

HORIZON BANCORP /IN/  
Form 10-Q  
November 12, 2009

**Table of Contents**

**HORIZON BANCORP**  
**FORM 10-Q**  
**United States**  
**SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**  
**QUARTERLY REPORT UNDER SECTION 13 OR 15 (d) OF**  
**THE SECURITIES EXCHANGE ACT OF 1934**  
**For the quarterly period ended September 30, 2009**  
**Commission file number 0-10792**  
**HORIZON BANCORP**  
(Exact name of registrant as specified in its charter)

**Indiana**

**35-1562417**

(State or other jurisdiction of incorporation or organization)

(I.R. S. Employer Identification No.)

**515 Franklin Square, Michigan City, Indiana**

**46360**

(Address of principal executive offices)

(Zip Code)

Registrant's telephone number, including area code: **(219) 879-0211**

Former name, former address and former fiscal year, if changed since last report: **N/A**

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

Smaller reporting  
company

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 3,273,881 at November 12, 2009.

**HORIZON BANCORP**  
**FORM 10-Q**  
**INDEX**

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Condensed Consolidated Balance Sheets 3

Condensed Consolidated Statements of Income 4

Condensed Consolidated Statements of Stockholders' Equity 5

Condensed Consolidated Statements of Cash Flows 6

Notes to Condensed Consolidated Financial Statements 7

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations 23

Item 3. Quantitative and Qualitative Disclosures about Market Risk 40

Item 4T. Controls and Procedures 40

PART II. OTHER INFORMATION

Item 1. Legal Proceedings 41

Item 1A. Risk Factors 41

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds 45

Item 3. Defaults Upon Senior Securities 45

Item 4. Submission of Matters to a Vote of Security Holders 45

Item 5. Other Information 45

Item 6. Exhibits 46

Signatures 47

Index To Exhibits 48

EX-31.1

EX-31.2

EX-32

**Table of Contents****PART 1 FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****HORIZON BANCORP AND SUBSIDIARIES****Condensed Consolidated Balance Sheets**

(Dollar Amounts in Thousands)

	<b>September 30 2009 (Unaudited)</b>	<b>December 31 2008</b>
<b>Assets</b>		
Cash and due from banks	\$ 10,848	\$ 36,001
Interest-bearing deposits	4,464	2,679
Investment securities, available for sale	333,031	301,638
Investment securities, held to maturity	15,661	1,630
Loans held for sale	6,119	5,955
Loans, net of allowance for loan losses of \$13,924 and \$11,410	861,785	870,557
Premises and equipment	29,972	28,280
Federal Reserve and Federal Home Loan Bank stock	13,225	12,625
Goodwill	5,787	5,787
Other intangible assets	1,521	1,751
Interest receivable	6,222	5,708
Cash value life insurance	22,966	22,451
Other assets	9,623	11,795
<b>Total assets</b>	<b>\$1,321,224</b>	<b>\$1,306,857</b>
<b>Liabilities</b>		
Deposits		
Non-interest bearing	\$ 87,725	\$ 83,642
Interest bearing	770,272	757,527
<b>Total deposits</b>	<b>857,997</b>	<b>841,169</b>
Borrowings	311,884	324,383
Subordinated debentures	27,837	27,837
Interest payable	1,304	1,910
Other liabilities	8,369	8,208
<b>Total liabilities</b>	<b>1,207,391</b>	<b>1,203,507</b>
<b>Commitments and contingent liabilities</b>		
<b>Stockholders Equity</b>		
Preferred stock, no par value, \$1,000 liquidation value		
Authorized, 1,000,000 shares		
Issued 25,000 shares		
Common stock, \$.2222 stated value	24,267	24,154
Authorized, 22,500,000 shares		
Issued, 3,271,631 and 3,254,482 shares	1,118	1,114
Additional paid-in capital	9,974	9,650

Edgar Filing: HORIZON BANCORP /IN/ - Form 10-Q

Retained earnings	<b>72,255</b>	67,804
Accumulated other comprehensive income	<b>6,219</b>	628
Total stockholders' equity	<b>113,833</b>	103,350
Total liabilities and stockholders' equity	<b>\$1,321,224</b>	\$1,306,857

See notes to condensed consolidated financial statements

3

---

**Table of Contents****HORIZON BANCORP AND SUBSIDIARIES****Condensed Consolidated Statements of Income**

(Dollar Amounts in Thousands, Except Per Share Data)

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30</b>		<b>September 30</b>	
	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
	<b>(Unaudited)</b>	<b>(Unaudited)</b>	<b>(Unaudited)</b>	<b>(Unaudited)</b>
<b>Interest Income</b>				
Loans receivable	<b>\$13,797</b>	\$14,202	<b>\$43,793</b>	\$ 43,763
Investment securities				
Taxable	<b>2,673</b>	2,172	<b>8,333</b>	6,934
Tax exempt	<b>1,015</b>	791	<b>2,882</b>	2,490
Total interest income	<b>17,485</b>	17,165	<b>55,008</b>	53,187
<b>Interest Expense</b>				
Deposits	<b>3,528</b>	4,261	<b>11,517</b>	15,552
Borrowed funds	<b>2,897</b>	3,108	<b>9,011</b>	8,782
Subordinated debentures	<b>341</b>	393	<b>1,082</b>	1,192
Total interest expense	<b>6,766</b>	7,762	<b>21,610</b>	25,526
<b>Net Interest Income</b>	<b>10,719</b>	9,403	<b>33,398</b>	27,661
Provision for loan losses	<b>3,416</b>	3,137	<b>9,903</b>	5,405
<b>Net Interest Income after Provision for Loan Losses</b>	<b>7,303</b>	6,266	<b>23,495</b>	22,256
<b>Other Income</b>				
Service charges on deposit accounts	<b>972</b>	1,065	<b>2,880</b>	2,975
Wire transfer fees	<b>201</b>	155	<b>709</b>	382
Interchange fees	<b>514</b>	216	<b>1,358</b>	618
Fiduciary activities	<b>745</b>	911	<b>2,486</b>	2,817
Gain (loss) on sale of securities	<b>422</b>		<b>422</b>	(15)
Gain on sale of mortgage loans	<b>1,277</b>	657	<b>4,861</b>	2,122
Mortgage servicing net of impairment	<b>35</b>	3	<b>(131)</b>	8
Increase in cash surrender value of bank owned life insurance	<b>206</b>	252	<b>547</b>	701
Death benefit on officer life insurance				538
Other income	<b>170</b>	92	<b>420</b>	316
Total other income	<b>4,542</b>	3,351	<b>13,552</b>	10,462

**Other Expenses**

Salaries and employee benefits	<b>4,539</b>	4,203	<b>14,264</b>	12,698
Net occupancy expenses	<b>941</b>	944	<b>2,872</b>	2,834
Data processing	<b>419</b>	391	<b>1,194</b>	1,073
Professional fees	<b>316</b>	263	<b>1,021</b>	803
Outside services and consultants	<b>366</b>	328	<b>1,043</b>	940
Loan expense	<b>631</b>	593	<b>1,841</b>	1,603
FDIC insurance expense	<b>400</b>	146	<b>1,751</b>	404
Other (gains) losses	<b>(25)</b>	25	<b>442</b>	267
Other Expenses	<b>1,342</b>	1,390	<b>3,826</b>	3,927
<b>Total other expenses</b>	<b>8,929</b>	8,283	<b>28,254</b>	24,549
<b>Income Before Income Tax</b>	<b>2,916</b>	1,334	<b>8,793</b>	8,169
Income tax expense	<b>559</b>	2	<b>1,737</b>	1,319
<b>Net Income</b>	<b>2,357</b>	1,332	<b>7,056</b>	6,850
Preferred stock dividend and discount accretion	<b>(351)</b>		<b>(1,051)</b>	
<b>Net Income Available to Common Shareholders</b>	<b>\$ 2,006</b>	\$ 1,332	<b>\$ 6,005</b>	\$ 6,850
<b>Basic Earnings Per Share</b>	<b>\$ 0.62</b>	\$ 0.42	<b>\$ 1.86</b>	\$ 2.14
<b>Diluted Earnings Per Share</b>	<b>\$ 0.61</b>	\$ 0.41	<b>\$ 1.84</b>	\$ 2.11
See notes to condensed consolidated financial statements				

**Table of Contents****Horizon Bancorp and Subsidiaries****Condensed Consolidated Statement of Stockholders Equity****(Unaudited)**

(Table Dollar Amounts in Thousands, Except Per Share Data)

	<b>Preferred Stock</b>	<b>Common Stock</b>	<b>Additional Paid-in Capital</b>	<b>Comprehensive Income</b>	<b>Retained Earnings</b>	<b>Accumulated Other Comprehensive Income</b>	<b>Total</b>
<b>Balances, December 31, 2008</b>	\$ 24,154	\$ 1,114	\$ 9,650		\$ 67,804	\$ 628	\$ 103,350
Net income				\$ 7,056	7,056		7,056
Amortization of discount on preferred stock	113				(113)		
Other comprehensive income (loss), net of tax:							
Unrealized gain on securities				5,523		5,523	5,523
Unrealized gain on derivative instruments				68		68	68
Comprehensive income				\$ 12,647			
Amortization of unearned compensation			147				147
Issuance of restricted shares		3	101				104
Exercise of stock options		1	31				32
Tax benefit related to stock options			16				16
Stock option expense			29				29
Cash dividends on preferred stock (5.00%)					(1,051)		(1,051)
Cash dividends on common stock (\$.51 per share)					(1,441)		(1,441)
<b>Balances, September 30, 2009</b>	<b>\$ 24,267</b>	<b>\$ 1,118</b>	<b>\$ 9,974</b>		<b>\$ 72,255</b>	<b>\$ 6,219</b>	<b>\$ 113,833</b>



See notes to condensed consolidated financial statements

**Table of Contents****HORIZON BANCORP AND SUBSIDIARIES****Condensed Consolidated Statements of Cash Flows**

(Dollar Amounts in Thousands)

	<b>Nine Months Ended September 30</b>	
	<b>2009</b>	<b>2008</b>
	<b>(Unaudited)</b>	<b>(Unaudited)</b>
<b>Operating Activities</b>		
Net income	\$ 7,056	\$ 6,850
Items not requiring (providing) cash		
Provision for loan losses	9,903	5,405
Depreciation and amortization	1,733	1,743
Share based compensation	29	28
Mortgage servicing rights impairment	124	5
Deferred income tax	(576)	(555)
Premium amortization on securities available for sale, net	491	239
(Gain) loss on sale of investment securities	(422)	15
Gain on sale of mortgage loans	(4,861)	(1,929)
Proceeds from sales of loans	270,354	108,659
Loans originated for sale	(267,847)	(103,152)
Increase in cash surrender value of life insurance	(515)	104
Loss on sale of other real estate owned	13	
Net change in		
Interest receivable	(514)	379
Interest payable	(606)	(490)
Other assets	961	(1,479)
Other liabilities	247	472
Net cash provided by operating activities	15,570	16,294
<b>Investing Activities</b>		
Net change in interest-bearing deposits	(1,785)	(937)
Purchases of securities available for sale	(89,034)	(38,751)
Proceeds from sales, maturities, calls, and principal repayments of securities available for sale	66,068	41,487
Purchase of securities held to maturity	(14,031)	(815)
Proceeds from maturities of securities held to maturity		85
Purchases of FRB Stock	(600)	
Net change in loans	(9,115)	(10,822)
Proceeds on sale of OREO and repossessed assets	8,833	
Recoveries on loans previously charged-off		799
Purchases of premises and equipment	(3,048)	(3,141)
Proceeds from sale of loans transferred to held for sale		37,695
Gain on sale of loans transferred to held for sale		(193)
Net cash provided by (used in) investing activities	(42,712)	25,407

**Financing Activities**

Net change in		
Deposits	<b>16,828</b>	(144,242)
Borrowings	<b>(12,499)</b>	69,590
Proceeds from issuance of stock	<b>136</b>	35
Tax benefit from issuance of stock	<b>16</b>	8
Dividends paid on preferred shares	<b>(1,051)</b>	
Dividends paid on common shares	<b>(1,441)</b>	(1,593)
Net cash provided by (used in) financing activities	<b>1,989</b>	(76,202)
<b>Net Change in Cash and Cash Equivalent</b>	<b>(25,153)</b>	<b>(34,501)</b>
<b>Cash and Cash Equivalents, Beginning of Period</b>	<b>36,001</b>	<b>55,029</b>
<b>Cash and Cash Equivalents, End of Period</b>	<b>\$ 10,848</b>	<b>\$ 20,528</b>
<b>Additional Cash Flows Information</b>		
Interest paid	<b>\$ 22,216</b>	<b>\$ 26,016</b>
Income taxes paid	<b>2,005</b>	1,405
Transfer of loans to other real estate owned	<b>7,578</b>	1,223
See notes to condensed consolidated financial statements		

Table of Contents**HORIZON BANCORP AND SUBSIDIARIES****Notes to Condensed Consolidated Financial Statements**

(Table Dollar Amounts in Thousands, Except Per Share Data)

**Note 1 Accounting Policies**

The accompanying consolidated financial statements include the accounts of Horizon Bancorp ( Horizon or the Company ) and its wholly-owned subsidiaries, including Horizon Bank, N.A. ( Bank ). All inter-company balances and transactions have been eliminated. The results of operations for the periods ended September 30, 2009 and September 30, 2008 are not necessarily indicative of the operating results for the full year of 2009 or 2008. The accompanying unaudited condensed consolidated financial statements reflect all adjustments that are, in the opinion of Horizon s management, necessary to fairly present the financial position, results of operations and cash flows of Horizon for the periods presented. Those adjustments consist only of normal recurring adjustments.

Certain information and note disclosures normally included in Horizon s annual financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted. These consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in Horizon s Annual Report on Form 10-K for 2008 filed with the Securities and Exchange Commission. The consolidated balance sheet of Horizon as of December 31, 2008 has been derived from the audited balance sheet of Horizon as of that date.

Basic earnings per share is computed by dividing net income available to common shareholders (net income less dividend requirements for preferred stock and accretion of preferred stock discount) by the weighted-average number of common shares outstanding. Diluted earnings per share reflect the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. In August 2002, substantially all of the participants in Horizon s Stock Option and Stock Appreciation Rights Plans voluntarily entered into an agreement with Horizon to cap the value of their stock appreciation rights ( SARS ) at \$14.67 per share and cease any future vesting of the SARS. These agreements with option holders make it more advantageous to exercise an option rather than a SAR whenever Horizon s stock price exceeds \$14.67 per share, therefore the option becomes potentially dilutive at \$14.67 per share or higher. The following table shows computation of basic and diluted earnings per share.

	<b>Three months ended September 30</b>		<b>Nine months ended September 30</b>	
	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
	<b>(Unaudited)</b>	<b>(Unaudited)</b>	<b>(Unaudited)</b>	<b>(Unaudited)</b>
<b>Basic earnings per share</b>				
Net income	\$ 2,357	\$ 1,332	\$ 7,056	\$ 6,850
Less: Preferred stock dividends and accretion of discount	351		1,051	
Net income available to common shareholders	\$ 2,006	\$ 1,332	\$ 6,005	\$ 6,850
Weighted average common shares outstanding	3,245,505	3,209,482	3,221,622	3,208,362
<b>Basic earnings per share</b>	\$ 0.62	\$ 0.42	\$ 1.86	\$ 2.14
<b>Diluted earnings per share</b>	\$ 2,006	\$ 1,332	\$ 6,005	\$ 6,850

Net income available to common  
shareholders

Weighted average common shares outstanding	<b>3,245,505</b>	3,209,482	<b>3,221,622</b>	3,208,362
Effect of dilutive securities:				
Restricted stock	<b>20,572</b>	34,257	<b>41,895</b>	26,903
Stock options	<b>7,665</b>	11,670	<b>6,637</b>	10,943
Weighted average shares outstanding	<b>3,273,742</b>	3,255,409	<b>3,270,154</b>	3,246,208
<b>Diluted earnings per share</b>	<b>\$ 0.61</b>	\$ 0.41	<b>\$ 1.84</b>	\$ 2.11

7

---

**Table of Contents****HORIZON BANCORP AND SUBSIDIARIES****Notes to Condensed Consolidated Financial Statements**

(Table Dollar Amounts in Thousands, Except Per Share Data)

At September 30, 2009 and 2008 there were 30,800 shares and 28,000 shares that were not included in the computation of diluted earnings per share because they were non-dilutive. Warrants to purchase 212,104 shares at September 30, 2009 were not included in the computation of diluted earnings per share because the effect would be non-dilutive.

Horizon has share-based employee compensation plans, which are described in the notes to the financial statements included in the December 31, 2008 Annual Report on Form 10-K.

**Reclassifications**

Certain reclassifications have been made to the 2008 consolidated financial statements to be comparable to 2009.

These reclassifications had no effect on net income.

**Note 2 Securities**

The fair value of securities is as follows:

	<b>Amortized Cost</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>	<b>Fair Value</b>
<b>September 30, 2009</b> (Unaudited)				
<b>Available for sale</b>				
U.S. Treasury and federal agencies	\$ 19,722	\$ 571	\$	\$ 20,293
State and municipal	96,371	4,585	(233)	100,723
Federal agency collateralized mortgage obligations	49,608	625	(299)	49,934
Federal agency mortgage-backed pools	156,300	5,328	(1)	161,627
Corporate notes	710	6	(262)	454
Total available for sale investment securities	\$322,711	\$11,115	\$ (795)	\$333,031
<b>Held to maturity, State and Municipal</b>	<b>\$ 15,661</b>	<b>\$ 4</b>	<b>\$ (1)</b>	<b>\$ 15,664</b>
<b>December 31, 2008</b>	<b>Amortized Cost</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>	<b>Fair Value</b>
<b>Available for sale</b>				
U.S. Treasury and federal agencies	\$ 23,661	\$ 1,253	\$	\$ 24,914
State and municipal	88,282	804	(2,101)	86,985
Federal agency collateralized mortgage obligations	13,063	223	(335)	12,951
Federal agency mortgage-backed pools	174,227	2,374	(212)	176,389
Corporate notes	587		(188)	399
Total available for sale investment securities	\$299,820	\$ 4,654	\$(2,836)	\$301,638
<b>Held to maturity, State and Municipal</b>	<b>\$ 1,630</b>	<b>\$ 4</b>	<b>\$</b>	<b>\$ 1,634</b>

Based on evaluation of available evidence, including recent changes in market interest rates, credit rating information, and information obtained from regulatory filings, management believes the declines in fair value for these securities are temporary. While these securities are held in the available for sale portfolio, Horizon intends and has the ability to

hold them until the earlier of a recovery in fair value or maturity.

Should the impairment of any of these securities become other than temporary, the cost basis of the investment will be reduced and the resulting loss recognized in net income in the period the other-than-

**Table of Contents****HORIZON BANCORP AND SUBSIDIARIES****Notes to Condensed Consolidated Financial Statements**

(Table Dollar Amounts in Thousands, Except Per Share Data)

temporary impairment is identified. At September 30, 2009, no individual investment security had an unrealized loss that was determined to be other-than-temporary.

The unrealized losses on the Company's investments in securities of state and municipal, federal agency collateralized mortgage obligations, and federal agency mortgage-backed pools were caused by interest rate increases and not a decline in credit quality. The contractual terms of those investments do not permit the issuer to settle the securities at a price less than the amortized cost basis of the investments or the Company expects to recover the amortized cost basis over the term of the securities. Because the Company does not intend to sell the investments and it is not likely that the Company will be required to sell the investments before recovery of their amortized cost basis, which may be maturity, the Company did not consider those investments to be other-than-temporarily impaired at September 30, 2009.

The amortized cost and fair value of securities available for sale and held to maturity at September 30, 2009 and December 31, 2008, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

	September 30, 2009 (Unaudited)		December 31, 2008	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
<b>Available for sale</b>				
Within one year	\$ 2,642	\$ 2,696	\$ 1,182	\$ 1,190
One to five years	21,067	21,815	10,569	10,926
Five to ten years	37,779	39,192	28,701	28,664
After ten years	55,315	57,767	72,078	71,518
	116,803	121,470	112,530	112,298
Federal agency collateralized mortgage obligations	49,608	49,934	13,063	12,951
Federal agency mortgage-backed pools	156,300	161,627	174,227	176,389
Total available for sale investment securities	\$ 322,711	\$ 333,031	\$ 299,820	\$ 301,638
<b>Held to maturity</b>				
Within one year	\$ 15,371	\$ 15,372	\$ 90	\$ 91
One to five years	290	292	1,540	1,543
Total held to maturity investment securities	\$ 15,661	\$ 15,664	\$ 1,630	\$ 1,634



**Table of Contents****HORIZON BANCORP AND SUBSIDIARIES****Notes to Condensed Consolidated Financial Statements**

(Table Dollar Amounts in Thousands, Except Per Share Data)

The following table shows investments gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position.

September 30, 2009 (Unaudited)	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
State and municipal	\$2,416	\$ (33)	\$3,430	\$ (201)	\$ 5,846	\$ (234)
Federal agency collateralized mortgage obligations	5,745	(163)	3,104	(136)	8,849	(299)
Federal agency mortgage-backed pools			44	(1)	44	(1)
Corporate notes			325	(262)	325	(262)
Total temporarily impaired securities	\$8,161	\$ (196)	\$6,903	\$ (600)	\$15,064	\$ (796)

December 31, 2008	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
State and municipal	\$47,215	\$ (1,973)	\$ 2,342	\$ (128)	\$49,557	\$ (2,101)
Federal agency collateralized mortgage obligations	4,026	(335)			4,026	(335)
Federal agency mortgage-backed pools	24,753	(161)	6,145	(51)	30,898	(212)
Corporate notes	399	(188)			399	(188)
Total temporarily impaired securities	\$76,393	\$ (2,657)	\$ 8,487	\$ (179)	\$ 84,880	\$ (2,836)

Information regarding security proceeds, gross gains and gross losses are presented below.

	Three months ended September 30		
	2009	2008	
<b>Sales of securities available for sale (Unaudited)</b>			
Proceeds	\$ 12,880	\$	
Gross gains	422		
Gross losses			
		Nine months ended September 30	
		2009	2008

**Sales of securities available for sale (Unaudited)**

Proceeds		<b>\$ 12,880</b>	\$ 30
Gross gains		<b>422</b>	
Gross losses			(15)

10

---

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**  
**Notes to Condensed Consolidated Financial Statements**  
(Table Dollar Amounts in Thousands, Except Per Share Data)

**Note 3 Loans**

	September 30, 2009 (Unaudited)	December 31 2008
Commercial	\$ 312,573	\$ 310,842
Residential mortgage	142,568	167,766
Mortgage warehouse	145,270	123,287
Installment	275,299	280,072
	<b>875,709</b>	881,967
Allowance for loan losses	<b>(13,924)</b>	(11,410)
<b>Total loans</b>	<b>\$ 861,785</b>	<b>\$ 870,557</b>

**Note 4 Allowance for Loan Losses**

	September 30, 2009 (Unaudited)	September 30, 2008 (Unaudited)
Balances, beginning of period	\$ 11,410	\$ 9,791
Provision for losses	9,903	5,405
Recoveries on loans	952	799
Loans charged off	<b>(8,341)</b>	(5,470)
<b>Balances, end of period</b>	<b>\$ 13,924</b>	<b>\$ 10,525</b>

**Note 5 Non-performing Assets**

	September 30, 2009 (Unaudited)	December 31 2008
<b>Non-performing loans</b>		
Commercial	\$ 9,235	\$ 5,167
Residential mortgage	4,926	1,904
Mortgage warehouse		
Installment	2,312	792
<b>Total non-performing loans</b>	<b>16,473</b>	<b>7,863</b>
<b>Other real estate owned and repossessed collateral</b>		
Commercial		
Residential mortgage	1,671	2,874

Mortgage warehouse Installment	142	207
<b>Total other real estate owned and repossessed collateral</b>	<b>1,813</b>	<b>3,081</b>
<b>Total non-performing assets</b>	<b>\$ 18,286</b>	<b>\$ 10,944</b>

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**  
**Notes to Condensed Consolidated Financial Statements**  
(Table Dollar Amounts in Thousands, Except Per Share Data)

**Note 6 Derivative financial instruments**

***Cash Flow Hedges***

As a strategy to maintain acceptable levels of exposure to the risk of changes in future cash flow due to interest rate fluctuations, the Company entered into interest rate swap agreements for a portion of its floating rate debt. The agreements provide for the Company to receive interest from the counterparty at three month LIBOR and to pay interest to the counterparty at a weighted average fixed rate of 5.38% on a notional amount of \$22.0 million at September 30, 2009. Under the agreements, the Company pays or receives the net interest amount monthly, with the monthly settlements included in interest expense.

Management has designated the interest rate swap agreement as a cash flow hedging instrument. For derivative instruments that are designated and qualify as a cash flow hedge, the effective portion of the gain or loss on the derivative is reported as a component of the other comprehensive income and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Gains and losses on the derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings. At September 30, 2009 the Company's cash flow hedge was effective and is not expected to have a significant impact the Company's net income over the next 12 months.

***Fair Value Hedges***

Fair value hedges are intended to reduce the interest rate risk associated with the underlying hedged item. The Company enters into fixed rate loan agreements as part of its lending policy. To mitigate the risk of changes in fair value based on fluctuations in interest rates, the Company has entered into interest rate swap agreements on individual loans, converting the fixed rate loans to a variable rate. For derivative instruments that are designated and qualify as a fair value hedge, the gain or loss on the derivative as well as the offsetting gain or loss on the hedged item attributable to the hedged risk are recognized in current earnings. At September 30, 2009 the Company's fair value hedges were effective and are not expected to have a significant impact the Company's net income over the next 12 months. The change in fair value of both the hedge instruments and the underlying loan agreements are recorded as gains or losses in interest income. The fair value hedges are considered to be highly effective and any hedge ineffectiveness was deemed not material. The notional amounts of the loan agreements being hedged were \$25.7 million at September 30, 2009.

***Other Derivative Instruments***

The Company enters into non-hedging derivatives in the form of mortgage loan forward sale commitments with investors and commitments to originate mortgage loans as part of its mortgage banking business. At September 30, 2009 the Company's fair value of these derivatives were recorded and over the next 12 months are not expected to have a significant impact the Company's net income.

The change in fair value of both the forward sale commitments and commitments to originate mortgage loans were recorded and the net gains or losses included in the Company's gain on sale of loans.

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**  
**Notes to Condensed Consolidated Financial Statements**  
(Table Dollar Amounts in Thousands, Except Per Share Data)

The following tables summarize the fair value of derivative financial instruments utilized by Horizon Bancorp:

Derivatives designated as  hedging instruments	Asset Derivative September 30, 2009 (Unaudited)		Liability Derivatives September 30, 2009 (Unaudited)	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Interest rate contracts	Loans	\$ 1,287	Other liabilities	\$ 1,287
Interest rate contracts			Other liabilities	746
<b>Total derivatives designated as hedging instruments</b>		1,287		2,033
<b>Derivatives not designated as hedging instruments</b>				
Mortgage loan contracts	Other assets	366	Other liabilities	(42)
<b>Total derivatives not designated as hedging instruments</b>		366		(42)
<b>Total derivatives</b>		\$ 1,653		\$ 1,991

The effect of the derivative instruments on the consolidated statement of income for the three and nine-month periods ended is as follows:

Derivative in cash flow hedging relationship	Amount of Gain Recognized in Other Comprehensive Income on Derivative (Effective Portion)	
	Three Months Ended September 30, 2009 (Unaudited)	Nine Months Ended September 30, 2009 (Unaudited)
Interest rate contracts	\$ (564)	\$ 68
<b>Total</b>	\$ (564)	\$ 68



**Table of Contents****HORIZON BANCORP AND SUBSIDIARIES****Notes to Condensed Consolidated Financial Statements**

(Table Dollar Amounts in Thousands, Except Per Share Data)

FASB Accounting Standards Codification ( ASC ) Topic 820-10-20 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Topic 820-10-55 establishes a fair value hierarchy that emphasizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value.

Derivative in fair value hedging relationship	Location of Gain (Loss) Recognized on Derivative	Amount of Gain (Loss) Recognized on Derivative	
		Three Months Ended Sept. 30, 2009 (Unaudited)	Nine Months Ended Sept 30, 2009 (Unaudited)
Interest rate contracts	Interest income loans	\$ 1,847	\$ (419)
Interest rate contracts	Interest income loans	(1,847)	419
<b>Total</b>		\$	\$

Derivative in fair value hedging	Location of Gain (Loss) Recognized on Derivative	Amount of Gain (Loss) Recognized on Derivative	
		Three Months Ended Sept 30, 2009 (Unaudited)	Nine Months Ended Sept 30, 2009 (Unaudited)
Mortgage contracts	Other income gain on sale of loans	\$ 553	\$ 177
<b>Total</b>		\$ 553	\$ 177

**Note 7 Disclosures about fair value of assets and liabilities**

The Fair Value Measurements topic of the FASB ASC defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. There are three levels of inputs that may be used to measure fair value:

**Level 1** Quoted prices in active markets for identical assets or liabilities

**Level 2**



Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities

**Level 3** Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities

Following is a description of the valuation methodologies used for instruments measured at fair value on a recurring basis and recognized in the accompanying financial statements, as well as the general classification of such instruments pursuant to the valuation hierarchy.

***Available for sale securities***

When quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated by using pricing

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**

**Notes to Condensed Consolidated Financial Statements**

(Table Dollar Amounts in Thousands, Except Per Share Data)

models, quoted prices of securities with similar characteristics or discounted cash flows. Level 2 securities include, U.S. Treasury and federal agency securities, state and municipal securities, federal agency mortgage obligations and mortgage-backed pools, and corporate notes. Level 2 securities are valued by a third party pricing service commonly used in the banking industry utilizing observable inputs. Observable inputs include dealer quotes, market spreads, cash flow analysis, the U.S. Treasury yield curve, trade execution data, market consensus prepayment spreads and available credit information and the bond's terms and conditions. The pricing provider utilizes evaluated pricing models that vary based on asset class. These models incorporate available market information including quoted prices of securities with similar characteristics and, because many fixed-income securities do not trade on a daily basis, apply available information through processes such as benchmark curves, benchmarking of like securities, sector grouping, and matrix pricing. In addition, model processes, such as an option adjusted spread model is used to develop prepayment and interest rate scenarios for securities with prepayment features.

***Hedged loans***

Certain fixed rate loans have been converted to variable rate loans through entering into interest rate swap agreements. Fair value of those fixed rate loans is based on discounting estimated cash flows using interest rates determined by a respective interest rate swap agreement. Loans are classified within Level 3 of the valuation hierarchy based on the unobservable inputs used.

***Interest rate swap agreements***

The fair value is estimated by a third party using inputs that are primarily unobservable and cannot be corroborated by observable market data and, therefore, are classified within Level 3 of the valuation hierarchy.

**Table of Contents****HORIZON BANCORP AND SUBSIDIARIES****Notes to Condensed Consolidated Financial Statements**

(Table Dollar Amounts in Thousands, Except Per Share Data)

The following table presents the fair value measurements of assets and liabilities recognized in the accompanying financial statements measured at fair value on a recurring basis and the level within the FASB ASC fair value hierarchy in which the fair value measurements fall at the following:

	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>September 30, 2009</b> (Unaudited)				
Available-for-sale securities				
U.S. Treasury and federal agencies	\$ 20,293	\$	\$ 20,293	\$
State and municipal	100,723		100,723	
Federal agency collateralized mortgage obligations	49,934		49,934	
Federal agency mortgage-backed pools	161,627		161,627	
Corporate notes	454		454	
Total available-for-sale securities	333,031		333,031	
Hedged loans	26,971			26,971
Forward sale commitments	366			366
Interest rate swap agreements	(2,033)			(2,033)
Commitments to originate loans	42			42
<b>December 31, 2008</b>				
Available-for-sale securities	\$ 301,638	\$	\$ 301,638	\$
Hedged loans	25,033			25,033
Forward sale commitments	670			670
Interest rate swap agreements	(2,557)			(2,557)
Commitments to originate loans	(438)			(438)
<b>September 30, 2008</b> (Unaudited)				
Available-for-sale securities	\$ 230,107	\$ 1,418	\$ 228,689	\$
Hedged loans	18,814			18,814
Interest rate swap agreements	(35)			(35)

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**  
**Notes to Condensed Consolidated Financial Statements**  
(Table Dollar Amounts in Thousands, Except Per Share Data)

The following is a reconciliation of the beginning and ending balances of recurring fair value measurements recognized in the accompanying condensed consolidated balance sheet using significant unobservable (level 3) inputs (Unaudited):

	<b>Hedged Loans</b>	<b>Forward Sale Commitments</b>	<b>Interest Rate Swaps</b>	<b>Commitments to Originate Loans</b>
<b>Beginning balance December 31, 2008</b>	\$ 25,033	\$ 670	\$ (2,557)	\$ (438)
Total realized and unrealized gains and losses				
Included in net income	24	(226)	(24)	258
Included in other comprehensive income, gross			(73)	
Purchases, issuances, and settlements	2,901			
Principal payments	(167)			
<b>Ending balance March 31, 2009</b>	27,791	444	(2,654)	(180)
Total realized and unrealized gains and losses				
Included in net income	(584)	(214)	584	37
Included in other comprehensive income, gross			194	
Principal payments	(190)			
<b>Ending balance June 30, 2009</b>	27,017	230	(1,876)	(143)
Total realized and unrealized gains and losses				
Included in net income	141	136	(141)	185
Included in other comprehensive income, gross			(16)	
Principal payments	(187)			
<b>Ending balance September 30, 2009</b>	\$ 26,971	\$ 366	\$ (2,033)	\$ 42
	<b>Hedged Loans</b>	<b>Forward Sale Commitments</b>	<b>Interest Rate Swaps</b>	<b>Commitments to Originate Loans</b>
<b>Beginning balance December 31, 2007</b>	\$	\$	\$	\$
Total realized and unrealized gains and losses				
Included in net income	195		(195)	
Included in other comprehensive income, gross			(584)	
Purchases, issuances, and settlements	11,437			
Principal payments	(31)			
<b>Ending balance March 31, 2008</b>	11,601		(779)	

Total realized and unrealized gains and losses				
Included in net income	(436)		436	
Included in other comprehensive income, gross			601	
Purchases, issuances, and settlements	5,166			
Principal payments	(62)			
<b>Ending balance June 30, 2008</b>	16,269		258	
Total realized and unrealized gains and losses				
Included in net income	198		(198)	
Included in other comprehensive income, gross			(95)	
Purchases, issuances, and settlements	2,506			
Principal payments	(159)			
<b>Ending balance September 30, 2008</b>	\$ 18,814	\$	\$ (35)	\$

**Table of Contents****HORIZON BANCORP AND SUBSIDIARIES****Notes to Condensed Consolidated Financial Statements**

(Table Dollar Amounts in Thousands, Except Per Share Data)

Realized gains and losses included in net income for the periods are reported in the condensed consolidated statements of income as follows (Unaudited):

<b>Non Interest Income</b>	<b>Nine Months Ended September 30</b>	
	<b>2009</b>	<b>2008</b>
<b>Total gains and losses from:</b>		
Hedged loans	\$ (419)	\$ (43)
Fair value interest rate swap agreements	419	43
Derivative loan commitments	177	
	\$ 177	\$

Certain other assets are measured at fair value on a nonrecurring basis in the course of business and are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment):

	<b>Fair Value</b>	<b>Quoted Prices in Active Markets for Identical Assets (Level 1)</b>	<b>Significant Other Observable Inputs (Level 2)</b>	<b>Significant Unobservable Inputs (Level 3)</b>
<b>September 30, 2009</b> (Unaudited)				
Impaired and non-accrual loans	\$ 11,276	\$	\$	\$ 11,276
Other real estate owned	1,671			1,671
<b>December 31, 2008</b>				
Impaired and non-accrual loans	\$ 4,685	\$	\$	\$ 4,685
Other real estate owned	2,874			2,874

**Impaired, non-accrual loans, and other real estate owned:** Fair value adjustments for impaired and non-accrual loans typically occur when there is evidence of impairment. Loans are designated as impaired when, in the judgment of management based on current information and events, it is probable that all amounts due according to the contractual terms of the loan agreement will not be collected. The measurement of loss associated with impaired loans can be based on either the observable market price of the loan or the fair value of the collateral. The Company measures fair value based on the value of the collateral securing the loans. Collateral may be in the form of real estate or personal property including equipment and inventory. The value of the collateral is determined based on internal estimates as well as third party appraisals or non-binding broker quotes. These measurements were classified as Level 3. The fair value of the Company's other real estate owned is determined using Level 3 inputs, which include current and prior appraisals and estimated costs to sell.

**Note 8 Fair Value of Financial Instruments**

The estimated fair value amounts were determined using available market information, current pricing information applicable to Horizon and various valuation methodologies. Where market quotations were not available, considerable management judgment was involved in the determination of estimated fair values. Therefore, the estimated fair value

of financial instruments shown below may not be representative of the amounts at which they could be exchanged in a current or future transaction. Due to the inherent uncertainties of expected cash flows of financial instruments, the use of alternate valuation assumptions and methods could have a significant effect on the derived estimated fair value amounts.

The estimated fair values of financial instruments, as shown below, are not intended to reflect the estimated liquidation or market value of Horizon taken as a whole. The disclosed fair value estimates are limited to

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**

**Notes to Condensed Consolidated Financial Statements**

(Table Dollar Amounts in Thousands, Except Per Share Data)

Horizon's significant financial instruments at September 30, 2009 and December 31, 2008. These include financial instruments recognized as assets and liabilities on the consolidated balance sheet as well as certain off-balance sheet financial instruments. The estimated fair values shown below do not include any valuation of assets and liabilities, which are not financial instruments as defined by the FASB ASC fair value hierarchy.

The following methods and assumptions were used to estimate the fair value of each class of financial instrument:

**Cash and Cash Equivalents** The carrying amounts approximate fair value.

**Interest-Bearing Deposits** The carrying amounts approximate fair value.

**Held-to-Maturity Securities** For debt securities held to maturity, fair values are based on quoted market prices or dealer quotes. For those securities where a quoted market price is not available, carrying amount is a reasonable estimate of fair value based upon comparison with similar securities.

**Loans Held for Sale** The carrying amounts approximate fair value.

**Net Loans** The fair value of portfolio loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. The carrying amounts of loans held for sale approximate fair value.

**Interest Receivable/Payable** The carrying amounts approximate fair value.

**FHLB and FRB Stock** Fair value of FHLB and FRB stock is based on the price at which it may be resold to the FHLB and FRB.

**Deposits** The fair value of demand deposits, savings accounts, interest-bearing checking accounts and money market deposits is the amount payable on demand at the reporting date. The fair value of fixed maturity certificates of deposit is estimated by discounting the future cash flows using rates currently offered for deposits of similar remaining maturity.

**Borrowings** Rates currently available to Horizon for debt with similar terms and remaining maturities are used to estimate fair values of existing borrowings.

**Subordinated Debentures** Rates currently available for debentures with similar terms and remaining maturities are used to estimate fair values of existing debentures.

**Commitments to Extend Credit and Standby Letter of Credit** The fair value of commitments is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The fair value of letters of credit is based on fees currently charged for similar agreements or on the estimated cost to terminate them or otherwise settle the obligations with the counterparties at the reporting date. Due to the short-term nature of these agreements, carrying amounts approximate fair value.



**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**  
**Notes to Condensed Consolidated Financial Statements**  
(Table Dollar Amounts in Thousands, Except Per Share Data)

The estimated fair values of Horizon's financial instruments are as follows:

	<b>September 30, 2009</b>		<b>December 31, 2008</b>	
	<b>(Unaudited)</b>			
	<b>Carrying</b>	<b>Fair</b>	<b>Carrying</b>	<b>Fair</b>
	<b>Amount</b>	<b>Value</b>	<b>Amount</b>	<b>Value</b>
<b>Assets</b>				
Cash and cash equivalents	\$ 10,848	\$ 10,848	\$ 36,001	\$ 36,001
Interest-bearing deposits	4,464	4,464	2,679	2,679
Investment securities available for sale	333,031	333,031	301,638	301,638
Investment securities held to maturity	15,661	15,664	1,630	1,634
Loans held for sale	6,119	6,119	5,955	5,955
Loans, net	861,785	878,960	870,557	870,329
Stock in FHLB and FRB	13,225	13,225	12,625	12,625
Interest receivable	6,222	6,222	5,708	5,708
<b>Liabilities</b>				
Non-interest bearing deposits	\$ 87,725	\$ 87,725	\$ 83,642	\$ 83,642
Interest-bearing deposits	770,272	759,740	757,527	739,867
Borrowings	311,884	333,203	324,383	334,616
Subordinated debentures	27,837	28,154	27,837	28,867
Interest payable	1,304	1,304	1,910	1,910

**Note 9 Other Comprehensive Income**

	<b>September</b>	<b>December 31,</b>
	<b>30, 2009</b>	<b>2008</b>
	<b>(Unaudited)</b>	
Unrealized gains (losses) on securities:		
Unrealized holding gains arising during the year	\$ 9,627	\$ 1,706
Less: reclassification adjustment for gains (losses) realized in net income	422	(15)
	9,205	1,721
Unrealized gain (loss) on derivative instruments	113	(851)
Net unrealized gains	9,318	870
Tax expense	(3,727)	(305)
Other comprehensive income	\$ 5,591	\$ 565

The components of accumulated other comprehensive income included in capital are as follows:

	<b>September</b>	<b>December 31,</b>
	<b>30, 2009</b>	<b>2008</b>
Unrealized holding gain on securities available for sale	\$ 6,704	\$ 1,181

Edgar Filing: HORIZON BANCORP /IN/ - Form 10-Q

Unrealized loss on derivative instruments	(485)	(553)
Total other comprehensive income	\$ 6,219	\$ 628

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**  
**Notes to Condensed Consolidated Financial Statements**  
(Table Dollar Amounts in Thousands, Except Per Share Data)

**Note 10 Subsequent Events**

Subsequent events have been evaluated through November 12, 2009 which is the date the financial statements were issued.

**Note 11 Future accounting matters**

***Financial Accounting Standards Board (FASB)***

**Accounting Standards Update (ASU) No. 2009-12, *Investments in Certain Entities that Calculate Net Asset Value per Share***

In September 2009, this ASU was issued and permits, as a practical expedient, a reporting entity to measure the fair value of an investment that is within the scope of the amendments in this ASU on the basis of the net asset value per share of the investment (or its equivalent) if the net asset value of the investment (or its equivalent) is calculated in a manner consistent with the measurement principles of Topic 946 as of the reporting entity's measurement date. The ASU also requires disclosures by major category of investment about the attributes of investments within the scope of the Update. ASU 2009-12 is effective for interim and annual periods ending after December 15, 2009. Horizon is currently assessing the impact of the ASU on our financial condition, results of operations, and disclosures.

**ASU No. 2009-05, *Measuring Liabilities at Fair Value codified in Fair Value Measurements and Disclosures (Topic 820) Measuring Liabilities at Fair Value***

In August 2009, this ASU provides amendments for fair value measurements of liabilities. It provides clarification that in circumstances in which a quoted price in an active market for the identical liability is not available, a reporting entity is required to measure fair value using one or more techniques. ASU 2009-05 also clarifies that when estimating a fair value of a liability, a reporting entity is not required to include a separate input or adjustment to other inputs relating to the existence of a restriction that prevents the transfer of the liability. ASU 2009-05 is effective for the first reporting period (including interim periods) beginning after issuance or fourth quarter 2009. Horizon is currently assessing the impact of the on our financial condition, results of operations, and disclosures.

**ASU 2009-01 (formerly SFAS No. 168), *Topic 105 Generally Accepted Accounting Principles FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles***

ASU 2009-01 establishes the FASB Accounting Standards Codification (Codification) as the single source of authoritative U.S. generally accepted accounting principles (U.S. GAAP) recognized by the FASB to be applied by nongovernmental entities. Rules and interpretive releases of the SEC under authority of federal securities laws are also sources of authoritative U.S. GAAP for SEC registrants. ASU 2009-01 was effective for financial statements issued for interim and annual periods ending after September 15, 2009. Horizon has made the appropriate changes to GAAP references in our financial statements.

**FASB ASC 810-10 (formerly SFAS No. 167), *Amendments to FASB Interpretation No. 46(R)***

In June 2009, the FASB issued SFAS 167 which amends the consolidation guidance applicable to variable interest entities. The amendments to the consolidation guidance affect all entities currently within the scope of FIN 46(R), as well as qualifying special-purpose entities (QSPEs) that are currently excluded from the scope of FIN 46(R). SFAS 167 is effective as of the beginning of the first annual reporting period that begins after November 15, 2009. Horizon is currently assessing the impact of SFAS 167 on our financial condition, results of operations, and disclosures.

**FASB ASC topic 860 (formerly SFAS No. 166), *Accounting for Transfers of Financial Assets, an amendment of FASB Statement No. 140***

SFAS 166 amends the derecognition accounting and disclosure guidance relating to SFAS 140. SFAS 166 eliminates the exemption from consolidation for QSPEs, it also requires a transferor to evaluate all existing QSPEs to determine whether it must be consolidated in accordance with SFAS 167. SFAS 166 is effective as

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**

**Notes to Condensed Consolidated Financial Statements**

(Table Dollar Amounts in Thousands, Except Per Share Data)

of the beginning of the first annual reporting period that begins after November 15, 2009. Horizon is currently assessing the impact of SFAS 166 on our financial condition, results of operations, and disclosures.

Accounting Standards Codification (ASC) 855 (formerly Statement No. 165), *Subsequent Events*

In May 2009, the FASB issued ASC 855 which establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or available to be issued. ASC 855 was effective for interim or annual periods ending after June 15, 2009. Horizon adopted the provisions of ASC 855 and this change is reflected in Note 10 - Subsequent Events.

ASC 825 (formerly FASB Staff Position (FSP) 107-1 and APB 28-1), *Interim Disclosures about Fair Value of Financial Instruments*

In April 2009, the FASB issued ASC 825 which requires a public entity to provide disclosures about fair value of financial instruments in interim financial information. ASC 825 is effective for interim and annual financial periods ending after June 15, 2009. Horizon adopted the provisions of ASC 825 on April 1, 2009 and the impact on our disclosures is more fully discussed in Note 8.

ASC 320 (formerly FSP FAS 115-2, FAS124-2 and EITF 99-20-2), *Recognition and Presentation of Other-Than-Temporary-Impairment*

In April 2009, the FASB issued ASC 320 which (i) changes existing guidance for determining whether an impairment is other than temporary to debt securities and (ii) replaces the existing requirement that the entity's management assert it has both the intent and ability to hold an impaired security until recovery with a requirement that management assert: (a) it does not have the intent to sell the security; and (b) it is more likely than not it will not have to sell the security before recovery of its cost basis. Under ASC 320, declines in the fair value of held-to-maturity and available-for-sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses to the extent the impairment is related to credit losses. The amount of impairment related to other factors is recognized in other comprehensive income. ASC 320 is effective for interim and annual periods ending after June 15, 2009. Horizon adopted the provisions of ASC 320 on April 1, 2009. Details related to the adoption of ASC 320 and the impact on our disclosures are more fully discussed in Note 2.

Earnings Per Share (EPS): (formerly FSP EITF 03-6-1), *Determining Whether Instruments Granted in Shared-Based Payment Transaction are Participating Securities*

In June 2008, the FASB issued ASC 260 which clarifies that unvested share-based payment awards with a right to receive nonforfeitable dividends are participating securities. ASC 260 also provides guidance on how to allocate earnings to participating securities and compute EPS using the two-class method. ASC 260 is effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those years. The provisions of ASC 260 did not have a material impact on our EPS calculation.

ASC 815 (formerly Statement No. 161), *Disclosures About Derivative Instruments and Hedging Activities*

In March 2008, the FASB issued ASC 815 which requires qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about fair value amounts of and gains and losses on derivative instruments, and disclosures about credit-risk-related contingent features in derivative agreements. ASC 815 is effective for fiscal years beginning after November 15, 2008. Horizon adopted the provisions of ASC 815 on January 1, 2009. The required disclosures are included in Note 6.

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**  
**Management's Discussion and Analysis of Financial Condition**  
**And Results of Operations**

**For the Three and Nine Months Ended September 30, 2009**

**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

***Forward Looking Statements***

This report contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, with respect to Horizon Bancorp ( Horizon or Company ) and Horizon Bank, N.A. (Bank). Horizon intends such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Reform Act of 1995, and is including this statement for the purposes of these safe harbor provisions. Forward-looking statements, which are based on certain assumptions and describe future plans, strategies and expectations of Horizon, are generally identifiable by use of the words believe, expect, intend, anticipate, estimate, project or similar expressions. Horizon's ability to predict results or the actual effect of future plans or strategies is inherently uncertain. Factors that could have a material adverse effect on Horizon's future activities and operating results include, but are not limited to:

***Credit risk:*** the risk that loan customers or other parties will be unable to perform their contractual obligations;

***Market risk:*** the risk that changes in market rates and prices will adversely affect the Company's financial condition or results of operation;

***Liquidity risk:*** the risk that Horizon or the Bank will have insufficient cash or access to cash to meet its operating needs;

***Operational risk:*** the risk of loss resulting from fraud, inadequate or failed internal processes, people and systems, or external events;

***Economic risk:*** the risk that the economy in the Company's markets could decline further resulting in increased unemployment, decreased real estate values and increased loan charge-offs; and

***Compliance risk:*** the risk of additional action by Horizon's regulators or additional regulation could hinder the Company's ability to do business profitably.

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

***Overview***

Horizon Bancorp ( Horizon or the Company ) is a registered bank holding company incorporated in Indiana and headquartered in Michigan City, Indiana. Horizon provides a broad range of banking services in Northwestern Indiana and Southwestern Michigan through its bank subsidiary, Horizon Bank, N.A. (the Bank ) and other affiliated entities. Horizon operates as a single segment, which is commercial banking. Horizon's Common Stock is traded on the Nasdaq Global Market under the symbol HBNC. The Bank was chartered as a national banking association in 1873 and has operated continuously since that time. The Bank is a full-service commercial bank offering commercial and retail banking services, corporate and individual trust and agency services, and other services incident to banking. Horizon continues to operate in a challenging and uncertain economic environment. Within the Company's primary market areas of Northwest Indiana and Southwest Michigan unemployment rates have increased over the last year. This rise in unemployment has been driven by factors including slowdowns in the steel and recreational vehicle industries as well as a continued slowdown in the housing industry. Like numerous other parts of the country, Northwest Indiana and Southwest Michigan are experiencing a rise in mortgage delinquencies and bankruptcy filings as a result of increased unemployment rates. Despite these economic factors, Horizon continues to post positive

results through the first nine months of 2009.

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**  
**Management's Discussion and Analysis of Financial Condition**  
**And Results of Operations**

**For the Three and Nine Months Ended September 30, 2009**

Following are some highlights of Horizons financial performance through the third quarter of 2009:

Horizon's year-to-date net income for the first nine months of 2009 was \$7.1 million, which exceeds last year's net income for the same time period of \$6.9 million.

Horizon's third quarter 2009 net income was \$2.4 million or \$0.61 diluted earnings per share.

Net interest margin for the third quarter increased compared to the prior quarter.

Horizon continued to experience strong residential mortgage loan volume through the third quarter.

Horizon's quarterly provision to the allowance for loan loss increased by approximately \$125,000 from the second quarter of 2009 increasing the allowance for loan losses to total loans to 1.58%.

Horizon's balance of Other Real Estate Owned of \$1.7 million at September 30, 2009 was at its lowest level since September 30, 2008.

Horizon's non-performing loans increased by \$3.0 million from June 30, 2009 to September 30, 2009.

Horizon's net loan charge-offs for the third quarter decreased from the previous two quarters.

Horizon's non-performing loans to total loans ratio as of September 30, 2009 was 1.87%, which compares favorably to National and State of Indiana peer averages.<sup>1</sup>

Horizon's capital ratios continue to be above the regulatory standards for well-capitalized banks.

***Critical Accounting Policies***

The notes to the consolidated financial statements included in Item 8 of the Company's Annual Report on Form 10-K for 2008 contain a summary of the Company's significant accounting policies. Certain of these policies are important to the portrayal of the Company's financial condition, since they require management to make difficult, complex or subjective judgments, some of which may relate to matters that are inherently uncertain. Management has identified the allowance for loan losses, intangible assets and hedge accounting as critical accounting policies.

**Allowance for Loan Losses**

An allowance for loan losses is maintained to absorb probable incurred loan losses inherent in the loan portfolio. The determination of the allowance for loan losses is a critical accounting policy that involves management's ongoing quarterly assessments of the probable incurred losses inherent in the loan portfolio. The identification of loans that have probable incurred losses is subjective, therefore, a general reserve is maintained to cover all probable losses within the entire loan portfolio. Horizon utilizes a loan grading system that helps identify, monitor and address asset quality problems in an adequate and timely manner. Each quarter, various factors affecting the quality of the loan portfolio are reviewed. Large credits are reviewed on an individual basis for loss potential. Other loans are reviewed as a group based upon previous trends of loss experience. Horizon also reviews the current and anticipated economic conditions of its lending market as well as transaction risk to determine the effect they may have on the loss experience of the loan portfolio.

<sup>1</sup> National peer group: Consists

of all insured commercial banks having assets between \$1 Billion and \$3 Billion as reported by the Uniform Bank Performance Report as of June 30, 2009. Indiana peer group: Consists of 18 publicly traded banks all headquartered in the State of Indiana as reported by the Uniform Bank Performance Reports as of June 30, 2009.



**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**  
**Management's Discussion and Analysis of Financial Condition**  
**And Results of Operations**  
**For the Three and Nine Months Ended September 30, 2009**

**Goodwill and Intangible Assets**

Management believes that the accounting for goodwill and other intangible assets also involves a higher degree of judgment than most other significant accounting policies. FASB ASC 350-10 establishes standards for the amortization of acquired intangible assets and impairment assessment of goodwill. At September 30, 2009, Horizon had core deposit intangibles of \$1.5 million subject to amortization and \$5.8 million of goodwill, which is not subject to amortization. Goodwill arising from business combinations represents the value attributable to unidentifiable intangible assets in the business acquired. Horizon's goodwill relates to the value inherent in the banking industry and that value is dependent upon the ability of Horizon to provide quality, cost effective banking services in a competitive marketplace. The goodwill value is supported by revenue that is in part driven by the volume of business transacted. A decrease in earnings resulting from a decline in the customer base or the inability to deliver cost effective services over sustained periods can lead to impairment of goodwill that could adversely affect earnings in future periods. FASB ASC 350-10 requires an annual evaluation of goodwill for impairment. The evaluation of goodwill for impairment requires the use of estimates and assumptions. Market price at the close of business on September 30, 2009 was \$17.10 per share compared to a book value of \$27.46 per common share. Horizon reported record earnings for the ninth consecutive year in 2008 and has continued to report strong earnings through the first nine months of 2009 and believes the decline in market price relates to an overall decline in the financial industry sector and is not specific to Horizon. Horizon engaged a third party to perform an impairment test of its goodwill in 2008. The evaluation included three approaches: 1) income approach using a discounted cash flow based on earnings capacity, 2) price to earnings multiples and 3) price to book value ratios. Approaches two and three use median results from 17 bank sale transactions that occurred during 2007 and 2008. The selling banks ranged in size from \$763.0 million to \$2.1 billion. The impairment test was performed as of November 30, 2008 and provided support that no impairment to the Company's goodwill was required based on its results.

Due to the evaluation being done as of November 30, 2008, the financial results for December 2008 were anticipated and included as part of this analysis. An additional \$20 million of capital was injected into Horizon Bank by the holding company but the calculated fair value of Horizon Bank was still well above its book value. There were no significant changes in the Company's stock price, book value, or earnings as of September 30, 2009 that would change the results of the evaluation completed at the end of 2008. Horizon has concluded that, based on its own internal evaluation and the independent impairment test conducted by a third party, the recorded value of goodwill is not impaired.

**Mortgage Servicing Rights**

Servicing assets are recognized as separate assets when rights are acquired through purchase or through the sale of financial assets on a servicing-retained basis. Capitalized servicing rights are amortized into non-interest income in proportion to, and over the period of, the estimated future net servicing income of the underlying financial assets. Servicing assets are evaluated regularly for impairment based upon the fair value of the rights as compared to amortized cost. Impairment is determined by stratifying servicing rights by predominant characteristics, such as interest rates, original loan terms and whether the loans are fixed or adjustable rate mortgages. Fair value is determined using prices for similar assets with similar characteristics, when available, or based upon discounted cash flows using market-based assumptions. When the book value of an individual stratum exceeds its fair value, an impairment reserve is recognized so that each individual stratum is carried at the lower of its amortized book value or fair value. In periods of falling market interest rates, accelerated loan prepayment speeds can adversely affect the fair value of these mortgage-servicing rights relative to their book value. In the event that the fair value of these assets was to increase in the future, Horizon can recognize the increased fair value to the extent of the impairment allowance but cannot recognize an asset in excess of its amortized book value. Future changes in management's assessment of the impairment of these servicing assets, as a result of changes in observable market data relating to market



**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**  
**Management's Discussion and Analysis of Financial Condition**  
**And Results of Operations**

**For the Three and Nine Months Ended September 30, 2009**

interest rates, loan prepayment speeds, and other factors, could impact Horizon's financial condition and results of operations either positively or adversely.

Generally, when market interest rates decline and other factors favorable to prepayments occur, there is a corresponding increase in prepayments as customers refinance existing mortgages under more favorable interest rate terms. When a mortgage loan is prepaid, the anticipated cash flows associated with servicing that loan are terminated, resulting in a reduction of the fair value of the capitalized mortgage servicing rights. To the extent that actual borrower prepayments do not react as anticipated by the prepayment model (i.e., the historical data observed in the model does not correspond to actual market activity), it is possible that the prepayment model could fail to accurately predict mortgage prepayments and could result in significant earnings volatility. To estimate prepayment speeds, Horizon utilizes a third-party prepayment model, which is based upon statistically derived data linked to certain key principal indicators involving historical borrower prepayment activity associated with mortgage loans in the secondary market, current market interest rates and other factors, including Horizon's own historical prepayment experience. For purposes of model valuation, estimates are made for each product type within the mortgage servicing rights portfolio on a monthly basis.

**Derivative Instruments**

As part of the Company's asset/liability management program, Horizon utilizes, from time-to-time, interest rate floors, caps or swaps to reduce the Company's sensitivity to interest rate fluctuations. These are derivative instruments, which are recorded as assets or liabilities in the consolidated balance sheets at fair value. Changes in the fair values of derivatives are reported in the consolidated income statements or other comprehensive income (OCI) depending on the use of the derivative and whether the instrument qualifies for hedge accounting. The key criterion for the hedge accounting is that the hedged relationship must be highly effective in achieving offsetting changes in those cash flows that are attributable to the hedged risk, both at inception of the hedge and on an ongoing basis.

Horizon's accounting policies related to derivatives reflect the guidance in FASB ASC 815-10. Derivatives that qualify for the hedge accounting treatment are designated as either: a hedge of the fair value of the recognized asset or liability or of an unrecognized firm commitment (a fair value hedge) or a hedge of a forecasted transaction or the variability of cash flows to be received or paid related to a recognized asset or liability (a cash flow hedge). For fair value hedges, the cumulative change in fair value of both the hedge instruments and the underlying loans is recorded in non-interest income. For cash flow hedges, changes in the fair values of the derivative instruments are reported in OCI to the extent the hedge is effective. The gains and losses on derivative instruments that are reported in OCI are reflected in the consolidated income statement in the periods in which the results of operations are impacted by the variability of the cash flows of the hedged item. Generally, net interest income is increased or decreased by amounts receivable or payable with respect to the derivatives, which qualify for hedge accounting. At inception of the hedge, Horizon establishes the method it uses for assessing the effectiveness of the hedging derivative and the measurement approach for determining the ineffective aspect of the hedge. The ineffective portion of the hedge, if any, is recognized currently in the consolidated statements of income. Horizon excludes the time value expiration of the hedge when measuring ineffectiveness.

**Valuation Measurements**

Valuation methodologies often involve a significant degree of judgment, particularly when there are no observable active markets for the items being valued. Investment securities, residential mortgage loans held for sale and derivatives are carried at fair value, as defined in FASB ASC 820, which requires key judgments affecting how fair value for such assets and liabilities is determined. In addition, the outcomes of valuations have a direct bearing on the carrying amounts of goodwill, mortgage servicing rights, and pension and other post-retirement benefit obligations. To determine the values of these assets and liabilities, as well as the

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**  
**Management's Discussion and Analysis of Financial Condition**  
**And Results of Operations**

**For the Three and Nine Months Ended September 30, 2009**

extent, to which related assets may be impaired, management makes assumptions and estimates related to discount rates, asset returns, prepayment rates and other factors. The use of different discount rates or other valuation assumptions could produce significantly different results, which could affect Horizon's results of operations.

27

---

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**  
**Management's Discussion and Analysis of Financial Condition**  
**And Results of Operations**  
**For the Three and Nine Months Ended September 30, 2009**

**Financial Condition**

On September 30, 2009, Horizon's total assets were \$1.3 billion, an increase of \$14.4 million from December 31, 2008 but a decrease of \$22.1 million from June 30, 2009 and a decrease of \$121.6 million from March 31, 2009. Due to the economic environment the financial institution industry was experiencing at the beginning of 2009, management determined it would be prudent to maintain higher liquidity levels. During that same time the Company's mortgage warehouse business line was experiencing significant growth due to the increase in mortgage loan refinancing activity, and this also created a need for additional liquidity. Management put into place several successful strategies during the first quarter of 2009 to generate the additional liquidity. As a result, the Company maintained excess cash and cash equivalents at the end of the first quarter and throughout most of the second quarter of 2009. A significant portion of that additional liquidity was generated from municipal money market deposits. This funding was designed to match the growth of assets in the mortgage warehouse business line and provide additional liquidity without utilizing asset based collateral borrowings or federal fund lines. During the second and third quarters the additional funding from the municipal money market accounts was moved out of the Bank and cash and cash equivalents and the municipal money market accounts were back to more historic levels. The Bank does not anticipate a need to maintain the level of excess liquidity during the fourth quarter as it did in the first half of the year.

Investment securities increased by approximately \$45.4 million compared to the end of 2008. This growth was partially a continuation from the fourth quarter of 2008 as additional investment securities were purchased to leverage the capital raised through the U.S. Department of Treasury's Capital Purchase Program which is part of the Economic Emergency Stabilization Act approved by Congress. The increase in investment securities held to maturity was primarily from local municipal tax anticipation warrants.

Investment securities were comprised of the following as of:

	<b>September 30, 2009</b>		<b>December 31, 2008</b>	
	<b>Amortized Cost</b>	<b>Fair Value</b>	<b>Amortized Cost</b>	<b>Fair Value</b>
<b>Investment securities</b>				
<b>Available for sale</b>				
U.S. Treasury and federal agencies	\$ 19,722	\$ 20,293	\$ 23,661	\$ 24,914
State and municipal	96,371	100,723	88,282	86,985
Federal agency collateralized mtg. obligations	49,608	49,934	13,063	12,951
Federal agency mortgage-backed pools	156,300	161,627	174,227	176,389
Corporate notes	710	454	587	399
<b>Total available for sale</b>	<b>322,711</b>	<b>333,031</b>	299,820	301,638
Total held to maturity, state and municipal	15,661	15,664	1,630	1,634
<b>Total investment securities</b>	<b>\$338,372</b>	<b>\$348,695</b>	\$301,450	\$303,272

Net loans decreased \$8.8 million since December 31, 2008. This decrease was the result of the reduction in both residential mortgage and installment loans as the loans originated for the portfolios were outpaced by the reduction in the existing loan balances. A portion of the this reduction was offset by an increase in the Company's mortgage warehouse business line as its customers utilized their warehouse lines to fund residential mortgage refinancing activity.

Total deposits increased \$16.8 million during the first nine months of 2009 and as indicated above, increased \$9.8 million since June 30, 2009 and decreased \$119.5 million since March 31, 2009. The decrease in deposits

---

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**  
**Management's Discussion and Analysis of Financial Condition**  
**And Results of Operations**

**For the Three and Nine Months Ended September 30, 2009**

since March 31, 2009 was primarily the result of reducing the additional funding that was generated during the first quarter of 2009 from the municipal money market accounts. The increase in deposits since December 31, 2008 was the result of increased transaction account deposits and brokered certificates of deposit partially offset by a decrease in public money market and consumer certificates of deposit. The Company has added \$42.6 million of long-term brokered certificates of deposit during the first nine months of 2009 to help in extending the duration of deposits. The total of brokered deposits at September 30, 2009 was \$93.2 million with a range of original terms of 20 months to 84 months with an average remaining life of 29 month and at an average cost of 3.57%.

The Company's borrowings have decreased \$12.5 million since December 31, 2008. The decrease in borrowings since the end of 2008 was primarily in FHLB advances. As FHLB advances have matured the Company has determined not to take additional advances and used long-term brokered certificates of deposit to replace any required long-term debt. This generates additional liquidity by not using available collateral to secure the borrowings. FHLB advances have decreased \$34.7 million during 2009. To partially offset the reduction in FHLB advances at September 30, 2009, there was a \$20.0 million short-term borrowing from the Company's federal fund lines.

Stockholders' equity totaled \$113.8 million at September 30, 2009 compared to \$103.4 million at December 31, 2008. The increase in stockholders' equity during the period was the result of generating net income and an increase in the market value of investment securities available for sale, reduced by dividends declared. At September 30, 2009, the ratio of average stockholders' equity to average assets was 8.53% compared to 6.65% at December 31, 2008. Book value per common share at September 30, 2009 increased to \$27.46 compared to \$24.68 at December 31, 2008.

***Results of Operations***

**Overview**

Consolidated net income for the three-month period ended September 30, 2009 was \$2.4 million, an increase of 77.0% from the \$1.3 million for the same period in 2008. Earnings per common share for the three months ended September 30, 2009 increased to \$0.62 basic and \$0.61 diluted, compared to \$0.42 basic and \$0.41 diluted for the same three-month period in 2008. Diluted earnings per share were reduced by \$0.11 per share due to the preferred stock dividends and the accretion of the discount on preferred stock, which is not available to common stockholders. The preferred stock was issued in the fourth quarter of 2008 and therefore did not affect the third quarter of 2008. Consolidated net income for the nine-month period ended September 30, 2009 was \$7.1 million, an increase of 3.0% from the \$6.9 million for the same period in 2008. However, earnings per common share for the nine months ended September 30, 2009 decreased to \$1.86 basic and \$1.84 diluted, compared to \$2.14 basic and \$2.11 diluted for the same nine-month period in 2008. Diluted earnings per share were reduced in 2009 by \$0.32 per share due to the preferred stock dividends and the accretion of the discount on preferred stock, which is not available to common stockholders.

**Net Interest Income**

The largest component of net income is net interest income. Net interest income is the difference between interest income, principally from loans and investment securities, and interest expense, principally on deposits and borrowings. Changes in the net interest income are the result of changes in volume and the net interest spread which affects the net interest margin. Volume refers to the average dollar levels of interest-earning assets and interest-bearing liabilities. Net interest spread refers to the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities. Net interest margin refers to net

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**  
**Management's Discussion and Analysis of Financial Condition**  
**And Results of Operations**

**For the Three and Nine Months Ended September 30, 2009**

interest income divided by average interest-earning assets and is influenced by the level and relative mix of interest-earning assets and interest-bearing liabilities.

The reduction in interest rates during 2009 has influenced the cost of the Company's interest bearing liabilities more significantly than the reduction in yields received on the Company's interest earning assets, resulting in an increase of the net interest margin for both the three and nine month periods ending September 30, 2009. Management believes that the current level of interest rates is driven by external factors and therefore impacts the results of the Company's net interest margin. Management does not expect a rise in interest rates in the short term, but an increase in rates is expected at some time in the future due to the current historically low interest rate environment.

Net interest income during the three months ended September 30, 2009 was \$10.7 million, an increase of \$1.3 million or 14.0% over the \$9.4 million earned during the same period in 2008. Yields on the Company's interest-earning assets decreased by 42 basis points to 5.83% for the three months ended September 30, 2009, from 6.25% for the same period in 2008. Interest income increased \$320,000 from \$17.2 million for the three months ended September 30, 2008 to \$17.5 million for the same period in 2009. This increase was due to the increased volume of interest earning assets partially offset by the decrease in the yield on interest earning assets. However, the asset yields on loans receivable has not declined at the same pace as some market indices partially due to interest rate floors that are in place on approximately \$330.5 million out of the \$476.7 million of the Company's adjustable rate loans.

Rates paid on interest-bearing liabilities decreased by 60 basis points during the same period due to the lower interest rate environment. Interest expense decreased \$1.0 million from \$7.8 million for the three-months ended September 30, 2008 to \$6.8 million for the same period in 2009. This decrease was due to the lower rates being paid on the Company's interest bearing liabilities but offset by the increased volume of interest bearing liabilities. Due to a more significant decrease in the rates paid on the Company's interest-bearing liabilities compared to the decrease in the yield on the Company's interest-earning assets, offset with the growth of the Company's interest earning assets and interest bearing liabilities, the net interest margin increased 19 basis points from 3.45% for the three months ended September 30, 2008 to 3.64% for the same period in 2009.



**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**  
**Management's Discussion and Analysis of Financial Condition**  
**And Results of Operations**

**For the Three and Nine Months Ended September 30, 2009**

The following are the average balance sheets for the three months ending:

	<b>Three Months Ended September 30, 2009</b>			<b>Three Months Ended September 30, 2008</b>		
	<b>Average Balance</b>	<b>Interest</b>	<b>Average Rate</b>	<b>Average Balance</b>	<b>Interest</b>	<b>Average Rate</b>
<b>ASSETS</b>						
Interest-earning assets						
Federal funds sold	\$ 10,711	\$ 7	0.26%	\$ 2,773	\$ 9	1.29%
Interest-earning deposits	7,783		0.00%	1,691	8	1.88%
Investment securities taxable	248,165	2,666	4.26%	173,217	2,155	4.95%
Investment securities non-taxable (1)	102,286	1,015	5.97%	78,712	791	4.70%
Loans receivable (2)	857,801	13,797	6.39%	845,391	14,202	6.69%
 Total interest-earning assets (1)	 1,226,746	 17,485	 5.83%	 1,101,784	 17,165	 6.25%
Noninterest-earning assets						
Cash and due from banks	15,277			17,483		
Allowance for loan losses	(12,513)			(9,788)		
Other assets	77,734			70,996		
	 \$ 1,307,244			 \$ 1,180,475		
 <b>LIABILITIES AND SHAREHOLDERS EQUITY</b>						
Interest-bearing liabilities						
Interest-bearing deposits	\$ 756,567	\$ 3,528	1.85%	\$ 691,900	\$ 4,261	2.45%
Borrowings	317,224	2,897	3.62%	296,844	3,108	4.17%
Subordinated debentures	27,837	341	4.86%	27,837	393	5.62%
 Total interest-bearing liabilities	 1,101,628	 6,766	 2.44%	 1,016,581	 7,762	 3.04%
Noninterest-bearing liabilities						
Demand deposits	84,897			80,762		
Accrued interest payable and other liabilities	9,238			7,105		
Shareholders' equity	111,481			76,027		
	 \$ 1,307,244			 \$ 1,180,475		

Net interest income/spread	\$ 10,719	3.39%	\$ 9,403	3.21%
Net interest income as a percent of average interest earning assets (1)		3.64%		3.45%

(1) Securities balances represent daily average balances for the fair value of securities. The average rate is calculated based on the daily average balance for the amortized cost of securities. Interest income is presented on a tax equivalent basis.

(2) Includes fees on loans. The inclusion of loan fees does not have a material effect on the average interest rate.

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES  
Management's Discussion and Analysis of Financial Condition  
And Results of Operations**

**For the Three and Nine Months Ended September 30, 2009**

Net interest income during the nine months ended September 30, 2009 was \$33.4 million, an increase of \$5.7 million or 20.7% over the \$27.7 million earned during the same period in 2008. Yields on the Company's interest-earning assets decreased by 41 basis points to 5.91% for the nine months ended September 30, 2009 from 6.32% for the same period in 2008. Interest income increased \$1.8 million from \$53.2 million for the nine months ended September 30, 2008 to \$55.0 million for the same period in 2009. This increase was due to the increased volume in interest earning assets partially offset by the decrease in the yield on interest earning assets.

Rates paid on interest-bearing liabilities decreased by 74 basis points during the same period due to the lower interest rate environment. Interest expense decreased \$3.9 million from \$25.5 million for the nine-months ended September 30, 2008 to \$21.6 million for the same period in 2009. This decrease was due to the lower rates being paid on the Company's interest bearing liabilities but offset by the increased volume of interest bearing liabilities. Due to a more significant decrease in the rates paid on the Company's interest-bearing liabilities compared to the decrease in the yield on the Company's interest-earning assets, offset with the growth of the Company's interest earning assets and interest bearing liabilities, the net interest margin increased 33 basis points from 3.31% for the nine months ended September 30, 2008 to 3.64% for the same period in 2009.

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**  
**Management's Discussion and Analysis of Financial Condition**  
**And Results of Operations**

**For the Three and Nine Months Ended September 30, 2009**

The following are the average balance sheets for the nine months ending:

	<b>Nine Months Ended September 30, 2009</b>			<b>Nine Months Ended September 30, 2008</b>		
	<b>Average Balance</b>	<b>Interest</b>	<b>Average Rate</b>	<b>Average Balance</b>	<b>Interest</b>	<b>Average Rate</b>
<b>ASSETS</b>						
Interest-earning assets						
Federal funds sold	\$ 27,647	\$ 9	0.04%	\$ 20,207	\$ 434	2.87%
Interest-earning deposits	6,979	54	1.03%	6,816	140	2.74%
Investment securities taxable	247,168	8,270	4.47%	174,293	6,360	4.87%
Investment securities non-taxable (1)	94,473	2,882	5.91%	80,811	2,490	4.84%
Loans receivable (2)	898,876	43,793	6.52%	851,673	43,763	6.87%
 Total interest-earning assets (1)	 1,275,143	 55,008	 5.91%	 1,133,800	 53,187	 6.32%
Noninterest-earning assets						
Cash and due from banks	15,370			17,365		
Allowance for loan losses	(11,742)			(9,712)		
Other assets	76,613			69,000		
	 \$ 1,355,384			 \$ 1,210,453		
 <b>LIABILITIES AND SHAREHOLDERS EQUITY</b>						
Interest-bearing liabilities						
Interest-bearing deposits	\$ 797,523	\$ 11,517	1.93%	\$ 747,171	\$ 15,552	2.78%
Borrowings	328,763	9,011	3.66%	275,848	8,782	4.25%
Subordinated debentures	27,837	1,082	5.20%	27,837	1,192	5.72%
 Total interest-bearing liabilities	 1,154,123	 21,610	 2.50%	 1,050,856	 25,526	 3.24%
Noninterest-bearing liabilities						
Demand deposits	82,548			76,940		
Accrued interest payable and other liabilities	9,180			7,211		
Shareholders' equity	109,533			75,446		
	 \$ 1,355,384			 \$ 1,210,453		

Net interest income/spread	\$ 33,398	3.41%	\$ 27,661	3.08%
Net interest income as a percent of average interest earning assets (1)		3.64%		3.31%

(1) Securities balances represent daily average balances for the fair value of securities. The average rate is calculated based on the daily average balance for the amortized cost of securities. Interest income is presented on a tax equivalent basis.

(2) Includes fees on loans. The inclusion of loan fees does not have a material effect on the average interest rate.

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**  
**Management's Discussion and Analysis of Financial Condition**  
**And Results of Operations**  
**For the Three and Nine Months Ended September 30, 2009**

**Provision for Loan Losses**

Horizon assesses the adequacy of its Allowance for Loan and Lease Losses ( ALLL ) by regularly reviewing the performance of its loan portfolios. During the third quarter of 2009, a provision for loan losses of \$3.4 million was required to adequately fund the ALLL compared to a provision of \$3.1 million for the third quarter of 2008. The provision for the current quarter resulted from continued losses primarily in the installment loan portfolios due to current economic conditions and trends and the need for additional specific reserves due to the increase in non-performing loans. Commercial loan net charge-offs during the third quarter of 2009 were \$530,000, residential mortgage loan net charge-offs were \$22,000, and installment loans net charge-offs were \$1.6 million. For the nine months ended September 30, 2009, the provision for loan losses totaled \$9.9 million compared to \$5.4 million in the prior year for the same period. Commercial loan net charge-offs during the first nine months of 2009 were \$1.9 million, residential mortgage loan net charge-offs were \$286,000, and installment loan net charge-offs were \$5.2 million. During the second quarter the Company determined that five recreational vehicle loans were part of a loan fraud perpetrated by a single recreational vehicle dealer. These loans resulted in \$1.4 million of the installment loan charge-offs included in the results for the nine months ended September 30, 2009. Consumer loan charge-offs continue to add to the need for higher quarterly provisions for loan losses but appear to be stabilizing as the amount of consumer charge-offs have decreased over the last two quarters. However, the increase in non-performing loans has contributed to the need for additional provision expense for loan losses as specific reserves are identified for non-performing residential mortgage and commercial loans.

Non-performing loans at September 30, 2009 increased to \$16.5 million or 1.87% of total loans compared to \$13.5 million or 1.49% at June 30, 2009, \$10.5 million or 1.11% at March 31, 2009, and \$7.9 million or 0.89% at December 31, 2008. Horizon's non-performing loan statistics, while having increased from the prior quarters, still compare favorably to National and State of Indiana peer averages<sup>2</sup> for the same ratio as of June 30, 2009 of 3.49% and 3.06% respectively. The increase in the Company's non-performing loans can be attributed to the slower economy and continued local unemployment causing lower business revenues and increased consumer bankruptcies. Management believes the total allowance of \$13.9 million or 1.58% of total loans is adequate to absorb probable incurred losses contained in the loan portfolios.

Non-accrual loans totaled \$15.6 million on September 30, 2009, up from \$12.8 million on June 30, 2009. The increase in the three months ended September 30, 2009 was due to increases in commercial, mortgage, and consumer loans. Commercial loan non-accruals increased from \$7.9 million on June 30, 2009 to \$9.2 million on September 30, 2009. This was primarily due to one commercial loan totaling \$1.6 million placed on non-accrual during the quarter. This loan is to a manufacturing company and is current and in the process of a restructure.

Loans to homebuilders and land developers totaled \$2.7 million of commercial non-accrual loans on September 30, 2009, followed by loans to restaurant operators totaling \$2.6 million. Mortgage loans on non-accrual increased from \$3.8 million to \$4.6 million during the third quarter. Consumer loans on non-accrual increased from \$1.2 million to \$1.8 million during the quarter. The primary reason for the increase of consumer loans on non-accrual is the increase of borrowers under Chapter 13 bankruptcy repayment plans.

<sup>2</sup> National peer group: Consists of all insured commercial banks having assets between \$1 Billion and \$3 Billion as

reported by the  
Uniform Bank  
Performance  
Report as of  
June 30, 2009.  
Indiana peer  
group: Consists  
of 18 publicly  
traded banks all  
headquartered in  
the State of  
Indiana as  
reported by the  
Uniform Bank  
Performance  
Reports as of  
June 30, 2009.

Table of Contents

**HORIZON BANCORP AND SUBSIDIARIES**  
**Management's Discussion and Analysis of Financial Condition**  
**And Results of Operations**

**For the Three and Nine Months Ended September 30, 2009**

Most consumer loans in bankruptcy are paying but are held as non-accrual loans until a stable payment pattern has been established under the plan.

Loans 90 days delinquent but still accruing totaled \$856,000 on September 30, 2009, up from \$687,000 on June 30, 2009. Horizon's policy is to place loans over 90 days delinquent on non-accrual unless they are well secured and in the process of collection.

Other Real Estate Owned (OREO) totaled \$1.7 million on September 30, 2009, down from \$2.2 million on June 30, 2009. The decline during the third quarter was due to the sale of six properties with a book balance of \$806,000 partially offset by the addition of five properties with a book balance of \$268,000. On September 30, 2009, OREO was comprised of 17 properties. Of these, 15 totaling \$1.3 million were residential mortgages and the other two were commercial. Repossessed property totaled \$142,000 on September 30, 2009, up from \$115,000 on June 30, 2009. On September 30, 2009, repossessed property consisted of 15 automobiles and one boat.

Non-Interest Income

The following is a summary of changes in non-interest income:

	<b>Three Months Ended</b>		<b>Amount</b>	<b>Percent</b>
	<b>Sept 30,</b>	<b>Sept 30,</b>	<b>Change</b>	<b>Change</b>
	<b>2009</b>	<b>2008</b>		
<b>Non-interest income</b>				
Service charges on deposit accounts	\$ 972	\$ 1,065	\$ (93)	-8.7%
Wire transfer fees	201	155	46	29.7%
Interchange fees	514	216	298	138.0%
Fiduciary activities	745	911	(166)	-18.2%
Gain (loss) on sale of securities	422		422	100.0%
Gain on sale of mortgage loans	1,277	657	620	94.4%
Mortgage servicing net of impairment	35	3	32	1066.7%
Increase in cash surrender value of bank owned life insurance	206	252	(46)	-18.3%
Other income	170	92	78	84.8%
<b>Total non-interest income</b>	<b>\$4,542</b>	<b>\$ 3,351</b>	<b>\$1,191</b>	<b>35.5%</b>

The gain on sale of mortgage loans contributed significantly to the increase in non-interest income during the third quarter of 2009. Residential mortgage refinancing continued to generate strong volumes of loan sales during the third quarter and the Company's residential mortgage loan division provided customers with the needed service to lower their mortgage interest rates along with an increase in first time home buyers due to the personal income tax incentives available. During the third quarter of 2009, the Company originated approximately \$61.3 million of mortgage loans to be sold on the secondary market compared to \$30.7 million for the same period last year. A gain on the sale of securities of \$422,000 was realized during the third quarter as our analysis determined that market conditions provided the opportunity to add these gains to capital without negatively impacting long term earnings. Wire transfer fee income has increased compared to the prior year as the Company's mortgage warehouse business line has had more activity due to increased residential mortgage refinancing volume. Interchange fees also contributed to the increase in non-interest income due to higher levels of activity in ATM and debit card transactions. These increases were offset by a decrease in service charge income from reduced overdraft fee income as the number of consumer overdrafts have



gone down, a decrease in fiduciary activity from less fee income from the Bank's trust subsidiary, and a decrease in the amount of added cash surrender value on bank owned life insurance due to lower returns on the related assets.

Table of Contents

**HORIZON BANCORP AND SUBSIDIARIES**  
**Management's Discussion and Analysis of Financial Condition**  
**And Results of Operations**  
**For the Three and Nine Months Ended September 30, 2009**

	Nine Months Ended		Amount	Percent
	Sept 30, 2009	Sept 30, 2008	Change	Change
<b>Non-interest income</b>				
Service charges on deposit accounts	\$ 2,880	\$ 2,975	\$ (95)	-3.2%
Wire transfer fees	709	382	327	85.6%
Interchange fees	1,358	618	740	119.7%
Fiduciary activities	2,486	2,817	(331)	-11.8%
Gain (loss) on sale of securities	422	(15)	437	-2913.3%
Gain on sale of mortgage loans	4,861	2,122	2,739	129.1%
Mortgage servicing net of impairment	(131)	8	(139)	-1737.5%
Increase in cash surrender value of bank owned life insurance	547	701	(154)	-22.0%
Death benefit on officer life insurance		538	(538)	-100.0%
Other income	420	316	104	32.9%
<b>Total non-interest income</b>	<b>\$13,552</b>	<b>\$10,462</b>	<b>\$3,090</b>	<b>29.5%</b>

The gain on sale of mortgage loans also contributed to the majority of the increase in non-interest income during the first nine months of 2009. During the first nine months of 2009 the Company originated approximately \$267.8 million of residential mortgage loans to be sold on the secondary market compared to \$103.2 million for the same period last year. Wire transfer fee income has increased compared to the prior year as the Company's mortgage warehouse business line has had more activity due to increased residential mortgage refinancing volume. Interchange fees also contributed to the increase in non-interest income due to higher levels of activity in ATM and debit card transactions. A gain on the sale of securities of \$422,000 was realized during the third quarter as our analysis determined that market conditions provided the opportunity to add these gains to capital without negatively impacting long term earnings. These increases were offset by a decrease in fiduciary activity from less fee income from the Bank's trust subsidiary, lower mortgage servicing income due to impairment charges in the Company's mortgage servicing asset, a decrease in the amount of added cash surrender value on bank owned life insurance due to lower returns on the related assets, and not replacing the income recorded in 2008 from the death benefit on officer life insurance.

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**  
**Management's Discussion and Analysis of Financial Condition**  
**And Results of Operations**  
**For the Three and Nine Months Ended September 30, 2009**

**Non-Interest Expense**

The following is a summary of changes in non-interest expense:

	<b>Three Months Ended</b>		<b>Amount</b>	<b>Percent</b>
	<b>Sept 30,</b>	<b>Sept 30,</b>		
	<b>2009</b>	<b>2008</b>	<b>Change</b>	<b>Change</b>
<b>Non-interest expense</b>				
Salaries and employee benefits	<b>\$4,166</b>	\$ 3,946	\$220	5.6%
Commissions	<b>373</b>	257	116	45.1%
Net occupancy expenses	<b>941</b>	944	(3)	-0.3%
Data processing	<b>419</b>	391	28	7.2%
Professional fees	<b>316</b>	263	53	20.2%
Outside services and consultants	<b>366</b>	328	38	11.6%
Loan expense	<b>631</b>	593	38	6.4%
FDIC deposit insurance	<b>400</b>	146	254	174.0%
Other (gains) losses	<b>(25)</b>	25	(50)	-200.0%
Other expenses	<b>1,342</b>	1,390	(48)	-3.5%
<b>Total non-interest expense</b>	<b>\$8,929</b>	\$ 8,283	\$646	7.8%

Non-interest expense increased from the third quarter of 2008. Salaries and benefits increased from the prior year primarily due to branch expansion and annual merit increases. Commissions paid to the mortgage loan division increased from the prior year based on the higher mortgage loan volume. Professional fees were higher compared to last year due to increasing rules and regulations requiring professional assistance from legal and accounting professionals. The Company's FDIC expense has increased significantly due to the higher assessment rates, including assessments imposed because of the Company's participation in the FDIC's Temporary Liquidity Guarantee Program (TLGP). Due to the recent difficult economic conditions, deposit insurance per account owner has been raised to \$250,000 for all types of accounts until January 1, 2014. The Company's participation in the TLGP allows non-interest bearing transaction accounts to receive unlimited insurance coverage until December 31, 2009, for increased FDIC insurance premiums of 10 basis points per \$100 of insured deposits. Deposit insurance will remain higher during the year based on the FDIC's rate increases. All other categories of non-interest expense did not have significant changes from the prior year.

	<b>Nine Months Ended</b>		<b>Amount</b>	<b>Percent</b>
	<b>Sept 30,</b>	<b>Sept 30,</b>		
	<b>2009</b>	<b>2008</b>	<b>Change</b>	<b>Change</b>
<b>Non-interest expense</b>				
Salaries and employee benefits	<b>\$12,689</b>	\$ 11,870	\$ 819	6.9%
Commissions	<b>1,575</b>	828	747	90.2%
Net occupancy expenses	<b>2,872</b>	2,834	38	1.3%
Data processing	<b>1,194</b>	1,073	121	11.3%
Professional fees	<b>1,021</b>	803	218	27.1%
Outside services and consultants	<b>1,043</b>	940	103	11.0%

Edgar Filing: HORIZON BANCORP /IN/ - Form 10-Q

Loan expense	<b>1,841</b>	1,603	238	14.8%
FDIC deposit insurance	<b>1,751</b>	404	1,347	333.4%
Other losses	<b>442</b>	267	175	65.5%
Other expenses	<b>3,826</b>	3,927	(101)	-2.6%
<b>Total non-interest expense</b>	<b>\$28,254</b>	\$ 24,549	\$3,705	15.1%

37

---

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**  
**Management's Discussion and Analysis of Financial Condition**  
**And Results of Operations**

**For the Three and Nine Months Ended September 30, 2009**

For the nine months ended September 30, 2009, non-interest expense increased compared to the same period last year. Salaries and benefits increased from the prior year primarily due to branch expansion and annual merit increases. Commissions paid to the mortgage loan division increased from the prior year based on the higher mortgage loan volume. Professional fees were higher compared to last year due to increasing rules and regulations requiring professional assistance from legal and accounting professionals. Also, loan expense was up from the prior year due to the increased volume of loan originations. The Company's FDIC expense has increased significantly due to higher assessment rates along with the special FDIC assessment of \$663,000 that was recorded in the second quarter of 2009 and due to the TLGP assessments discussed above. The FDIC has extended this insurance protection from December 31, 2009 until June 30, 2010, at a cost of 15 basis points per \$100 of insured deposits for financial institutions assigned to Risk Category I, unless a participating financial institution opted out on or before November 2, 2009. The Bank did not opt out, so this enhanced insurance protection will be available to its customers through June 30, 2010. Deposit insurance will remain higher during the year based on the FDIC's rate increases. Other losses for the first nine months of 2009 included a one-time charge of \$100,000 for the deductible paid on a wire transfer fraud totaling \$210,000 perpetrated on the bank during the first quarter of 2009 and \$229,000 in other real estate owned write-downs. All other categories of non-interest expense did not have significant changes from the prior year. On September 29, 2009, the FDIC issued a notice of proposed rule making (NPR) that would require insured depository institutions to prepay their quarterly risk-based assessments for the fourth quarter of 2009, and for all of 2010, 2011, and 2012, on December 30, 2009, along with each institution's risk based deposit insurance assessment for the third quarter of 2009. The NPR also provides that no additional special assessments would be imposed in 2009; current assessment rates would be maintained through December 31, 2010; and that there would be a uniform increase in risk based assessment rates of 3 basis points effective January 1, 2011. Based on current deposit levels, management estimates the amount of the prepayment would be \$5.7 million if the NPR is adopted as proposed.

**Income Taxes**

Income tax expense for the third quarter of 2009 was \$559,000 compared to \$2,000 of tax expense for the third quarter of 2008. The effective tax rate for the third quarter of 2009 was 19.2% compared to 0.0% in 2008.

Tax refunds were received in both nine-month periods ending September 30, 2009 and 2008 in the amounts of \$100,000 and \$163,000. Considering the impact of the \$538,000 of income received in the second quarter of 2008 from the death benefit on officer life insurance which was tax free and reduced taxable income and the tax refunds received in both periods, the effective tax rate for the nine months ending September 30, 2009 was 19.8% compared to 16.1% in 2008.

**Liquidity**

The Bank maintains a stable base of core deposits provided by long standing relationships with individuals and local businesses. These deposits are the principal source of liquidity for Horizon. Other sources of liquidity for Horizon include earnings, loan repayment, investment security sales and maturities, sale of residential mortgage loans, and borrowing relationships with correspondent banks, including the Federal Home Loan Bank (FHLB). During the nine months ended September 30, 2009, cash and cash equivalents decreased by approximately \$25.2 million. The decrease is primarily due to the growth in investment securities. At September 30, 2009, in addition to liquidity provided from the normal operating, funding, and investing activities of Horizon, the Bank had available approximately \$245.3 million in unused credit lines with various money center banks, including the FHLB.

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**  
**Management's Discussion and Analysis of Financial Condition**  
**And Results of Operations**  
**For the Three and Nine Months Ended September 30, 2009**

***Capital Resources***

The capital resources of Horizon and the Bank exceed regulatory capital ratios for well capitalized banks at September 30, 2009. Stockholders' equity totaled \$113.8 million as of September 30, 2009, compared to \$103.4 million as of December 31, 2008. For the three-months ended September 30, 2009, the ratio of average stockholders' equity to average assets was 8.53% compared to 6.65% for quarter ending December 31, 2008. Horizon's capital increased during the nine months as a result of increased earnings and an improvement in unrealized gain on securities available for sale net of dividends declared and the amortization of unearned compensation.

Horizon declared dividends in the amount of \$0.51 per share during the first nine months of 2009 compared to \$0.49 per share for the same period of 2008. The dividend payout ratio (dividends as a percent of net income) was 27.4% and 23.0% for the first nine months of 2009 and 2008. For additional information regarding dividend conditions, see Horizon's Annual Report on Form 10-K for 2008.

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES  
Management's Discussion and Analysis of Financial Condition  
And Results of Operations**

**For the Three and Nine Months Ended September 30, 2009**

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Refer to Horizon's 2008 Annual Report on Form 10-K for analysis of its interest rate sensitivity. Horizon believes there have been no significant changes in its interest rate sensitivity since it was reported in its 2008 Annual Report on Form 10-K.

**ITEM 4T. CONTROLS AND PROCEDURES**

**Evaluation Of Disclosure Controls And Procedures**

Based on an evaluation of disclosure controls and procedures as of September 30, 2009, Horizon's Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of Horizon's disclosure controls (as defined in Exchange Act Rule 13a-15(e) of the Securities Exchange Act of 1934 (the "Exchange Act")). Based on such evaluation, such officers have concluded that, as of the evaluation date, Horizon's disclosure controls and procedures are effective to ensure that the information required to be disclosed by Horizon in the reports it files under the Exchange Act is recorded, processed, summarized and reported within the time specified in Securities and Exchange Commission rules and forms and are designed to ensure that information required to be disclosed in those reports is accumulated and communicated to management as appropriate to allow timely decisions regarding disclosure.

**Changes In Internal Controls**

Horizon's management, including its Chief Executive Officer and Chief Financial Officer, also have concluded that during the fiscal quarter ended September 30, 2009, there have been no changes in Horizon's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, Horizon's internal control over financial reporting.

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**

**Part II Other Information**  
**For the Nine Months Ended September 30, 2009**

**ITEM 1. LEGAL PROCEEDINGS**

Horizon is continuing to investigate the legitimacy of claims made by First Horizon National Corporation, headquartered in Memphis, Tennessee ( FHNC ), regarding FHNC 's trademark rights in the name Horizon Bank (and other names that include the word Horizon ). An attorney representing FNHC raised the claims in a letter dated October 27, 2008, and proposed that Horizon assign its common law rights in that name to FHNC in exchange for a license back to use the Horizon name in Horizon 's current trade area and a reasonable zone of expansion. Horizon and its subsidiaries are involved in various legal proceedings incidental to the conduct of their business. Management does not expect that the outcome of any such proceedings will have a material adverse effect on our consolidated financial position or results of operations.

**ITEM 1A. RISK FACTORS**

There are certain risks and uncertainties in our business that could cause our actual results to differ materially from those anticipated. In ITEM 1A. RISK FACTORS of Part I of Horizon 's Annual Report on Form 10-K for the fiscal year ended December 31, 2008 (the 2008 Form 10-K ), Horizon included a detailed discussion of our risk factors. The following information updates certain of our risk factors and should be read in conjunction with the risk factors disclosed in the 2008 Form 10-K. These risk factors should be read carefully in connection with evaluating our business and in connection with the forward-looking statements contained in this Quarterly Report on Form 10-Q. Any of the risks described below or in the 2008 Form 10-K could materially adversely affect our business, financial condition or future results and the actual outcome of matters as to which forward-looking statements are made. These are not the only risks Horizon faces. Additional risks and uncertainties not currently known to us or that Horizon currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results.

***Risks Related to our Business***

**Changes in market interest rates could adversely affect our financial condition and results of operations.**

Our financial condition and results of operations are significantly affected by changes in market interest rates. Our results of operations depend substantially on our net interest income, which is the difference between the interest income that we earn on our interest-earning assets and the interest expense that we pay on our interest-bearing liabilities. Our profitability depends on our ability to manage our assets and liabilities during periods of changing market interest rates. If rates increase rapidly as a result of an improving economy, we may have to increase the rates paid on our deposits and borrowed funds more quickly than loans and investments re-price, resulting in a negative impact on interest spreads and net interest income. The impact of rising rates could be compounded if deposit customers move funds from savings accounts to higher rate certificate of deposit accounts. Conversely, should market interest rates fall below current levels, our net interest margin could also be negatively affected, as competitive pressures could keep us from further reducing rates on our deposits, and prepayments and curtailments on assets may continue. Such movements may cause a decrease in our interest rate spread and net interest margin, and therefore, decrease our profitability.

Changes in interest rates also could affect loan volume. For instance, an increase in interest rates could cause a decrease in the demand for mortgage loans, which could result in a significant decline in our revenue stream.



Table of Contents**HORIZON BANCORP AND SUBSIDIARIES****Part II Other Information****For the Nine Months Ended September 30, 2009**

We also are subject to reinvestment risk associated with changes in interest rates. Changes in interest rates may affect the average life of loans and mortgage-related securities. Increases in interest rates may decrease loan demand and/or may make it more difficult for borrowers to repay adjustable rate loans. Decreases in interest rates often result in increased prepayments of loans and mortgage-related securities, as borrowers refinance their loans to reduce borrowing costs. Under these circumstances, we are subject to reinvestment risk to the extent that we are unable to reinvest the cash received from such prepayments in loans or other investments that have interest rates that are comparable to the interest rates on existing loans and securities.

**Our deposit insurance premiums could be substantially higher in the future which will have an adverse effect on our future earnings.**

During 2008, there were higher levels of bank failures which dramatically increased the costs of the Federal Deposit Insurance Corporation ( FDIC ) and depleted the deposit insurance fund. In order to maintain a strong funding position and restore reserve ratios of the deposit insurance fund, the FDIC voted on December 16, 2008 to increase assessment rates of insured institutions uniformly by 7 basis points (7 cents for every \$100 of deposits), beginning with the first quarter of 2009. Additional changes, beginning April 1, 2009, were to require riskier institutions to pay a larger share of premiums by factoring in rate adjustments based on secured liabilities and unsecured debt levels.

On May 22, 2009, the FDIC adopted a final rule that imposed a special assessment for the second quarter of 2009 of 5 basis points on each insured depository institution's assets minus its Tier 1 capital as of June 30, 2009, which will be collected on September 30, 2009. Horizon's special assessment for this period was \$663,000. The FDIC further decided on May 22, 2009 that it could impose a similar assessment for each of the third and fourth quarters of 2009. The latest possible date for imposing additional special assessments under the final rule would be December 31, 2009, with collection on March 30, 2010.

On September 29, 2009, the FDIC issued a notice of proposed rule making ( NPR ) that would require insured depository institutions to prepay their quarterly risk-based assessments for the fourth quarter of 2009, and for all of 2010, 2011, and 2012, on December 30, 2009, along with each institution's risk based deposit insurance assessment for the third quarter of 2009. The NPR also provides that no additional special assessments would be imposed in 2009; current assessment rates would be maintained through December 31, 2010; and that there would be a uniform increase in risk based assessment rates of 3 basis points effective January 1, 2011. Based on current deposit levels, management estimates the amount of the prepayment would be \$5.7 million if the NPR is adopted as proposed. Horizon is generally unable to control the amount of premiums that Horizon is required to pay for FDIC insurance. As a result, Horizon may be required to pay even higher FDIC premiums than the recently increased levels. These announced increases and any future increases in FDIC insurance premiums may materially adversely affect our results of operations and our ability to continue to pay dividends on our common shares at the current rate.

**Because of our participation in the TARP Capital Purchase Program, Horizon is subject to various restrictions on dividends, share repurchases and executive compensation.**

Horizon is a participant in the Capital Purchase Program, which is a component program of the Troubled Assets Relief Program ( TARP ) established by the United States Department of the Treasury (the U.S. Treasury ) pursuant to the Emergency Economic Stabilization Act of 2008 ( EESA ). Pursuant to the agreements Horizon entered into as part of the Capital Purchase Program, Horizon is unable to declare dividend payments on our common shares if Horizon is in arrears on the payment of dividends on the Series A Preferred Shares Horizon issued to the U.S. Treasury. Further, Horizon is not permitted to increase dividends on our common shares above the amount of the last quarterly cash dividend per common share declared prior to October 14, 2008 (\$0.17 per common share) without the U.S. Treasury's approval until

**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**  
**Part II Other Information**  
**For the Nine Months Ended September 30, 2009**

December 23, 2011, unless all of the Series A Preferred Shares have been redeemed or transferred by the U.S. Treasury to unaffiliated third parties.

In addition, our ability to repurchase our shares is restricted. The consent of the U.S. Treasury generally is required for us to make any share repurchase (other than in connection with the administration of any employee benefit plan in the ordinary course of business and consistent with past practice) until December 23, 2011, unless all of the Series A Preferred Shares have been redeemed or transferred by the U.S. Treasury to unaffiliated third parties. Further, our common shares may not be repurchased if Horizon is in arrears on the payment of Series A Preferred Share dividends to the U.S. Treasury.

As a recipient of government funding under the Capital Purchase Program, Horizon must also comply with the executive compensation and corporate governance standards imposed by the American Recovery and Reinvestment Act of 2009 (the ARRA ) and the standards established by the Secretary of the Treasury under the ARRA, for so long as the U.S. Treasury holds any of our securities or upon exercise of the Warrant Horizon issued to the U.S. Treasury as part of the Capital Purchase Program, excluding any period during which the U.S. Treasury holds only the Warrant (the TARP Period ). On September 15, 2009, the Secretary of the Treasury established executive compensation and corporate governance standards applicable to TARP recipients, including Horizon, by promulgating an Interim Final Rule under 31 C.F.R. Part 30 (the Interim Final Rule ). The ARRA and the Interim Final Rule impose limitations on our executive compensation practices by:

- Limiting the deductibility, for U.S. federal income tax purposes, of compensation paid to any of our Senior Executive Officers (as defined in the Interim Final Rule) to \$500,000 per year;

- Prohibiting the payment or accrual of any bonus, retention award or incentive compensation to our five most highly-compensated employees, except in the form and under the limited circumstances permitted by the Interim Final Rule;

- Prohibiting the payment of golden parachute payments (as defined in the Interim Final Rule) to our Senior Executive Officers or any of our next five most highly-compensated employees upon a departure from Horizon or due to a change in control of Horizon, except for payments for services performed or benefits accrued;

- Requiring Horizon to clawback any bonus, retention award or incentive compensation paid (or under a legally binding obligation to be paid) to a Senior Executive Officer or any of our next 20 most highly-compensated employees if the payment was based on materially inaccurate financial statements or any other materially inaccurate performance metric criteria;

- Prohibiting Horizon from maintaining any employee compensation plan (as defined in the Interim Final Rule) that would encourage the manipulation of our reported earnings to enhance the compensation of any of our employees;

- Prohibiting Horizon from maintaining compensation plans and arrangements for our Senior Executive Officers that encourage our Senior Executive Officers to take unnecessary and excessive risks that threaten the value of Horizon;

- Prohibiting Horizon from providing (formally or informally) gross-ups to any of our Senior Executive Officers or our next 20 most highly-compensated employees; and

- Subjecting any bonus, retention award or other compensation paid before February 17, 2009 to our Senior Executive Officers or our next 20 most highly-compensated employees to retroactive review



**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**

**Part II Other Information**

**For the Nine Months Ended September 30, 2009**

by the U.S. Treasury to determine whether any such payments were inconsistent with the purposes of TARP or otherwise contrary to the public interest.

The ARRA and the Interim Final Rule also required that the Horizon Board of Directors adopt a Company-wide policy regarding excessive or luxury expenditures, which Horizon has done.

Although Horizon was already in compliance with many of these standards and limitations prior to its participation in the Capital Purchase Program and the subsequent adoption of the ARRA and the Interim Final Rule, these standards and limitations decrease (in some cases substantially) Horizon's discretion over certain decisions regarding its dividend practices and how it compensates its executive officers and other employees. The limitations on compensation may have the effect of limiting Horizon's ability to attract and retain executive officers and other employees which will be detrimental to our long-term success.

**The TARP lending goals may not be attainable and may adversely affect our business and asset quality.**

Congress and the bank regulators have encouraged recipients of TARP capital, including Horizon, to use such capital to make more loans, and it may not be possible to safely, soundly and profitably make sufficient loans to creditworthy persons in the current economy to satisfy such goals. Congressional demands for additional lending by TARP capital recipients, and regulatory demands for demonstrating and reporting such lending are increasing. On November 12, 2008, the bank regulatory agencies issued a statement encouraging banks to, among other things, lend prudently and responsibly to creditworthy borrowers and to work with borrowers to preserve homeownership and avoid preventable foreclosures. Horizon continues to lend (and have been able to expand our lending using the funds Horizon received through the Capital Purchase Program) and to report our lending to the U.S. Treasury. The future demands for additional lending, however, are unclear and uncertain, and Horizon could be forced to make loans that involve risks or terms that Horizon would not otherwise find acceptable or in our shareholders' best interest. Such loans could adversely affect our results of operations and financial condition, and may be in conflict with bank regulations and requirements as to liquidity and capital. The profitability of funding such loans using deposits may also be adversely affected by increased FDIC insurance premiums.

**Our ability to repurchase the preferred shares issued to the U.S. Treasury (and therefore obtain relief from the limitations and restrictions of TARP and ARRA) is limited.**

The rules and policies applicable to recipients of capital under the TARP Capital Purchase Program continue to evolve and their scope, timing and effect cannot be predicted. Any redemption of the securities sold to the U.S. Treasury to avoid these restrictions would require prior Federal Reserve and U.S. Treasury approval. Based on recently issued Federal Reserve guidelines, institutions seeking to redeem the preferred stock issued pursuant to the Capital Purchase Program must demonstrate an ability to access the long-term debt markets without reliance on the FDIC's Temporary Liquidity Guarantee Program, successfully demonstrate access to public equity markets and meet a number of additional requirements and considerations before Horizon can redeem any securities sold to the U.S. Treasury. Therefore, it is uncertain if Horizon will be able to redeem such securities even if Horizon has sufficient financial resources to do so.

**Table of Contents****HORIZON BANCORP AND SUBSIDIARIES****Part II Other Information****For the Nine Months Ended September 30, 2009****ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

The following table presents information with respect to shares of Common Stock the Company withheld during the quarter ended September 30, 2009:

**Issuer Purchases of Equity Securities**

	<b>Total Number of Shares Purchased</b>	<b>Average Price Paid Per Share</b>	<b>Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs</b>	<b>Minimum Number of Shares That may yet be Purchased Under the Plan or Program</b>
July 1 - 31, 2009		\$		
August 1 - 30, 2009	13,000 (1)	15.75		
September 1 - 30, 2009				

(1) The 13,000 shares withheld were not part of a publicly announced repurchase plan or program. These shares were withheld and then sold on the open market by Horizon as payment for taxes associated with the vesting of restricted stock exercises.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

Not Applicable

**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

Not Applicable

**ITEM 5. OTHER INFORMATION**

Not Applicable



**Table of Contents**

**HORIZON BANCORP AND SUBSIDIARIES**  
**Part II Other Information**  
**For the Nine Months Ended September 30, 2009**

**ITEM 6. EXHIBITS**

(a) Exhibits

- Exhibit 3.1 Amended and Restated Bylaws of Horizon Bancorp (as amended through July 14, 2009) (incorporated by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K filed on July 16, 2009)
- Exhibit 31.1 Certification of Craig M. Dwight
- Exhibit 31.2 Certification of Mark E. Secor
- Exhibit 32 Certification of Chief Executive and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

**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.

HORIZON BANCORP

Dated: November 12, 2009

/s/ Craig M. Dwight

Craig M. Dwight  
Chief Executive Officer

Dated: November 12, 2009

/s/ Mark E. Secor

Mark E. Secor  
Chief Financial Officer

47

---



**Table of Contents**

**INDEX TO EXHIBITS**

The following documents are included as Exhibits to this Report.

**Exhibit**

- 31.1 Certification of Craig M. Dwight
- 31.2 Certification of Mark E. Secor
- 32 Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

48