as of March 31, 2015. OREO is carried at appraised value less estimated cost of disposal at the date of acquisition. Additional discounts could be required to market and sell the properties, resulting in a write down through expense. Nonperforming loans totaled \$12.6 million (1.07% of total bank loans) as of March 31, 2015, compared to \$13.0 million (1.15% of total bank loans) as of December 31, 2014.

At March 31, 2015, nonperforming loans consisted of \$3.5 million in nonaccrual loans, \$8.1 million in TDRs and \$1.0 million in loans past due 90 days or more and still accruing interest. This compares with \$3.3 million, \$8.9 million and \$0.8 million, respectively, as of December 31, 2014. Nonaccrual loans increased by \$0.2 million, or 6.4%, at March 31, 2015 compared to December 31, 2014. The Company experienced a \$0.8 million, or 9.4%, decrease in restructured loans from December 31, 2014 to March 31, 2015, primarily due to payments and a payoff collected from TDR-status borrowers, as well as the movement of two borrowers out of TDR status. During the same period, loans past due 90 days or more and still accruing interest increased \$0.2 million, or 22.3%, from December 31, 2014 to March 31, 2015. Additionally, loans past due 30 to 89 days (not included in the nonperforming loan totals) were \$3.7 million as of March 31, 2015 compared with \$3.9 million as of December 31, 2014, a decrease of \$0.2 million or 4.7%. The pending merger is not expected to have a material impact on the Company's level of nonperforming loans. Loan Review and Classification Process for Agricultural, Commercial and Industrial, and Commercial Real Estate Loans:

The Company maintains a loan review and classification process which involves multiple officers of the Company and is designed to assess the general quality of credit underwriting and to promote early identification of potential problem loans. All commercial and agricultural loan officers are charged with the responsibility of risk rating all loans in their portfolios and updating the ratings, positively or negatively, on an ongoing basis as conditions warrant. A monthly loan officer validation worksheet documents this process. Risk ratings are selected from an 8-point scale with ratings as follows: ratings 1- 4 Satisfactory (pass), rating 5 Watch (potential weakness), rating 6 Substandard

(well-defined weakness), rating 7 Doubtful, and rating 8 Loss.

When a loan officer originates a new loan, based upon proper loan authorization, he or she documents the credit file with an offering sheet summary, supplemental underwriting analysis, relevant financial information and collateral evaluations. All of this information is used in the determination of the initial loan risk rating. The Company's loan review department undertakes independent credit reviews of relationships based on either criteria established by loan policy, risk-focused sampling, or random sampling. Loan policy requires the top 50 lending relationships by total exposure as well as all classified and Watch rated credits over \$250,000 be reviewed no less than annually. The individual loan reviews consider such items as: loan type; nature, type and estimated value of collateral; borrower and/or guarantor estimated financial strength; most recently available financial information;

Table of Contents

related loans and total borrower exposure; and current/anticipated performance of the loan. The results of such reviews are presented to executive management.

Through the review of delinquency reports, updated financial statements or other relevant information, the lending officer and/or loan review personnel may determine that a loan relationship has weakened to the point that a criticized (loan grade 5) or classified (loan grades 6 through 8) status is warranted. When a loan relationship with total related exposure of \$1.0 million or greater is adversely graded (5 or above), or is classified as a TDR (regardless of size), the lending officer is then charged with preparing a loan strategy summary worksheet that outlines the background of the credit problem, current repayment status of the loans, current collateral evaluation and a workout plan of action. This plan may include goals to improve the credit rating, assist the borrower in moving the loans to another institution and/or collateral liquidation. All such reports are first presented to regional management and then to the board of directors by the Executive Vice President, Chief Credit Officer (or a designee).

Depending upon the individual facts and circumstances and the result of the Classified/Watch review process, loan officers and/or loan review personnel may categorize the loan relationship as impaired. Once that determination has occurred, the loan officer, in conjunction with regional management, will complete an evaluation of the collateral (for collateral-dependent loans) based upon the estimated collateral value, adjusting for current market conditions and other local factors that may affect collateral value. Loan review personnel may also complete an independent impairment analysis when deemed necessary. These judgmental evaluations may produce an initial specific allowance for placement in the Company's allowance for loan and lease losses calculation. As soon as practical, an updated value estimate of the collateral backing that impaired loan relationship is completed. After the updated value is determined, regional management, with assistance from the loan review department, reviews the valuation and updates the specific allowance analysis for each loan relationship accordingly. The board of directors on a quarterly basis reviews the Classified/Watch reports including changes in credit grades of 5 or higher as well as all impaired loans, the related allowances and OREO.

In general, once the specific allowance has been finalized, regional and executive management will consider a charge-off prior to the calendar quarter-end in which that reserve calculation is finalized.

The review process also provides for the upgrade of loans that show improvement since the last review.

#### Restructured Loans

We restructure loans for our customers who appear to be able to meet the terms of their loan over the long term, but who may be unable to meet the terms of the loan in the near term due to individual circumstances. We consider the customer's past performance, previous and current credit history, the individual circumstances surrounding the current difficulties and their plan to meet the terms of the loan in the future prior to restructuring the terms of the loan. The following factors are indicators that the Bank has granted a concession (one or multiple items may be present):

- The borrower receives a reduction of the stated interest rate for the remaining original life of the debt.
- The borrower receives an extension of the maturity date or dates at a stated interest rate lower than the current market interest rate for new debt with similar risk characteristics.
- The borrower receives a reduction of the face amount or maturity amount of the debt as stated in the instrument or other agreement.
- The borrower receives a deferral of required payments (principal and/or interest).
- The borrower receives a reduction of the accrued interest.

Generally, loans are restructured through short-term interest rate relief, short-term principal payment relief or short-term principal and interest payment relief. Once a restructured loan has gone 90 days or more past due or is placed on nonaccrual status, it is included in the 90 days and over past due or nonaccrual totals in the previous table. During the three months ended March 31, 2015, the Company restructured no loans by granting a concession to a borrower experiencing financial difficulties.



Table of Contents

We consider all TDRs, regardless of whether they are performing in accordance with their modified terms, to be impaired loans when determining our allowance for loan losses. A summary of restructured loans as of March 31, 2015 and December 31, 2014 is as follows:

	March 31, 2015	December 31, 2014
(in thousands)		
Restructured Loans (TDRs):		
In compliance with modified terms	\$8,084	\$8,918
Not in compliance with modified terms - on nonaccrual status	567	522
Total restructured loans	\$8,651	\$9,440

## Allowance for Loan Losses

Our ALLL as of March 31, 2015 was \$16.5 million, which was 1.40% of total bank loans (excluding loan pool participations) as of that date. This compares with an ALLL of \$16.4 million as of December 31, 2014, which was 1.44% of total bank loans as of that date. Gross charge-offs for the first three months of 2015 totaled \$0.8 million, while recoveries of previously charged-off loans totaled \$0.4 million. Annualized net loan charge offs to average bank loans for the first three months of 2015 was 0.15% compared to 0.09% for the year ended December 31, 2014. As of March 31, 2015, the ALLL was 131.3% of nonperforming loans compared with 125.7% as of December 31, 2014. Based on the inherent risk in the loan portfolio, we believe that as of March 31, 2015, the ALLL was adequate; however, there is no assurance losses will not exceed the allowance, and any growth in the loan portfolio or uncertainty in the general economy may require that management continue to evaluate the adequacy of the ALLL and make additional provisions in future periods as deemed necessary.

There were no changes to our ALLL calculation methodology during the first three months of 2015. Classified and impaired loans are reviewed per the requirements of FASB ASC Topic 310.

We currently track the loan to value ("LTV") ratio of loans in our portfolio, and those loans in excess of internal and supervisory guidelines are presented to the Bank's board of directors on a quarterly basis. At March 31, 2015, there were 4 owner-occupied 1-4 family loans with a LTV ratio of 100% or greater. In addition, there were 41 home equity loans without credit enhancement that had a LTV ratio of 100% or greater. We have the first lien on 32 of these equity loans and other financial institutions have the first lien on the remaining 9.

We review all impaired and nonperforming loans individually on a quarterly basis to determine their level of impairment due to collateral deficiency or insufficient cash-flow based on a discounted cash-flow analysis. At March 31, 2015, TDRs were not a material portion of the loan portfolio. We review loans 90 days and over past due that are still accruing interest no less than quarterly to determine if there is a strong reason that the credit should not be placed on non-accrual.

## Capital Resources

Total shareholders' equity was \$197.4 million as of March 31, 2015, compared to \$192.7 million as of December 31, 2014, an increase of \$4.7 million, or 2.4%. This increase was primarily attributable to net income of \$4.8 million for the first three months of 2015, a \$1.0 million increase in accumulated other comprehensive income due to market value adjustments on investment securities available for sale, and a \$0.3 million decrease in treasury stock due to the issuance of 15,853 shares of Company common stock in connection with stock compensation plans. These increases were partially offset by the payment of \$1.3 million in common stock dividends. No shares of Company common stock were repurchased in the first quarter of 2015.

Total shareholders' equity was 11.10% of total assets as of March 31, 2015 and was 10.71% as of December 31, 2014. The ratio of tangible equity to tangible assets was 10.69% as of March 31, 2015 and 10.29% as of December 31, 2014. Our Tier 1 capital to risk-weighted assets ratio was 14.27% as of March 31, 2015 and was 13.47% as of December 31, 2014. Risk-based capital guidelines require the classification of assets and some off-balance-sheet items in terms of credit-risk exposure and the measuring of capital as a percentage of the risk-adjusted asset totals. We believe that, as of March 31, 2015, the Company and the Bank met all capital adequacy requirements to which we were subject. As of that date, the Bank was "well capitalized" under regulatory prompt corrective action provisions.

In July 2013, the U.S. federal banking authorities approved the implementation of the Basel III regulatory capital reforms and issued rules (the "Basel III Rules") effecting certain changes required by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Dodd-Frank Act"). The Basel III Rules are applicable to all U.S. banks that are subject to minimum capital requirements, as well as to bank and savings and loan holding companies other than "small bank holding companies" (generally bank holding companies with consolidated assets of less than \$1.0 billion). The Basel III Rules not only increase most of the required minimum regulatory capital ratios, but they also introduce a new Common Equity Tier 1 Capital ratio and the concept of a capital conservation buffer. The Basel III Rules also expand the definition of capital as in effect currently

Table of Contents

by establishing criteria that instruments must meet to be considered Additional Tier 1 Capital (Tier 1 Capital in addition to Common Equity) and Tier 2 Capital. A number of instruments that now generally qualify as Tier 1 Capital will not qualify, or their qualifications will change, when the Basel III Rules are fully implemented. The Basel III Rules also permit banking organizations with less than \$15.0 billion in assets to retain, through a one-time election, the existing treatment for accumulated other comprehensive income, which currently does not affect regulatory capital. The Company elected to retain this treatment, which reduces the volatility of regulatory capital levels. The Basel III Rules have maintained the general structure of the current prompt corrective action framework, while incorporating the increased requirements. The prompt corrective action guidelines were also revised to add the Common Equity Tier 1 Capital ratio. In order to be a “well-capitalized” depository institution under the new regime, a bank and holding company must maintain a Common Equity Tier 1 Capital ratio of 6.5% or more; a Tier 1 Capital ratio of 8% or more; a Total Capital ratio of 10% or more; and a leverage ratio of 5% or more. Generally, financial institutions became subject to the new Basel III Rules on January 1, 2015, with phase-in periods for many of the changes.

We have traditionally disclosed certain non-GAAP ratios and amounts to evaluate and measure our financial condition, including our Tier 1 capital to risk-weighted assets ratio. We believe this ratio provides investors with information regarding our financial condition and how we evaluate our financial condition internally. The following table provides a reconciliation of this non-GAAP measure to the most comparable GAAP equivalent.

(in thousands)	At March 31, 2015		At December 31, 2014	
Tier 1 capital				
Total shareholders' equity	\$197,392		\$192,731	
Less: Net unrealized gains on securities available for sale	(6,317	)	(5,322	)
Disallowed Intangibles	(3,262	)	(8,511	)
Common equity tier 1 capital	\$187,813		—	
Plus: Long term debt (qualifying restricted core capital)	10,825		15,464	
Tier 1 capital	\$198,638		\$194,362	
Risk-weighted assets	\$1,392,047		\$1,442,585	
Tier 1 capital to risk-weighted assets	14.27	%	13.47	%
Common equity tier 1 capital to risk-weighted assets	13.49	%	N/A	

The following table provides the capital levels and minimum required capital levels for the Company and the Bank:

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions				
	Amount	Ratio	Amount	Ratio	Amount	Ratio			
(dollars in thousands)									
At March 31, 2015									
Consolidated:									
Total capital/risk based	\$216,049	15.52	%	\$111,364	8.00	%	N/A	N/A	
Tier 1 capital/risk based	198,638	14.27		83,523	6.00		N/A	N/A	
Common equity tier 1 capital/risk based	187,813	13.49		62,642	4.50		N/A	N/A	
Tier 1 capital/adjusted average	198,638	11.26		70,565	4.00		N/A	N/A	
MidWestOne Bank:									
Total capital/risk based	\$201,623	14.56	%	\$110,764	8.00	%	\$138,455	10.00	%
Tier 1 capital/risk based	184,316	13.31		83,073	6.00		110,764	8.00	
Common equity tier 1 capital/risk based	184,316	13.31		62,305	4.50		89,996	6.50	
Tier 1 capital/adjusted average	184,316	10.50		70,197	4.00		87,746	5.00	
At December 31, 2014									

Edgar Filing: MidWestOne Financial Group, Inc. - Form 10-Q

Consolidated:

Total capital/risk based	\$212,559	14.73	%	\$115,407	8.00	%	N/A	N/A
Tier 1 capital/risk based	194,362	13.47		57,703	4.00		N/A	N/A
Tier 1 capital/adjusted average	194,362	10.85		71,647	4.00		N/A	N/A
MidWestOne Bank:								
Total capital/risk based	\$197,018	13.75	%	\$114,624	8.00	%	\$143,280	10.00 %
Tier 1 capital/risk based	179,098	12.50		57,312	4.00		85,968	6.00
Tier 1 capital/adjusted average	179,098	10.05		71,249	4.00		89,061	5.00

## Table of Contents

On February 15, 2015, 20,900 restricted stock units were granted to certain officers of the Company. Additionally, during the first three months of 2015, 15,853 shares of common stock were issued in connection with the vesting of previously awarded grants of restricted stock units, of which 1,210 shares were surrendered by grantees to satisfy tax requirements, and 925 nonvested restricted stock units were forfeited. No shares of common stock were issued in connection with the exercise of previously issued stock options.

### Liquidity

Liquidity management involves meeting the cash flow requirements of depositors and borrowers. We conduct liquidity management on both a daily and long-term basis, and adjust our investments in liquid assets based on expected loan demand, projected loan maturities and payments, estimated cash flows from loan pool participations, expected deposit flows, yields available on interest-bearing deposits, and the objectives of our asset/liability management program. We had liquid assets (cash and cash equivalents) of \$21.5 million as of March 31, 2015, compared with \$23.4 million as of December 31, 2014. Interest-bearing deposits in banks at March 31, 2015, increased to \$1.0 million, an increase of \$0.6 million from December 31, 2014. Investment securities classified as available for sale, totaling \$409.0 million and \$474.9 million as of March 31, 2015 and December 31, 2014, respectively, could be sold to meet liquidity needs if necessary. Additionally, our bank subsidiary maintains unsecured lines of credit with several correspondent banks and secured lines with the Federal Reserve Bank Discount Window and the FHLB that would allow it to borrow funds on a short-term basis, if necessary. Management believes that the Company had sufficient liquidity as of March 31, 2015 to meet the needs of borrowers and depositors.

Our principal sources of funds were proceeds from the maturity and sale of investment securities and funds provided by operations. While scheduled loan amortization and maturing interest-bearing deposits are relatively predictable sources of funds, deposit flows and loan prepayments are greatly influenced by economic conditions, the general level of interest rates, and competition. We utilize particular sources of funds based on comparative costs and availability. This includes fixed-rate FHLB borrowings that can generally be obtained at a more favorable cost than deposits of comparable maturity. We generally manage the pricing of our deposits to maintain a steady deposit base but from time to time may decide, as we have done in the past, not to pay rates on deposits as high as our competition.

As of March 31, 2015, we had \$15.5 million of long-term debt outstanding. This amount represents indebtedness payable under junior subordinated debentures issued to a subsidiary trust that issued trust preferred securities in a pooled offering. The junior subordinated debentures were issued with a 30-year term. The interest rate on the debt is a variable rate, based on the three-month LIBOR rate plus 1.59%, with interest payable quarterly. At March 31, 2015, the interest rate on the debt was 1.86%.

### Inflation

The effects of price changes and inflation can vary substantially for most financial institutions. While management believes that inflation affects the growth of total assets, it is difficult to assess its overall impact on the Company. Management believes this to be the case due to the fact that generally neither the timing nor the magnitude of the inflationary changes in the consumer price index ("CPI") coincides with changes in interest rates. The price of one or more of the components of the CPI may fluctuate considerably and thereby influence the overall CPI without having a corresponding effect on interest rates or upon the cost of those goods and services normally purchased by us. In years of high inflation and high interest rates, intermediate and long-term interest rates tend to increase, thereby adversely impacting the market values of investment securities, mortgage loans and other long-term fixed rate loans held by financial institutions. In addition, higher short-term interest rates caused by inflation tend to increase financial institutions' cost of funds. In other years, the reverse situation may occur.

### Off-Balance-Sheet Arrangements

We are a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of our customers, which include commitments to extend credit, commitments to originate residential mortgage loans held for sale, commercial letters of credit, and standby letters of credit. Commitments to extend credit are agreements to lend to customers at predetermined interest rates, as long as there is no violation of any condition established in the contracts. Our exposure to credit loss in the event of nonperformance by the other party to the commitments to extend credit is represented by the contractual amount of those instruments. We use the same credit policies in making commitments as we do for on-balance-sheet instruments.

Commitments to extend credit 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. We evaluate each customer's creditworthiness on a case-by-case basis. As of March 31, 2015, outstanding commitments to extend credit totaled approximately \$276.5 million. We have established a reserve of \$0.2 million, which represents our estimate of probable losses as a result of these transactions. This reserve is not part of our allowance for loan losses. Commitments under standby and performance letters of credit outstanding aggregated \$3.7 million as of March 31, 2015. We do not anticipate any losses as a result of these transactions.

Table of Contents

Residential mortgage loans sold to others are predominantly conventional residential first lien mortgages originated under our usual underwriting procedures, and are most often sold on a nonrecourse basis. At March 31, 2015, there were approximately \$8.3 million of mandatory commitments with investors to sell not yet originated residential mortgage loans. We do not anticipate any losses as a result of these transactions.

## Table of Contents

### Item 3. Quantitative and Qualitative Disclosures about Market Risk.

In general, market risk is the risk of change in asset values due to movements in underlying market rates and prices. Interest rate risk is the risk to earnings and capital arising from movements in interest rates. Interest rate risk is the most significant market risk affecting the Company as other types of market risk, such as foreign currency exchange rate risk and commodity price risk, play a lesser role in the normal course of our business activities.

In addition to interest rate risk, economic conditions in recent years have made liquidity risk (in particular, funding liquidity risk) a more prevalent concern among financial institutions. In general, liquidity risk is the risk of being unable to fund an entity's obligations to creditors (including, in the case of banks, obligations to depositors) as such obligations become due and/or fund its acquisition of assets.

#### Liquidity Risk

Liquidity refers to our ability to fund operations, to meet depositor withdrawals, to provide for our customers' credit needs, and to meet maturing obligations and existing commitments. Our liquidity principally depends on cash flows from operating activities, investment in and maturity of assets, changes in balances of deposits and borrowings, and our ability to borrow funds.

Net cash inflows from operating activities were \$8.6 million in the first three months of 2015, compared with \$5.7 million in the first three months of 2014. Net income before depreciation, amortization, and accretion is generally the primary contributor for net cash inflows from operating activities.

Net cash inflows from investing activities were \$20.0 million in the first three months of 2015, compared to net cash inflows of \$18.2 million in the comparable three-month period of 2014. In the first three months of 2015, investment securities transactions resulted in net cash inflows of \$65.1 million, compared to inflows of \$3.8 million during the same period of 2014. Increased loan volume accounted for net cash outflows of \$44.2 million for the first three months of 2015, compared with \$15.0 million of net inflows for the same period of 2014. Purchases of premises and equipment resulted in a \$2.2 million cash outflow in the first three months of 2015, compared to outflows of \$2.8 million relating to premises and equipment in the comparable period of 2014, both resulting from the two large building projects currently underway to restore and remodel the main office of the Bank and headquarters of the Company, and to construct a new Home Mortgage Center. Cash inflows from loan pool participations were \$1.1 million during the first three months of 2015 compared to \$2.1 million during the same period of 2014.

Net cash used in financing activities in the first three months of 2015 was \$30.5 million, compared with net cash used of \$13.5 million for the same period of 2014. The largest financing cash outflows during the three months ended March 31, 2015 was the net decrease of \$15.0 million in FHLB borrowings, the decrease of \$8.5 million in federal funds purchased, and the use of \$1.3 million to pay dividends.

To further mitigate liquidity risk, the Bank has several sources of liquidity in place to maximize funding availability and increase the diversification of funding sources. The criteria for evaluating the use of these sources include volume concentration (percentage of liabilities), cost, volatility, and the fit with the current asset/liability management plan.

These acceptable sources of liquidity include:

- Federal Funds Lines
- FHLB Borrowings
- Brokered Deposits
- Brokered Repurchase Agreements
- Federal Reserve Bank Discount Window

#### Federal Funds Lines:

Routine liquidity requirements are met by fluctuations in the Bank's federal funds position. The principal function of these funds is to maintain short-term liquidity. Unsecured federal funds purchased lines are viewed as a volatile liability and are not used as a long-term funding solution, especially when used to fund long-term assets. Multiple correspondent relationships are preferable and federal funds sold exposure to any one customer is continuously monitored. The current federal funds purchased limit is 10% of total assets, or the amount of established federal funds lines, whichever is smaller. Currently, the Bank has unsecured federal funds lines totaling \$55.0 million, which lines are tested annually to ensure availability.

#### FHLB Borrowings:



FHLB borrowings provide both a source of liquidity and long-term funding for the Bank. Use of this type of funding is coordinated with both the strategic balance sheet growth projections and interest rate risk profile of the Bank. Factors that are taken into account when contemplating use of FHLB borrowings are the effective interest rate, the collateral requirements,

## Table of Contents

community investment program credits, and the implications and cost of having to purchase incremental FHLB stock. The current FHLB borrowing limit is 35% of total assets. As of March 31, 2015, the Bank had \$78.0 million in outstanding FHLB borrowings, leaving \$177.1 million available for liquidity needs, based on collateral capacity. These borrowings are secured by various real estate loans (residential, commercial and agricultural).

### Brokered Deposits:

The Bank has brokered certificate of deposit lines/deposit relationships available to help diversify its various funding sources. Brokered deposits offer several benefits relative to other funding sources, such as: maturity structures which cannot be duplicated in the current deposit market, deposit gathering which does not cannibalize the existing deposit base, the unsecured nature of these liabilities, and the ability to quickly generate funds. However, brokered deposits are often viewed as a volatile liability by banking regulators and market participants. This viewpoint, and the desire to not develop a large funding concentration in any one area outside of the Bank's core market area, is reflected in an internal policy stating that the Bank limit the use of brokered deposits as a funding source to no more than 10% of total assets. Board approval is required to exceed this limit. The Bank will also have to maintain a "well capitalized" standing to access brokered deposits, as an "adequately capitalized" rating would require an FDIC waiver to do so, and an "undercapitalized" rating would prohibit the Bank from using brokered deposits altogether.

### Brokered Repurchase Agreements:

Brokered repurchase agreements may be established with approved brokerage firms and banks. Repurchase agreements create rollover risk (the risk that a broker will discontinue the relationship due to market factors) and are not used as a long-term funding solution, especially when used to fund long-term assets. Collateral requirements and availability are evaluated and monitored. The current policy limit for brokered repurchase agreements is 10% of total assets. There were no outstanding brokered repurchase agreements at March 31, 2015.

### Federal Reserve Bank Discount Window:

The Federal Reserve Bank Discount Window is another source of liquidity, particularly during difficult economic times. The Bank has a borrowing capacity with the Federal Reserve Bank of Chicago limited by the amount of municipal securities pledged against the line. As of March 31, 2015, the Bank had municipal securities with an approximate market value of \$13.2 million pledged for liquidity purposes.

### Interest Rate Risk

The nature of the banking business, which involves paying interest on deposits at varying rates and terms and charging interest on loans at other rates and terms, creates interest rate risk. As a result, net interest margin and earnings and the market value of assets and liabilities are subject to fluctuations arising from the movement of interest rates. We manage several forms of interest rate risk, including asset/liability mismatch, basis risk and prepayment risk. A key management objective is to maintain a risk profile in which variations in net interest income stay within the limits and guidelines of the Bank's Asset/Liability Management Policy.

Like most financial institutions, our net income can be significantly influenced by a variety of external factors, including: overall economic conditions, policies and actions of regulatory authorities, the amounts of and rates at which assets and liabilities reprice, variances in prepayment of loans and securities other than those that are assumed, early withdrawal of deposits, exercise of call options on borrowings or securities, competition, a general rise or decline in interest rates, changes in the slope of the yield-curve, changes in historical relationships between indices (such as LIBOR and prime), and balance sheet growth or contraction. Our asset and liability committee seeks to manage interest rate risk under a variety of rate environments by structuring our balance sheet and off-balance-sheet positions in such a way that changes in interest rates do not have a large negative impact. The risk is monitored and managed within approved policy limits.

We use a third-party service to model and measure our exposure to potential interest rate changes. For various assumed hypothetical changes in market interest rates, numerous other assumptions are made, such as prepayment speeds on loans and securities backed by mortgages, the slope of the Treasury yield curve, the rates and volumes of our deposits, and the rates and volumes of our loans. This analysis measures the estimated change in net interest income in the event of hypothetical changes in interest rates. The following table presents our projected changes in net interest income for the various interest rate shock levels at March 31, 2015 and December 31, 2014.



Table of Contents

## Analysis of Net Interest Income Sensitivity

	Immediate Change in Rates			
	-200	-100	+100	+200
(dollars in thousands)				
March 31, 2015				
Dollar change	\$ (160 )	\$ 107	\$ (44 )	\$ 234
Percent change	(0.3 )%	0.2 %	(0.1 )%	0.4 %
December 31, 2014				
Dollar change	\$ (315 )	\$ 171	\$ (369 )	\$ (491 )
Percent change	(0.6 )%	0.3 %	(0.7 )%	(0.9 )%

As shown above, at March 31, 2015, the effect of an immediate and sustained 200 basis point increase in interest rates would be an increase our net interest income by approximately \$0.2 million. The effect of an immediate and sustained 200 basis point decrease in rates would decrease our net interest income by approximately \$0.2 million. These changes in net interest income under various interest rate scenarios are small relative to the overall level of net interest income. In fact, changes of this magnitude are well within the range of what would be considered neutral interest rate sensitivity. In the current low interest rate environment, model results of a 200 basis point drop in interest rates are of questionable value as many interest-bearing liabilities and interest-earning assets cannot re-price significantly lower than current levels. As part of a strategy to mitigate net interest margin compression in a low interest rate environment, management has incorporated interest rate floors on most newly originated floating rate loans. While incorporating interest rate floors on loans has been successful in maintaining our net interest margin in the current low rate environment, the coupon rates on these loans will lag when interest rates rise. These loans have floor rates that are between 0.0% and 2.0% above the fully indexed rate. Therefore, interest rates must rise up to 2.0% before some of these loans would experience an increase in the coupon rate.

Computations of the prospective effects of hypothetical interest rate changes were based on numerous assumptions. Actual values may differ from those projections set forth above. Further, the computations do not contemplate any actions we could have undertaken in response to changes in interest rates.

## Item 4. Controls and Procedures.

## Disclosure Controls and Procedures

Under supervision and with the participation of certain members of our management, including our chief executive officer and chief financial officer, we completed an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) as of March 31, 2015. Based on this evaluation, our chief executive officer and chief financial officer have concluded that the disclosure controls and procedures were effective as of the end of the period covered by this report with respect to timely communication to them and other members of management responsible for preparing periodic reports of material information required to be disclosed in this report as it relates to the Company and our consolidated subsidiaries.

The effectiveness of our or any system of disclosure controls and procedures is subject to certain limitations, including the exercise of judgment in designing, implementing, and evaluating the controls and procedures, the assumptions used in identifying the likelihood of future events, and the inability to eliminate misconduct completely. As a result, there can be no assurance that our disclosure controls and procedures will prevent all errors or fraud or ensure that all material information will be made known to appropriate management in a timely fashion. By their nature, our or any system of disclosure controls and procedures can provide only reasonable assurance regarding management's control objectives.

## Changes in Internal Control over Financial Reporting

There was no change in our internal control over financial reporting during the last fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

## Special Cautionary Note Regarding Forward-Looking Statements

This report contains certain “forward-looking statements” within the meaning of such term in the Private Securities Litigation Reform Act of 1995. We and our representatives may, from time to time, make written or oral statements that are “forward-looking” and provide information other than historical information. These statements involve known and unknown risks, uncertainties and other factors that may cause actual results to be materially different from any results, levels of activity,

Table of Contents

performance or achievements expressed or implied by any forward-looking statement. These factors include, among other things, the factors listed below.

Forward-looking statements, which may be based upon beliefs, expectations and assumptions of our management and on information currently available to management, are generally identifiable by the use of words such as “believe”, “expect”, “anticipate”, “should”, “could”, “would”, “plans”, “intend”, “project”, “estimate”, “forecast”, “may” or similar expressions. Forward-looking statements are subject to certain risks and uncertainties that could cause actual results to differ materially from those expressed in, or implied by, these statements. Readers are cautioned not to place undue reliance on any such forward-looking statements, which speak only as of the date made. Additionally, we undertake no obligation to update any statement in light of new information or future events, except as required under federal securities law.

Our ability to predict results or the actual effect of future plans or strategies is inherently uncertain. Factors that could have an impact on our ability to achieve operating results, growth plan goals and future prospects include, but are not limited to, the following:

- credit quality deterioration or pronounced and sustained reduction in real estate market values could cause an increase in our allowance for credit losses and a reduction in net earnings;
- the risks of mergers, including with Central Bancshares, including, without limitation, the related time and costs of implementing such transactions, integrating operations as part of these transactions and possible failures to achieve expected gains, revenue growth and/or expense savings from such transactions;
- our management’s ability to reduce and effectively manage interest rate risk and the impact of interest rates in general on the volatility of our net interest income;
- changes in the economic environment, competition, or other factors that may affect our ability to acquire loans or influence the anticipated growth rate of loans and deposits and the quality of the loan portfolio and loan and deposit pricing;
- fluctuations in the value of our investment securities;
- governmental monetary and fiscal policies;
- legislative and regulatory changes, including changes in banking, securities and tax laws and regulations and their application by our regulators (particularly with respect to the Dodd-Frank Act and the extensive regulations promulgated and to be promulgated thereunder, as well as the Basel III Rules, which became effective January 1, 2015), and changes in the scope and cost of FDIC insurance and other coverages;
- the ability to attract and retain key executives and employees experienced in banking and financial services;
- the sufficiency of the allowance for loan losses to absorb the amount of actual losses inherent in our existing loan portfolio;
- our ability to adapt successfully to technological changes to compete effectively in the marketplace;
- credit risks and risks from concentrations (by geographic area and by industry) within our loan portfolio;
- the effects of competition from other commercial banks, thrifts, mortgage banking firms, consumer finance companies, credit unions, securities brokerage firms, insurance companies, money market and other mutual funds, and other financial institutions operating in our markets or elsewhere or providing similar services;
- the failure of assumptions underlying the establishment of allowances for loan losses and estimation of values of collateral and various financial assets and liabilities;
- volatility of rate-sensitive deposits;
- operational risks, including data processing system failures or fraud;
- asset/liability matching risks and liquidity risks;
- the costs, effects and outcomes of existing or future litigation;
- changes in general economic or industry conditions, nationally or in the communities in which we conduct business;
- changes in accounting policies and practices, as may be adopted by state and federal regulatory agencies and the Financial Accounting Standards Board; and
- other factors and risks described under “Risk Factors” in our Annual Report on Form 10-K for the period ended December 31, 2014.

We qualify all of our forward-looking statements by the foregoing cautionary statements. Because of these risks and other uncertainties, our actual future results, performance or achievement, or industry results, may be materially different from the results indicated by these forward-looking statements. In addition, our past results of operations are not necessarily indicative of our future results.

Table of Contents

PART II – OTHER INFORMATION

Item 1. Legal Proceedings.

The Company and its subsidiaries are from time to time parties to various legal actions arising in the normal course of business. We believe that there are no threatened or pending proceedings, other than ordinary routine litigation incidental to the Company's business, against the Company or its subsidiaries, which, if determined adversely, would have a material adverse effect on the business or financial condition of the Company.

Item 1A. Risk Factors.

There have been no material changes from the risk factors set forth in Part I, Item 1A. "Risk Factors" of our Annual Report on Form 10-K for the period ended December 31, 2014. Please refer to that section of our Form 10-K for disclosures regarding the risks and uncertainties related to our business.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

Issuer Purchases of Equity Securities

We did not repurchase any of our equity securities during the quarter covered by this report.

On July 17, 2014, the board of directors of the Company approved a new share repurchase program, allowing for the repurchase of up to \$5.0 million of stock through December 31, 2016. The new repurchase program replaces the Company's prior repurchase program, pursuant to which the Company had repurchased approximately \$3.7 million of common stock since January 1, 2013. Pursuant to the program, the Company may continue to repurchase shares from time to time in the open market, and the method, timing and amounts of repurchase will be solely in the discretion of the Company's management. The repurchase program does not require the Company to acquire a specific number of shares. Therefore, the amount of shares repurchased pursuant to the program will depend on several factors, including market conditions, capital and liquidity requirements, and alternative uses for cash available. Of the \$5.0 million of stock authorized under the repurchase plan, \$3.8 million remained available for possible future repurchases as of March 31, 2015.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. Mine Safety Disclosures.

Not Applicable.

Item 5. Other Information.

None.



Table of Contents

## Item 6. Exhibits.

Exhibit Number	Description	Incorporated by Reference to:
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a)	Filed herewith
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a)	Filed herewith
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	Filed herewith
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	Filed herewith
101.INS	XBRL Instance Document	Filed herewith
101.SCH	XBRL Taxonomy Extension Schema Document	Filed herewith
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document	Filed herewith
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document	Filed herewith
101.LAB	XBRL Taxonomy Extension Label Linkbase Document	Filed herewith
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document	Filed herewith

Table of Contents

SIGNATURES

Pursuant to the requirements 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.

MIDWESTONE FINANCIAL GROUP, INC.

Dated: April 30, 2015

By: /s/ CHARLES N. FUNK  
Charles N. Funk  
President and Chief Executive Officer

By: /s/ GARY J. ORTALE  
Gary J. Ortale  
Executive Vice President and Chief Financial Officer