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**Heartland**
FINANCIAL USA, INC.

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March 4, 2009

Mr. Neil M. Barofsky
Special Inspector General
Office of the Special Inspector General
Troubled Asset Relief Program
1500 Pennsylvania Ave., N.W., Suite 1064
Washington, D.C. 20220

**Re: SIGTARP Response**

Dear Mr. Barofsky,

This letter is to respond to your request, by letter of February 6, 2009, for information relating to the application of TARP funds, and implementation of executive compensation requirements associated with the receipt of TARP funds, by Heartland Financial USA, Inc. ("Heartland").

Heartland applied to participate in the Capital Purchase Program (the "CPP") on November 12, 2008, received notice of approval for TARP CPP funding on December 11, 2008, and closed December 19, 2008 on the sale to the United States Department of the Treasury of 81,698 shares of its Fixed Rate Cumulative Perpetual Preferred Stock, Series B, together with warrants to purchase 609,687 shares of its common stock, for $81,698,000.

You have specifically requested the following information:

> *(1) A narrative response specifically outlining (a) your anticipated use of TARP funds; (b) whether the TARP funds were segregated from other institutional funds; (c) your actual use of TARP funds to date; and (d) your expected use of unspent TARP funds. In your response, please take into consideration your anticipated use of TARP funds at the time that you applied for such funds, or any actions that [sic] have taken that you would have not have been able to take absent the infusion of TARP funds.*

In response to this request, please be advised that:

(a) As further described below, Heartland anticipates using the additional capital and liquidity resulting from the receipt of TARP funds to support organic growth, support the acquisition of distressed institutions and to provide the capital cushion necessary to allow it to continue to operate and lend in a particularly challenging economy for the banking industry.

Heartland was, and is, well capitalized and not in need of additional capital to support its capital position. Nevertheless, prior to becoming aware of the TARP CPP program, Heartland had considered other means of raising equity capital in order to increase its capital position to support growth organically [redacted]

Heartland's subsidiary banks continue to pursue new customer relationships and opportunities to offer additional products and services to existing customers, including loans. Heartland has in the past and will continue to deploy capital to its subsidiary banks, as necessary to support their actual and prospective growth and operate them on a well capitalized basis. It is anticipated that TARP funds will be one source for providing this capital support to Heartland's subsidiary banks.

In furtherance of this effort, Heartland is developing or has implemented the following programs at its subsidiary banks:

- The Heartland Residential Loss Mitigation Program for loans held in portfolio at Heartland subsidiary banks. This program is designed to assist borrowers through a variety of loan modification measures designed to lower the borrower's monthly mortgage payments so as to increase the borrower's ability to stay in the home and avoid foreclosure.

- A low cost consumer loan program designed to encourage qualified borrowers to utilize the credit for purchases specifically in their local markets.

- Assisting in the implementation of Freddie/Fannie mortgage foreclosure relief programs in its role as servicer for loans that Heartland subsidiaries have sold to Freddie/Fannie but retains the servicing.

- Heartland subsidiary banks continue to be Small Business Administration preferred lenders and continue to utilize government guaranteed programs in order to strengthen and stimulate small business lending in Heartland markets.

[redacted]

Heartland's management also took notice of the instability in the banking industry and the potential for a prolonged economic downturn that could continue to have a significant adverse impact on the banking industry. The actions of the Treasury Department and the Federal Reserve Board have underscored these concerns. Management believes

Heartland has the resources to survive a prolonged economic downturn and, with the additional capital from the receipt of TARP funds, the ability to continue to operate and to continue to lend without restriction, even if the economic impact on the organization is greater than anticipated.

(b) The TARP funds were not segregated from other institutional funds.

(c) As indicated in response to (b) above, the TARP funds were not segregated and therefore cannot be traced to specific disbursements. However, following receipt of the TARP funds, Heartland did pay off and terminate a line of credit from a consortium of correspondent lenders, the terms of which could have restricted Heartland's operational flexibility in the current economic climate. To the extent the receipt of TARP funds has resulted in additional un-invested funds, those funds have been invested in short term investment vehicles until needed to enhance the capitalization of one or more subsidiary banks (b) (4) [redacted] Additionally, Heartland suspended planned dividends from its subsidiary banks for the 4th quarter of 2008 and the 1st quarter of 2009, and injected capital into certain subsidiary banks, increasing the capital at the subsidiary bank level by $11.8 million and when fully leveraged, increasing the banks lending capacity by $118 million.

(d) Heartland's anticipated use of TARP funds is as described in response to (a) above.

> *(2) Your specific plans, and the status of implementation of those plans, for addressing executive compensation requirements associated with the funding. Information provided regarding executive compensation should also include any assessments made of loan risks and their relationship to executive compensation; how limitations on executive compensation will be implemented in line with Department of Treasury guidelines; and whether any such limitations may be offset by other changes to other longer-term or deferred forms of executive compensation.*

None of Heartland's existing compensation plans provide for compensation that exceeded the original limitations set forth in the Interim Final Regulations adopted by the Department of Treasury. The Compensation/Nominating Committee (the "Committee"), in conjunction with the closing of Heartland's TARP CPP transaction and the Heartland Board of Directors approved generalized amendments applicable to any executive benefit plan designed to clarify that, to the extent a plan was inconsistent with those regulations, it was amended to conform to those regulations, and then obtained the specific consent of each of Heartland's five highest named executive officers to the amendment.

Heartland's existing executive compensation falls well within the requirements of the Interim Final Rule promulgated by the Treasury at 12 CFR Part 30 as it existed, and was incorporated into the securities purchase agreement by letter agreement with the Department of Treasury on December 19, 2008, as well as the additional interpretations under that Interim Final Rule issued in January 2009 and the February 4, 2009 Treasury notice (TG-15) as applied to institutions not in need of "exceptional assistance." In addition, no changes have been approved or made to offset the limitations imposed by these requirements.

Consistent with applicable regulations and the letter agreement dated December 19, 2008 with the Department of Treasury, the Committee has scheduled time at its March 2009 meeting to meet with Heartland's senior risk officer to review and discuss senior executive officer ("SEO") incentive compensation arrangements to ensure that the SEO incentive compensation arrangements do not encourage SEO's to take unnecessary and excessive risks, including loan risks.

Heartland has also been quite cognizant of compensation requirements stemming not only from the original TARPCPP letter agreement with the Department of Treasury but also more recently as outlined by Secretary Geithner in his report on the Financial Stability Plan ("Plan") on February 10, 2009 as well as in Title VII of the American Recovery and Reinvestment Tax Act ("Act") of 2009. In this regard, we understand that certain compensation arrangements permissible under the letter agreement may not be permissible under the provisions of the Act, including those that require elimination of incentive plans for the five most highly paid employees and the elimination of severance packages for officers. We also have monitored the Securities and Exchange Commission's guidance on the advisory vote on existing executive compensation plans. Heartland will monitor upcoming regulatory commentary and guidance to determine if changes will be needed to existing executive compensation and the timing of these changes.

In preparation for this response, we have segregated all TARP documentation, whether in physical or electronic format for future use as necessary.

I certify the accuracy of all statements and representations made in this letter subject to the requirements and penalties set forth in Title 18, United States Code, Section 1001.

Sincerely,

John K. Schmidt
Executive Vice President
Chief Operating Officer and Chief Financial Officer