

HORIZON BANCORP /IN/
Form 10-Q
November 14, 2011
[Table of Contents](#)

United States
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

**QUARTERLY REPORT UNDER SECTION 13 OR 15 (d) OF
THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended September 30, 2011

Commission file number 0-10792

HORIZON BANCORP

(Exact name of registrant as specified in its charter)

Indiana
(State or other jurisdiction of

35-1562417
(I.R.S. Employer

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

incorporation or organization)

Identification No.)

515 Franklin Square,

Michigan City, Indiana
(Address of principal executive offices)

46360
(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 Do not check if a smaller reporting company

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: 3,309,512 shares of Common Stock, no par value, at November 14, 2011.

Table of Contents

HORIZON BANCORP

FORM 10-Q

INDEX

PART I. FINANCIAL INFORMATION

Item 1.	Financial Statements	
	<u>Condensed Consolidated Balance Sheets</u>	3
	<u>Condensed Consolidated Statements of Income</u>	4
	<u>Condensed Consolidated Statement of Stockholders' Equity</u>	5
	<u>Condensed Consolidated Statements of Cash Flows</u>	6
	<u>Notes to Condensed Consolidated Financial Statements</u>	7
Item 2.	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	33
Item 3.	<u>Quantitative and Qualitative Disclosures about Market Risk</u>	48
Item 4.	<u>Controls and Procedures</u>	48

PART II. OTHER INFORMATION

Item 1.	<u>Legal Proceedings</u>	49
Item 1A.	<u>Risk Factors</u>	49
Item 2.	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	60
Item 3.	<u>Defaults Upon Senior Securities</u>	61
Item 4.	<u>(Removed and reserved)</u>	61
Item 5.	<u>Other Information</u>	61
Item 6.	<u>Exhibits</u>	62
	<u>Signatures</u>	63
	<u>Index To Exhibits</u>	64

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

(Dollar Amounts in Thousands)

	September 30 2011 (Unaudited)	December 31 2010
Assets		
Cash and due from banks	\$ 18,462	\$ 15,683
Investment securities, available for sale	430,702	382,344
Investment securities, held to maturity	10,632	9,595
Loans held for sale	12,300	18,833
Loans, net of allowance for loan losses of \$19,110 and \$19,064	906,730	863,813
Premises and equipment	34,289	34,194
Federal Reserve and Federal Home Loan Bank stock	12,390	13,664
Goodwill	5,910	5,910
Other intangible assets	2,403	2,741
Interest receivable	6,651	6,519
Cash value life insurance	29,959	27,195
Other assets	20,382	20,428
Total assets	\$ 1,490,810	\$ 1,400,919
Liabilities		
Deposits		
Non-interest bearing	\$ 121,483	\$ 107,606
Interest bearing	868,266	877,892
Total deposits	989,749	985,498
Borrowings	336,095	260,741
Subordinated debentures	30,653	30,584
Interest payable	582	781
Other liabilities	15,051	11,032
Total liabilities	1,372,130	1,288,636
Commitments and contingent liabilities		
Stockholders Equity		
Preferred stock, \$.01 par value, \$1,000 liquidation value Authorized, 1,000,000 Series A shares Issued 0 and 18,750 shares		18,217
Preferred stock, \$.01 par value, \$1,000 liquidation value Authorized, 1,000,000 Series B shares Issued 12,500 and 0 shares	12,500	
Common stock, \$.2222 stated value Authorized, 22,500,000 shares Issued, 3,309,512 and 3,300,659 shares	1,126	1,122
Additional paid-in capital	10,579	10,356
Retained earnings	86,524	80,240
Accumulated other comprehensive income	7,951	2,348
Total stockholders equity	118,680	112,283

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

Total liabilities and stockholders' equity	\$ 1,490,810	\$ 1,400,919
--	---------------------	--------------

See notes to condensed consolidated financial statements

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

(Dollar Amounts in Thousands, Except Per Share Data)

	Three Months Ended September 30		Nine Months Ended September 30	
	2011	2010	2011	2010
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
Interest Income				
Loans receivable	\$ 12,481	\$ 14,466	\$ 36,260	\$ 40,283
Investment securities				
Taxable	2,542	2,431	7,828	7,394
Tax exempt	988	979	3,066	3,138
Total interest income	16,011	17,876	47,154	50,815
Interest Expense				
Deposits	1,978	2,769	6,510	8,238
Borrowed funds	1,583	2,026	4,760	6,807
Subordinated debentures	459	461	1,363	1,229
Total interest expense	4,020	5,256	12,633	16,274
Net Interest Income	11,991	12,620	34,521	34,541
Provision for loan losses	1,564	2,657	4,444	8,890
Net Interest Income after Provision for Loan Losses	10,427	9,963	30,077	25,651
Other Income				
Service charges on deposit accounts	802	921	2,422	2,750
Wire transfer fees	167	211	412	536
Interchange fees	721	649	1,905	1,663
Fiduciary activities	1,016	934	2,911	2,936
Gain on sale of securities	1,115	336	1,754	467
Gain on sale of mortgage loans	2,145	2,473	3,986	5,529
Mortgage servicing income net of impairment	(172)	(331)	691	(363)
Increase in cash surrender value of bank owned life insurance	245	246	661	599
Death benefit on officer life insurance	453		453	
Other income	46	209	105	828
Total other income	6,538	5,648	15,300	14,945
Other Expenses				
Salaries and employee benefits	6,081	5,985	16,912	15,973
Net occupancy expenses	1,056	1,036	3,176	3,077
Data processing	549	502	1,450	1,474
Professional fees	359	417	1,039	1,418
Outside services and consultants	454	374	1,221	1,163
Loan expense	820	855	2,276	2,376
FDIC insurance expense	254	423	944	1,219
Other losses	1,088	143	1,365	180
Other expenses	1,652	1,522	4,675	4,115

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

Total other expenses	12,313	11,257	33,058	30,995
Income Before Income Tax	4,652	4,354	12,319	9,601
Income tax expense	1,235	1,075	3,044	2,016
Net Income	3,417	3,279	9,275	7,585
Preferred stock dividend and discount accretion	(710)	(353)	(1,263)	(1,057)
Net Income Available to Common Shareholders	\$ 2,707	\$ 2,926	\$ 8,012	\$ 6,528
Basic Earnings Per Share	\$ 0.82	\$ 0.89	\$ 2.44	\$ 1.99
Diluted Earnings Per Share	0.80	0.88	2.37	1.96

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)

	Preferred Stock	Common Stock	Additional Paid-in Capital	Comprehensive Income	Retained Earnings	Accumulated Other Comprehensive Income	Total
Balances, December 31, 2010	\$ 18,217	\$ 1,122	\$ 10,356		\$ 80,240	\$ 2,348	\$ 112,283
Net income				\$ 9,275	9,275		9,275
Redemption of preferred stock	(18,750)						(18,750)
Issuance of preferred stock	12,500						12,500
Other comprehensive income, net of tax:							
Unrealized gain on securities				7,871		7,871	7,871
Unrealized losses on derivative instruments				(2,268)		(2,268)	(2,268)
Comprehensive income				\$ 14,878			
Amortization of unearned compensation			77				77
Issuance of restricted shares		3	57				60
Exercise of stock options		1	54				55
Tax benefit related to stock options			8				8
Stock option expense			27				27
Cash dividends on preferred stock (5.00%)					(730)		(730)
Cash dividends on common stock (\$.52 per share)					(1,728)		(1,728)
Accretion of discount on preferred stock	533				(533)		
Balances, September 30, 2011	\$ 12,500	\$ 1,126	\$ 10,579		\$ 86,524	\$ 7,951	\$ 118,680

See notes to condensed consolidated financial statements

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

(Dollar Amounts in Thousands)

	Nine Months Ended September 30	
	2011	2010
	(Unaudited)	(Unaudited)
Operating Activities		
Net income	\$ 9,275	\$ 7,585
Items not requiring (providing) cash		
Provision for loan losses	4,444	8,890
Depreciation and amortization	1,868	1,715
Share based compensation	27	20
Mortgage servicing rights impairment	(464)	409
Deferred income tax		(923)
Premium amortization on securities available for sale, net	1,612	1,326
Gain on sale of investment securities	(1,754)	(467)
Gain on sale of mortgage loans	(3,986)	(5,529)
Proceeds from sales of loans	178,239	188,564
Loans originated for sale	(174,253)	(184,368)
Change in cash surrender value of life insurance	236	(566)
(Gain) loss on sale of other real estate owned	126	(352)
Net change in		
Interest receivable	(132)	(195)
Interest payable	(199)	(369)
Other assets	(1,590)	5,010
Other liabilities	1,416	1,776
Net cash provided by operating activities	14,865	22,526
Investing Activities		
Purchases of securities available for sale	(170,689)	(165,749)
Proceeds from sales, maturities, calls, and principal repayments of securities available for sale	134,583	157,412
Purchase of securities held to maturity	(2,437)	(15,332)
Proceeds from maturities of securities held to maturity	1,400	13,500
(Purchase) proceeds from the sale of Federal Home Loan Bank stock	1,274	(78)
Net change in loans	(44,766)	(40,260)
Proceeds on the sale of OREO and repossessed assets	2,008	2,982
Purchases of premises and equipment	(1,548)	(2,020)
Purchases of bank owned life insurance	(3,000)	
Purchases and assumption of ATSB		3,406
Net cash used in investing activities	(83,175)	(46,139)
Financing Activities		
Net change in		
Deposits	4,251	(50,242)
Borrowings	75,423	25,774
Redemption of preferred stock	(18,750)	
Issuance of preferred stock	12,500	
Proceeds from issuance of stock	115	120
Tax benefit from issuance of stock	8	77
Dividends paid on common shares	(1,728)	(1,679)

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

Dividends paid on preferred shares	(730)	(937)
Net cash provided by (used in) financing activities	71,089	(26,887)
Net Change in Cash and Cash Equivalent	2,779	(50,500)
Cash and Cash Equivalents, Beginning of Period	15,683	68,702
Cash and Cash Equivalents, End of Period	\$ 18,462	\$ 18,202
Additional Cash Flows Information		
Interest paid	\$ 12,832	\$ 16,643
Income taxes paid	2,100	2,180
Transfer of loans to other real estate owned	4,273	7,937
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 condensed 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, 2011 and September 30, 2010 are not necessarily indicative of the operating results for the full year of 2011 or 2010. 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 condensed 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 2010 filed with the Securities and Exchange Commission on March 11, 2011. The consolidated condensed balance sheet of Horizon as of December 31, 2010 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. The following table shows computation of basic and diluted earnings per share.

	Three months ended September 30		Nine months ended September 30	
	2011 (Unaudited)	2010 (Unaudited)	2011 (Unaudited)	2010 (Unaudited)
Basic earnings per share				
Net income	\$ 3,417	\$ 3,279	\$ 9,275	\$ 7,585
Less: Preferred stock dividends and accretion of discount	710	353	1,263	1,057
Net income available to common shareholders	\$ 2,707	\$ 2,926	\$ 8,012	\$ 6,528
Weighted average common shares outstanding	3,295,130	3,279,201	3,289,911	3,275,969
Basic earnings per share	\$ 0.82	\$ 0.89	\$ 2.44	\$ 1.99
Diluted earnings per share				
Net income available to common shareholders	\$ 2,707	\$ 2,926	\$ 8,012	\$ 6,528
Weighted average common shares outstanding	3,295,130	3,279,201	3,289,911	3,275,969
Effect of dilutive securities:				
Warrants	72,589	42,397	74,519	31,953
Restricted stock	1,955	14,295	6,078	12,910
Stock options	6,579	741	6,803	2,998
Weighted average shares outstanding	3,376,253	3,336,634	3,377,311	3,323,830
Diluted earnings per share	\$ 0.80	\$ 0.88	\$ 2.37	\$ 1.96

At September 30, 2011 and 2010, there were 20,500 shares and 48,000 shares that were not included in the computation of diluted earnings per share because they were non-dilutive.

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

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

Horizon has share-based employee compensation plans, which are described in the notes to the financial statements included in the December 31, 2010 Annual Report on Form 10-K.

Reclassifications

Certain reclassifications have been made to the 2010 consolidated financial statements to be comparable to 2011. These reclassifications had no effect on net income.

Note 2 Securities

The fair value of securities is as follows:

September 30, 2011 (Unaudited)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale				
U.S. Treasury and federal agencies	\$ 10,818	\$ 358	\$	\$ 11,176
State and municipal	136,147	7,648	(45)	143,750
Federal agency collateralized mortgage obligations	87,688	2,407		90,095
Federal agency mortgage-backed pools	175,090	6,633		181,723
Private labeled mortgage-backed pools	3,817	116		3,933
Corporate notes	42		(17)	25
Total available for sale investment securities	\$ 413,602	\$ 17,162	\$ (62)	\$ 430,702
Held to maturity, State and Municipal	\$ 10,632	\$	\$	\$ 10,632

December 31, 2010	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale				
U.S. Treasury and federal agencies	\$ 24,727	\$ 643	\$ (119)	\$ 25,251
State and municipal	132,380	1,511	(2,402)	131,489
Federal agency collateralized mortgage obligations	100,106	1,945	(214)	101,837
Federal agency mortgage-backed pools	114,390	3,865	(360)	117,895
Private labeled mortgage-backed pools	5,197	126		5,323
Corporate notes	555		(6)	549
Total available for sale investment securities	\$ 377,355	\$ 8,090	\$ (3,101)	\$ 382,344
Held to maturity, State and Municipal	\$ 9,595	\$	\$	\$ 9,595

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

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-temporary impairment is identified. At September 30, 2011, 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 United States Department of the Treasury (U.S. Treasury) and federal agencies, securities of state and municipal governmental agencies, and federal agency mortgage-backed pools were caused by interest rate volatility 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. 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 at maturity, the Company did not consider those investments to be other-than-temporarily impaired at September 30, 2011.

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

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

The amortized cost and fair value of securities available for sale and held to maturity at September 30, 2011 and December 31, 2010, 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, 2011 (Unaudited)		December 31, 2010	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Available for sale				
Within one year	\$ 1,070	\$ 1,079	\$ 855	\$ 866
One to five years	27,187	28,257	28,240	28,949
Five to ten years	51,311	54,380	44,179	44,450
After ten years	67,439	71,235	84,388	83,024
	147,007	154,951	157,662	157,289
Federal agency collateralized mortgage obligations	87,688	90,095	100,106	101,837
Federal agency mortgage-backed pools	175,090	181,723	114,390	117,895
Private labeled mortgage-backed pools	3,817	3,933	5,197	5,323
Total available for sale investment securities	\$ 413,602	\$ 430,702	\$ 377,355	\$ 382,344
Held to maturity				
Within one year	\$ 10,532	\$ 10,532	\$ 9,495	\$ 9,495
One to five years	100	100	100	100
Total held to maturity investment securities	\$ 10,632	\$ 10,632	\$ 9,595	\$ 9,595

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

	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
September 30, 2011 (Unaudited)						
U.S. Treasury and federal agencies	\$	\$	\$	\$	\$	\$
State and municipal	2,984	(41)	495	(4)	3,479	(45)
Federal agency collateralized mortgage obligations						
Federal agency mortgage-backed pools			25		25	
Corporate notes	26	(17)			26	(17)
Total temporarily impaired securities	\$ 3,010	\$ (58)	\$ 520	\$ (4)	\$ 3,530	\$ (62)

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

	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
December 31, 2010						
U.S. Treasury and federal agencies	\$ 9,881	\$ (119)	\$	\$	\$ 9,881	\$ (119)
State and municipal	60,401	(2,370)	568	(32)	60,969	(2,402)
Federal agency collateralized mortgage obligations	21,130	(214)			21,130	(214)
Federal agency mortgage-backed pools	27,033	(360)	32		27,065	(360)
Corporate notes	26	(6)			26	(6)
Total temporarily impaired securities	\$ 118,471	\$ (3,069)	\$ 600	\$ (32)	\$ 119,071	\$ (3,101)

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

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

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Sales of securities available for sale (Unaudited)				
Proceeds	\$ 153,299	\$ 146,811	\$ 170,689	\$ 165,749
Gross gains	1,115	464	1,754	599
Gross losses		128		132

Note 3 Loans

	September 30 2011 (Unaudited)	December 31 2010
Commercial		
Working capital and equipment	\$ 167,387	\$ 151,414
Real estate, including agriculture	167,924	167,785
Tax exempt	3,474	2,925
Other	6,581	7,894
Total	345,366	330,018
Real estate		
1-4 family	161,166	157,478
Other	4,263	4,957
Total	165,429	162,435
Consumer		
Auto	134,718	136,014
Recreation	4,795	6,086
Real estate/home improvement	27,378	29,184
Home equity	91,125	90,580
Unsecured	3,200	3,091
Other	2,718	1,726
Total	263,934	266,681
Mortgage warehouse	151,111	123,743
Total	151,111	123,743
Total loans	925,840	882,877
Allowance for loan losses	(19,110)	(19,064)
Loans, net	\$ 906,730	\$ 863,813

Commercial

Commercial loans are primarily based on the identified cash flows of the borrower and secondarily on the underlying collateral provided by the borrower. The cash flows of borrowers, however, may not be as expected and the collateral securing these loans may fluctuate in value. Most commercial loans are secured by the assets being financed or other business assets such as accounts receivable or inventory and may incorporate a personal guarantee; however, some short-term loans may be made on an unsecured basis. In the case of loans secured by accounts receivable,

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

the availability of funds for the repayment of these loans may be substantially dependent on the ability of the borrower to collect amounts due from its customers.

Commercial real estate loans are viewed primarily as cash flow loans and secondarily as loans secured by real estate. Commercial real estate lending typically involves higher loan principal amounts and the repayment of these loans is generally dependent on the successful operation of the property securing the loan or the business conducted on the property securing the loan. Commercial real estate loans may be more adversely

Table of Contents

HORIZON BANCORP AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

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

affected by conditions in the real estate markets or in the general economy. The properties securing the Company's commercial real estate portfolio are diverse in terms of property type, which are monitored for concentrations of credit. Management monitors and evaluates commercial real estate loans based on collateral, cash flow and risk grade criteria. As a general rule, the Company avoids financing single purpose projects, such as churches, schools, restaurants, and golf courses unless other underwriting factors are present to help mitigate risk. In addition, management tracks the level of owner-occupied commercial real estate loans versus non-owner occupied loans.

Real Estate and Consumer

With respect to residential loans that are secured by 1-4 family residences and are generally owner occupied, the Company generally establishes a maximum loan-to-value ratio and requires private mortgage insurance if that ratio is exceeded. Home equity loans are typically secured by a subordinate interest in 1-4 family residences, and consumer loans are secured by consumer assets such as automobiles or recreational vehicles. Some consumer loans are unsecured such as small installment loans and certain lines of credit. Repayment of these loans is primarily dependent on the personal income of the borrowers, which can be impacted by economic conditions in their market areas such as unemployment levels. Repayment can also be impacted by changes in property values on residential properties. Risk is mitigated by the fact that the loans are of smaller individual amounts and spread over a large number of borrowers.

Mortgage Warehousing

Horizon's mortgage warehouse lending has specific mortgage companies as customers of Horizon Bank. Individual mortgage loans originated by these mortgage companies are funded as a secured borrowing with pledge of collateral under Horizon's agreement with the mortgage company. Each individual mortgage is assigned to Horizon until the loan is sold to the secondary market by the mortgage company. In addition, Horizon takes possession of each original note and forwards such note to the end investor once the mortgage company has sold the loan. At the time a loan is transferred to the secondary market, the mortgage company repurchases the loan under its option within the agreement. Due to the repurchase feature contained in the agreement, the transaction does not qualify as a sale and therefore is accounted for as a secured borrowing with pledge of collateral pursuant to the agreement with the mortgage company. When the individual loan is sold to the end investor by the mortgage company the proceeds from the sale of the loan are received by Horizon and used to payoff the loan balance with Horizon along with any accrued interest and any related fees. The remaining balance from the sale is forwarded to the mortgage company. These individual loans typically are sold by the mortgage company within 30 days and are seldom held more than 90 days. Interest income is accrued during this period and collected at the time each loan is sold. Fee income for each loan sold is collected when the loan is sold and no costs are deferred due to the term between each loan funding and related payoff is typically less than 30 days.

Based on the agreements with each mortgage company, at any time a mortgage company can repurchase from Horizon their outstanding loan balance on an individual mortgage and regain possession of the original note. Horizon also has the option to request that the mortgage company repurchase an individual mortgage. Should this occur, Horizon would return the original note and reassign the assignment of the mortgage to the mortgage company. Also, in the event that the end investor would not be able to honor the sales commitment and the mortgage company would not be able to repurchase its loan on an individual mortgage, Horizon would be able to exercise its rights under the agreement.

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 the recorded investment of individual loan categories.

September 30, 2011 (unaudited)	Loan Balance	Interest Due	Deferred Fees / (Costs)	Recorded Investment
Owner occupied real estate	\$ 128,696	\$ 385	\$ 28	\$ 129,109
Non owner occupied real estate	141,643	377	84	142,104
Residential spec homes	2,598	2		2,600
Development & spec land loans	7,548	10		7,558
Commercial and industrial	64,765	227	4	64,996
Total commercial	345,250	1,001	116	346,367
Residential mortgage	157,870	579	64	158,513
Residential construction	7,495	13		7,508
Mortgage warehouse	151,111			151,111
Total real estate	316,476	592	64	317,132
Direct installment	23,994	82	(357)	23,719
Direct installment purchased	1,100			1,100
Indirect installment	127,665	397	1	128,063
Home equity	112,272	533	(741)	112,064
Total consumer	265,031	1,012	(1,097)	264,946
Total loans	926,757	2,605	(917)	928,445
Allowance for loan losses	(19,110)			(19,110)
Net loans	\$ 907,647	\$ 2,605	\$ (917)	\$ 909,335

December 31, 2010	Loan Balance	Interest Due	Deferred Fees / (Costs)	Recorded Investment
Owner occupied real estate	\$ 125,883	\$ 442	\$ 26	\$ 126,351
Non owner occupied real estate	136,986	364	87	137,437
Residential spec homes	2,257	4	(2)	2,259
Development & spec land loans	6,439	14		6,453
Commercial and industrial	58,336	234	6	58,576
Total commercial	329,901	1,058	117	331,076
Residential mortgage	154,891	592	76	155,559
Residential construction	7,467	13	1	7,481
Mortgage warehouse	123,743	332		124,075
Total real estate	286,101	937	77	287,115
Direct installment	23,527	97	(338)	23,286

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

Direct installment purchased	1,869			1,869
Indirect installment	128,122	491	7	128,620
Home equity	114,202	563	(708)	114,057
Total consumer	267,720	1,151	(1,039)	267,832
Total loans	883,722	3,146	(845)	886,023
Allowance for loan losses	(19,064)			(19,064)
Net loans	\$ 864,658	\$ 3,146	\$ (845)	\$ 866,959

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

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

Note 4 Allowance for Loan Losses

The historical loss experience is determined by portfolio segment and is based on the actual loss history experienced by the Company over the prior one to five years. Management believes the two-year historical loss experience methodology is appropriate in the current economic environment, as it captures loss rates that are comparable to the current period being analyzed.

	Three Months Ended		Nine Months Ended	
	September 30 2011 (Unaudited)	September 30 2010 (Unaudited)	September 30 2011 (Unaudited)	September 30 2010 (Unaudited)
Balance at beginning of the period	\$ 18,586	\$ 16,543	\$ 19,064	\$ 16,015
Loans charged-off:				
Commercial				
Owner occupied real estate	65	350	189	1,308
Non owner occupied real estate	196		310	288
Residential development				780
Development & Spec Land Loans				907
Commercial and industrial	17	150	227	
Total commercial	278	500	726	3,283
Real estate				
Residential mortgage	86	86	837	683
Residential construction				
Mortgage warehouse				
Total real estate	86	86	837	683
Consumer				
Direct Installment	78	91	480	430
Direct Installment Purchased				
Indirect Installment	494	460	1,280	2,189
Home Equity	359	215	1,888	1,083
Total consumer	931	766	3,648	3,702
Total loans charged-off	1,295	1,352	5,211	7,668
Recoveries of loans previously charged-off:				
Commercial				
Owner occupied real estate		5	18	5
Non owner occupied real estate				
Residential development				66
Development & Spec Land Loans				
Commercial and industrial	9	15	14	15
Total commercial	9	20	32	86
Real estate				
Residential mortgage			10	1

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

Residential construction				
Mortgage warehouse				
Total real estate			10	1
Consumer				
Direct Installment	16	9	83	49
Direct Installment Purchased				
Indirect Installment	179	147	568	646
Home Equity	51	6	120	11
Total consumer	246	162	771	706
Total loan recoveries	255	182	813	793
Net loans charged-off	1,040	1,170	4,398	6,875
Provision charged to operating expense	1,564	2,657	4,444	8,890
Balance at the end of the period	\$ 19,110	\$ 18,030	\$ 19,110	\$ 18,030

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

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

Management's general practice is to proactively charge down loans individually evaluated for impairment to the fair value of the underlying collateral.

Consistent with regulatory guidance, charge-offs on all loan segments are taken when specific loans, or portions thereof, are considered uncollectible. The Company's policy is to promptly charge these loans off in the period the uncollectible loss is reasonably determined.

For all loan portfolio segments except 1-4 family residential properties and consumer, the Company promptly charges-off loans, or portions thereof, when available information confirms that specific loans are uncollectible based on information that includes, but is not limited to, (1) the deteriorating financial condition of the borrower, (2) declining collateral values, and/or (3) legal action, including bankruptcy, that impairs the borrower's ability to adequately meet its obligations. For impaired loans that are considered to be solely collateral dependent, a partial charge-off is recorded when a loss has been confirmed by an updated appraisal or other appropriate valuation of the collateral.

The Company charges-off 1-4 family residential and consumer loans, or portions thereof, when the Company reasonably determines the amount of the loss. The Company adheres to timeframes established by applicable regulatory guidance which provides for the charge-down of 1-4 family first and junior lien mortgages to the net realizable value less costs to sell when the loan is 180 days past due, charge-off of unsecured open-end loans when the loan is 90 days past due, and charge down to the net realizable value when other secured loans are 90 days past due. Loans at these respective delinquency thresholds for which the Company can clearly document that the loan is both well-secured and in the process of collection, such that collection will occur regardless of delinquency status, need not be charged off.

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment analysis:

September 30, 2011 (Unaudited)	Commercial	Real Estate	Mortgage Warehousing	Consumer	Total Allowance
Allowance For Loan Losses					
Ending allowance balance attributable to loans:					
Individually evaluated for impairment	\$ 1,806	\$	\$	\$	\$ 1,806
Collectively evaluated for impairment	6,345	2,457	1,477	7,025	17,304
Total ending allowance balance	\$ 8,151	\$ 2,457	\$ 1,477	\$ 7,025	\$ 19,110
Loans:					
Individually evaluated for impairment	\$ 12,562	\$	\$	\$	\$ 12,562
Collectively evaluated for impairment	333,805	166,021	151,111	264,946	915,883
Total ending loans balance	\$ 346,367	\$ 166,021	\$ 151,111	\$ 264,946	\$ 928,445

December 31, 2010	Commercial	Real Estate	Mortgage Warehousing	Consumer	Total Allowance
Allowance For Loan Losses					
Ending allowance balance attributable to loans:					
Individually evaluated for impairment	\$ 1,457	\$	\$	\$	\$ 1,457
Collectively evaluated for impairment	6,097	2,379	1,435	7,696	17,607

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

Total ending allowance balance	\$ 7,554	\$ 2,379	\$ 1,435	\$ 7,696	\$ 19,064
Loans:					
Individually evaluated for impairment	\$ 8,123	\$	\$	\$	\$ 8,123
Collectively evaluated for impairment	322,953	163,040	124,075	267,832	877,900
Total ending loans balance	\$ 331,076	\$ 163,040	\$ 124,075	\$ 267,832	\$ 886,023

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

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

Note 5 Non-performing Assets and Impaired Loans

The following table presents the nonaccrual, loans past due over 90 days still on accrual, and trouble debt restructured (TDR s) by class of loans:

September 30, 2011 (Unaudited)	Nonaccrual	Loans Past Due Over 90 Days Still Accruing	Non Performing TDR s	Performing TDR s	Total Non-Performing Loans
Commercial					
Owner occupied real estate	\$ 2,734	\$	\$	\$	\$ 2,734
Non owner occupied real estate	7,685		217		7,902
Residential development					
Development & Spec Land Loans	90				90
Commercial and industrial	384		144	841	1,369
Total commercial	10,893		361	841	12,095
Real estate					
Residential mortgage	3,395		1,312	2,059	6,766
Residential construction	142			293	435
Mortgage warehouse					
Total real estate	3,537		1,312	2,352	7,201
Consumer					
Direct Installment	259	1			260
Direct Installment Purchased					
Indirect Installment	1,131	40			1,171
Home Equity	1,979	56		849	2,884
Total Consumer	3,369	97		849	4,315
Total	\$ 17,799	\$ 97	\$ 1,673	\$ 4,042	\$ 23,611

December 31, 2010	Nonaccrual	Loans Past Due Over 90 Days Still Accruing	Non Performing TDR s	Performing TDR s	Total Non-Performing Loans
Commercial					
Owner occupied real estate	\$ 1,358	\$	\$	\$	\$ 1,358
Non owner occupied real estate	5,439		421		5,860
Residential development	16				16
Development & Spec Land Loans	250				250
Commercial and industrial	445		153		598
Total commercial	7,508		574		8,082

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

Real estate					
Residential mortgage	5,278	222	241	3,380	9,121
Residential construction	205				205
Mortgage warehouse					
Total real estate	5,483	222	241	3,380	9,326
Consumer					
Direct Installment	251	23			274
Direct Installment Purchased		5			5
Indirect Installment	1,328	98			1,426
Home Equity	2,103	10	37	165	2,315
Total Consumer	3,682	136	37	165	4,020
Total	\$ 16,673	\$ 358	\$ 852	\$ 3,545	\$ 21,428

Table of Contents

HORIZON BANCORP AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

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

From time to time, the Bank obtains information that may lead management to believe that the collection of payments may be doubtful on a particular loan. In recognition of this, it is management's policy to convert the loan from an earning asset to a non-accruing loan. The entire balance of a loan is considered delinquent if the minimum payment contractually required to be made is not received by the specified due date. Further, it is management's policy to place a loan on a non-accrual status when delinquent in excess of 90 days or have had the accrual of interest discontinued by management. The officer responsible for the loan, the Chief Operating Officer and the senior collection officer must review all loans placed on non-accrual status. Subsequent payments on non-accrual loans are recorded as a reduction of principal, and interest income is recorded only after principal recovery is reasonably assured. Nonaccrual loans are returned to accrual status when, in the opinion of management, the financial position of the borrower indicates there is no longer any reasonable doubt as to the timely collection of interest or principal. The Company requires a period of satisfactory performance of not less than six months before returning a nonaccrual loan to accrual status.

A loan becomes impaired when, based on current information, it is probable that a creditor will be unable to collect all amounts due according to the contractual terms of the loan agreement. When a loan is classified as impaired, the degree of impairment must be recognized by estimating future cash flows from the debtor. The present value of these cash flows is computed at a discount rate based on the interest rate contained in the loan agreement. However, if a particular loan has a determinable market value, the creditor may use that value. Also, if the loan is secured and considered collateral dependent, the creditor may use the fair value of the collateral. Interest income on loans individually classified as impaired is recognized on a cash basis after all past due and current principal payments have been made.

Smaller-balance, homogeneous loans are evaluated for impairment in total. Such loans include residential first mortgage loans secured by 1-4 family residences, residential construction loans, automobile, home equity, second mortgage loans and mortgage warehouse loans. Commercial loans and mortgage loans secured by other properties are evaluated individually for impairment. When analysis of borrower operating results and financial condition indicate that underlying cash flows of a borrower's business are not adequate to meet its debt service requirements, the loan is evaluated for impairment. Often this is associated with a delay or shortfall in payments of 30 days or more. Loans are generally moved to non-accrual status when 90 days or more past due. These loans are often considered impaired. Impaired loans, or portions thereof, are charged off when deemed uncollectible.

Loans for which it is probable that the Company will not collect all principal and interest due according to contractual terms, including TDRs, are measured for impairment. Allowable methods for determining the amount of impairment include estimating fair value using the fair value of the collateral for collateral-dependent loans.

The Company's TDRs are considered impaired loans and included in the allowance methodology using the guidance for impaired loans. At September 30, 2011 the type of concessions the Company has made on restructured loans has been temporary rate reductions and/or reductions in monthly payments. Any modification to a loan that is a concession and is not in the normal course of lending is considered a restructured loan. A restructured loan is returned to accruing status after six consecutive payments but is still reported as TDR unless the loan bears interest at a market rate. As of September 30, 2011, the Company had \$5.7 million in TDRs and \$4.0 million were performing according to the restructured terms. The financial statement impact of non-performing TDRs was not material for the nine months ending September 30, 2011. There was \$271,000 of specific reserves for commercial TDRs at September 30, 2011 due to the value of the collateral.

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

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

Loans classified as troubled debt restructuring during the three and nine months ended September 30, 2011, segregated by class, are shown in the table below.

(Dollars in thousands)	Three Months Ended September 30, 2011 (Unaudited)		Nine Months Ended September 30, 2011 (Unaudited)	
	Number of Defaults	Unpaid Principal Balance	Number of Defaults	Unpaid Principal Balance
Commercial				
Owner occupied real estate		\$		\$
Non owner occupied real estate				
Residential development				
Development & Spec Land Loans				
Commercial and industrial			1	841
Total commercial			1	841
Real estate				
Residential mortgage			2	174
Residential construction				
Mortgage warehouse				
Total real estate			2	174
Consumer				
Direct Installment				
Direct Installment Purchased				
Indirect Installment				
Home Equity	1	76	8	724
Total Consumer	1	76	8	724
Total	1	\$ 76	11	\$ 1,739

Troubled debt restructured loans which had payment defaults during the three and nine months ended September 30, 2011, segregated by class, are shown in the table below. Default occurs when a loan is 90 days or more past due or transferred to nonaccrual.

(Dollars in thousands)	Three Months Ended September 30, 2011 (Unaudited)		Nine Months Ended September 30, 2011 (Unaudited)	
	Number of Defaults	Unpaid Principal Balance	Number of Defaults	Unpaid Principal Balance
Commercial				
Owner occupied real estate		\$		\$
Non owner occupied real estate				
Residential development				

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

Development & Spec Land Loans					
Commercial and industrial			2		361
Total commercial			2		361
Real estate					
Residential mortgage			2		1,143
Residential construction					
Mortgage warehouse					
Total real estate			2		1,143
Consumer					
Direct Installment					
Direct Installment Purchased					
Indirect Installment					
Home Equity	1	26	2		65
Total Consumer	1	26	2		65
Total	1	\$ 26	6	\$	1,569

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 commercial loans individually evaluated for impairment by class of loans:

September 30, 2011 (Unaudited)	Unpaid Principal Balance	Recorded Investment	Allowance For Loan Loss Allocated	Nine Months Ending Average Balance in Impaired Loans	Interest Income Recognized	Three Months Ending Average Balance in Impaired Loans	Interest Income Recognized
With no recorded allowance Commercial							
Owner occupied real estate	\$ 1,315	\$ 1,314	\$	\$ 856	\$ 32	\$ 1,224	\$ 31
Non owner occupied real estate	2,403	2,625		985	89	1,683	85
Residential development				9			
Development & Spec Land Loans		111		69			
Commercial and industrial	1,154	1,156		1,099	47	1,091	47
Total commercial	4,872	5,206		3,018	168	3,998	163
With an allowance recorded Commercial							
Owner occupied real estate	1,420	1,420	460	1,234		1,449	
Non owner occupied real estate	5,499	5,538	996	4,859		4,943	
Residential development							
Development & Spec Land Loans	90	90	125	179		90	
Commercial and industrial	234	308	225	393		284	
Total commercial	7,243	7,356	1,806	6,665		6,766	
Total	\$ 12,115	\$ 12,562	\$ 1,806	\$ 9,683	\$ 168	\$ 10,764	\$ 163

December 31, 2010	Unpaid Principal Balance	Recorded Investment	Allowance For Loan Loss Allocated	Twelve Months Ending Average Balance in Impaired Loans	Interest Income Recognized
With no recorded allowance Commercial					
Owner occupied real estate	\$ 720	\$ 721	\$	\$ 2,434	\$ 19
Non owner occupied real estate	928	929		1,195	36
Residential development					
Development & Spec Land Loans				770	
Commercial and industrial	118	118		785	
Total commercial	1,766	1,768		5,184	55
With an allowance recorded Commercial					
Owner occupied real estate	639	640	385	68	15
Non owner occupied real estate	4,932	4,970	665	2,677	115
Residential development	16	16	16	7	2

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

Development & Spec Land Loans	250	250	126	250	
Commercial and industrial	479	479	265	316	13
Total commercial	6,316	6,355	1,457	3,318	145
Total	\$ 8,082	\$ 8,123	\$ 1,457	\$ 8,502	\$ 200

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 payment status by class of loans:

September 30, 2011 (Unaudited)	30 - 59 Days Past Due	60 - 89 Days Past Due	Greater than 90 Days Past Due	Total Past Due	Loans Not Past Due	Total
Commercial						
Owner occupied real estate	\$ 59	\$ 144	\$	\$ 203	\$ 128,493	\$ 128,696
Non owner occupied real estate					141,643	141,643
Residential development					2,598	2,598
Development & Spec Land Loans					7,548	7,548
Commercial and industrial	238			238	64,527	64,765
Total commercial	297	144		441	344,809	345,250
Real estate						
Residential mortgage	1,275			1,275	156,595	157,870
Residential construction	293			293	7,202	7,495
Mortgage warehouse					151,111	151,111
Total real estate	1,568			1,568	314,908	316,476
Consumer						
Direct Installment	128	35	1	164	23,830	23,994
Direct Installment Purchased	20	18		38	1,062	1,100
Indirect Installment	1,357	198	40	1,595	126,070	127,665
Home Equity	424	52	56	532	111,740	112,272
Total consumer	1,929	303	97	2,329	262,702	265,031
Total	\$ 3,794	\$ 447	\$ 97	\$ 4,338	\$ 922,419	\$ 926,757

December 31, 2010	30 - 59 Days Past Due	60 - 89 Days Past Due	Greater than 90 Days Past Due	Total Past Due	Loans Not Past Due	Total
Commercial						
Owner occupied real estate	\$ 229	\$	\$	\$ 229	\$ 125,654	\$ 125,883
Non owner occupied real estate	461			461	136,525	136,986
Residential development					2,257	2,257
Development & Spec Land Loans					6,439	6,439
Commercial and industrial	74			74	58,262	58,336
Total commercial	764			764	329,137	329,901
Real estate						
Residential mortgage	317	91	222	630	154,261	154,891
Residential construction	293			293	7,174	7,467
Mortgage warehouse					123,743	123,743

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

Total real estate	610	91	222	923	285,178	286,101
Consumer						
Direct Installment	294	156	23	473	23,054	23,527
Direct Installment Purchased	51	31	5	87	1,782	1,869
Indirect Installment	2,360	433	98	2,891	125,231	128,122
Home Equity	899	218	10	1,127	113,075	114,202
Total consumer	3,604	838	136	4,578	263,142	267,720
Total	\$ 4,978	\$ 929	\$ 358	\$ 6,265	\$ 877,457	\$ 883,722

The entire balance of a loan is considered delinquent if the minimum payment contractually required to be made is not received by the specified due date.

Horizon Bank's processes for determining credit quality differ slightly depending on whether a new loan or a renewed loan is being underwritten, or whether an existing loan is re-evaluated for credit quality. The latter usually occurs upon receipt of current financial information or other pertinent data that would trigger a change in the loan grade.

Table of Contents

HORIZON BANCORP AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

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

For new and renewed commercial loans, the Bank's Credit Department, which acts independently of the loan officer, assigns the credit quality grade to the loan. Loan grades for loans with an aggregate credit exposure of \$500,000 or greater are validated by the Loan Committee, which is chaired by the Chief Operating Officer (COO).

Commercial loan officers are responsible for reviewing their loan portfolios and report any adverse material change to the COO or Loan Committee. When circumstances warrant a change in the credit quality grade, loan officers are required to notify the COO and the Credit Department of the change in the loan grade. Downgrades are accepted immediately by the COO however, lenders must present their factual information to either the Loan Committee or the COO when recommending an upgrade. One of the requirements for a loan officer to meet the annual bonus criteria is that the loan officer did not have any of his/her loans downgraded by either Internal Loan Review or Bank Regulators to a classified grade; that is, substandard, doubtful or loss.

The COO meets weekly with loan officers to discuss the status of past-due loans and classified loans. These meetings are also designed to give the loan officers an opportunity to identify an existing loan that should be downgraded to a classified grade.

Monthly, Senior Management attends the Watch Committee, which reviews all of the past due, classified, and impaired loans and the relative trends of these assets. This committee also reviews the actions taken by management regarding foreclosure mitigation, loan extensions, troubled debt restructures, and collateral repossessions. The information reviewed in this meeting acts as a precursor for developing Management's analysis of the adequacy of the Allowance for Loan and Lease Losses.

For real estate and consumer loans, Horizon uses a grading system based on delinquency. Loans that are 90 days or more past due, on non-accrual, or a troubled debt restructure are graded Substandard. After being 90 days delinquent a loan is charged off unless it is well secured and in the process of collection. If the latter case exists, the loan is placed on non-accrual. Occasionally a mortgage loan may be graded as Special Mention. When this situation arises, it is because the characteristics of the loan and the borrower fit the definition of a Risk Grade 5 described below, which is normally used for grading commercial loans. Loans not graded Substandard are considered Pass.

Horizon Bank employs an eight-grade rating system to determine the credit quality of commercial loans. The first four grades represent acceptable quality, and the last four grades mirror the criticized and classified grades used by the bank regulatory agencies (special mention, substandard, doubtful, and loss). The loan grade definitions are detailed below.

Risk Grade 1: Excellent (Pass)

Loans secured by liquid collateral, such as certificates of deposit, reputable bank letters of credit, or other cash equivalents; loans that are guaranteed or otherwise backed by the full faith and credit of the United States government or an agency thereof, such as the Small Business Administration; or loans to any publicly held company with a current long-term debt rating of A or better.

Risk Grade 2: Good (Pass)

Loans to businesses that have strong financial statements containing an unqualified opinion from a CPA firm and at least three consecutive years of profits; loans supported by unaudited financial statements containing strong balance sheets, five consecutive years of profits, a five-year satisfactory relationship with the Bank, and key balance sheet and income statement trends that are either stable or positive; loans secured by publicly traded marketable securities where there is no impediment to liquidation; loans to individuals backed by liquid personal assets and unblemished credit history; or loans to publicly held companies with current long-term debt ratings of Baa or better.

Risk Grade 3: Satisfactory (Pass)

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

Loans supported by financial statements (audited or unaudited) that indicate average or slightly below average risk and having some deficiency or vulnerability to changing economic conditions; loans with some weakness but offsetting features of other support are readily available; loans that are meeting the terms of repayment, but which may be susceptible to deterioration if adverse factors are encountered.

Table of Contents

HORIZON BANCORP AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

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

Loans may be graded Satisfactory when there is no recent information on which to base a current risk evaluation and the following conditions apply:

At inception, the loan was properly underwritten, did not possess an unwarranted level of credit risk, and the loan met the above criteria for a risk grade of Excellent, Good, or Satisfactory;

At inception, the loan was secured with collateral possessing a loan value adequate to protect the Bank from loss.

The loan has exhibited two or more years of satisfactory repayment with a reasonable reduction of the principal balance.

During the period that the loan has been outstanding, there has been no evidence of any credit weakness. Some examples of weakness include slow payment, lack of cooperation by the borrower, breach of loan covenants, or the borrower is in an industry known to be experiencing problems. If any of these credit weaknesses is observed, a lower risk grade may be warranted.

Risk Grade 4: Satisfactory/Monitored (Pass)

Loans in this category are considered to be of acceptable credit quality, but contain greater credit risk than Satisfactory loans due to weak balance sheets, marginal earnings or cash flow, lack of financial information, weakening markets, insufficient or questionable collateral coverage or other uncertainties. These loans warrant a higher than average level of monitoring to ensure that weaknesses do not advance. The level of risk in a Satisfactory/Monitored loan is within acceptable underwriting guidelines so long as the loan is given the proper level of management supervision. Loans that normally fall into this grade include construction of commercial real estate buildings, land development and subdivisions, and rental properties that have not attained stabilization.

Risk Grade 5: Special Mention

Loans which possess some credit deficiency or potential weakness which deserves close attention. Such loans pose an unwarranted financial risk that, if not corrected, could weaken the loan by adversely impacting the future repayment ability of the borrower. The key distinctions of a Special Mention classification are that (1) it is indicative of an unwarranted level of risk and (2) weaknesses are considered potential, not defined, impairments to the primary source of repayment. These loans may be to borrowers with adverse trends in financial performance, collateral value and/or marketability, or balance sheet strength.

Risk Grade 6: Substandard

One or more of the following characteristics may be exhibited in loans classified Substandard:

Loans which possess a defined credit weakness. The likelihood that a loan will be paid from the primary source of repayment is uncertain. Financial deterioration is under way and very close attention is warranted to ensure that the loan is collected without loss.

Loans are inadequately protected by the current net worth and paying capacity of the obligor.

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

The primary source of repayment is gone, and the Bank is forced to rely on a secondary source of repayment, such as collateral liquidation or guarantees.

Loans have a distinct possibility that the Bank will sustain some loss if deficiencies are not corrected.

Unusual courses of action are needed to maintain a high probability of repayment.

The borrower is not generating enough cash flow to repay loan principal; however, it continues to make interest payments.

Table of Contents

HORIZON BANCORP AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

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

The lender is forced into a subordinated or unsecured position due to flaws in documentation.

Loans have been restructured so that payment schedules, terms, and collateral represent concessions to the borrower when compared to the normal loan terms.

The lender is seriously contemplating foreclosure or legal action due to the apparent deterioration in the loan.

There is a significant deterioration in market conditions to which the borrower is highly vulnerable.

Risk Grade 7: Doubtful

One or more of the following characteristics may be present in loans classified Doubtful:

Loans have all of the weaknesses of those classified as Substandard. However, based on existing conditions, these weaknesses make full collection of principal highly improbable.

The primary source of repayment is gone, and there is considerable doubt as to the quality of the secondary source of repayment.

The possibility of loss is high but because of certain important pending factors which may strengthen the loan, loss classification is deferred until the exact status of repayment is known.

Risk Grade 8: Loss

Loans are considered uncollectible and of such little value that continuing to carry them as assets is not feasible. Loans will be classified Loss when it is neither practical nor desirable to defer writing off or reserving all or a portion of a basically worthless asset, even though partial recovery may be possible at some time in the future.

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

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

September 30, 2011 (Unaudited)	Pass	Special Mention	Substandard	Doubtful	Total
Commercial					
Owner occupied real estate	\$ 104,849	\$ 4,438	\$ 19,409	\$	\$ 128,696
Non owner occupied real estate	114,652	11,882	15,109		141,643
Residential development	597	531	1,470		2,598
Development & Spec Land Loans	2,351	863	4,334		7,548
Commercial and industrial	54,839	2,771	7,155		64,765
Total commercial	277,288	20,485	47,477		345,250
Real estate					
Residential mortgage	151,104		6,766		157,870
Residential construction	7,060		435		7,495
Mortgage warehouse	151,111				151,111
Total real estate	309,275		7,201		316,476
Consumer					
Direct Installment	23,734		260		23,994
Direct Installment Purchased	1,100				1,100
Indirect Installment	126,494		1,171		127,665
Home Equity	109,388		2,884		112,272
Total Consumer	260,716		4,315		265,031
Total	\$ 847,279	\$ 20,485	\$ 58,993	\$	\$ 926,757
December 31, 2010	Pass	Special Mention	Substandard	Doubtful	Total
Commercial					
Owner occupied real estate	\$ 94,722	\$ 13,656	\$ 17,506	\$	\$ 125,883
Non owner occupied real estate	119,041	6,107	11,838		136,986
Residential development	834	537	886		2,257
Development & Spec Land Loans	4,378	746	1,315		6,439
Commercial and industrial	45,831	6,856	5,649		58,336
Total commercial	264,805	27,902	37,195		329,901
Real estate					
Residential mortgage	145,770		9,121		154,891
Residential construction	7,262		205		7,467
Mortgage warehouse	123,743				123,743
Total real estate	276,775		9,326		286,101
Consumer					
Direct Installment	23,253		274		23,527
Direct Installment Purchased	1,864		5		1,869
Indirect Installment	126,696		1,426		128,122
Home Equity	111,888		2,314		114,202

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

Total Consumer	263,701		4,019		267,720
Total	\$ 805,281	\$ 27,902	\$ 50,539	\$	\$ 883,722

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 5.63% on a notional amount of \$30.6 million at September 30, 2011. Under these 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, 2011, 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 activities. 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, 2011, the Company's fair value hedges were effective and are not expected to have a significant impact on 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 \$47.6 million at September 30, 2011.

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, 2011, the Company's fair value of these derivatives was recorded and over the next 12 months is not expected to have a significant impact on 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:

	Asset Derivative September 30, 2011		Liability Derivatives September 30, 2011	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Derivatives designated as hedging instruments (Unaudited)				
Interest rate contracts	Loans	\$ 974	Other liabilities	\$ 2,374
Interest rate contracts	Other Assets	1,401	Other liabilities	4,866
Total derivatives designated as hedging instruments		2,375		7,240
Derivatives not designated as hedging instruments				
Mortgage loan contracts	Other assets	749	Other liabilities	
Total derivatives not designated as hedging instruments		749		
Total derivatives		\$ 3,124		\$ 7,240

	Asset Derivative December 31, 2010		Liability Derivatives December 31, 2010	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Derivatives designated as hedging instruments				
Interest rate contracts	Loans	\$ 1,388	Other liabilities	\$ 2,039
Interest rate contracts	Other Assets	651	Other liabilities	1,376
Total derivatives designated as hedging instruments		2,039		3,415
Derivatives not designated as hedging instruments				
Mortgage loan contracts	Other assets	407	Other liabilities	
Total derivatives not designated as hedging instruments		407		
Total derivatives		\$ 2,446		\$ 3,415

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

Amount of Loss Recognized in Other Comprehensive Income on Derivative	Amount of Loss Recognized in Other Comprehensive Income on
---	--

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

Derivative in cash flow hedging relationship	(Effective Portion) Three Months Ended September 30		Derivative (Effective Portion) Nine Months Ended September 30	
	2011 (Unaudited)	2010 (Unaudited)	2011 (Unaudited)	2010 (Unaudited)
Interest rate contracts	\$ (1,951)	\$ (900)	\$ (2,268)	\$ (1,557)

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.

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

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

Derivative in fair value hedging relationship	Location of gain (loss) recognized on derivative	Amount of Gain (Loss) Recognized on Derivative		Amount of Gain (Loss) Recognized on Derivative	
		Three Months Ended September 30		Nine Months Ended September 30	
		2011 (Unaudited)	2010 (Unaudited)	2011 (Unaudited)	2010 (Unaudited)
Interest rate contracts	Interest income - loans	\$ 394	\$ 560	\$ 335	\$ 1,773
Interest rate contracts	Interest income - loans	(394)	(560)	(335)	(1,773)
Total		\$	\$	\$	\$

Derivative not designated as hedging relationship	Location of gain (loss) recognized on derivative	Amount of Gain (Loss) Recognized on Derivative		Amount of Gain (Loss) Recognized on Derivative	
		Three Months Ended September 30		Nine Months Ended September 30	
		2011 (Unaudited)	2010 (Unaudited)	2011 (Unaudited)	2010 (Unaudited)
Mortgage contracts	Other income - gain on sale of loans	\$ 359	\$ (40)	\$ 1,157	\$ 560
Total		\$ 359	\$ (40)	\$ 1,157	\$ 560

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 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.

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

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.

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

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

Hedged loans

Certain fixed rate loans have been converted to variable rate loans by entering into interest rate swap agreements. The fair value of those fixed rate loans is based on discounting the estimated cash flows using interest rates determined by the 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 of the Company's interest rate swap agreements 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.

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)
September 30, 2011 (Unaudited)				
Available-for-sale securities				
U.S. Treasury and federal agencies	\$ 11,176	\$	\$ 11,176	\$
State and municipal	143,750		143,750	
Federal agency collateralized mortgage obligations	90,095		90,095	
Federal agency mortgage-backed pools	181,723		181,723	
Private labeled mortgage-backed pools	3,933		3,933	
Corporate notes	25		25	
Total available-for-sale securities	430,702		430,702	
Hedged loans	53,555			53,555
Forward sale commitments	749			749
Interest rate swap agreements	(7,241)			(7,241)
Commitments to originate loans				
December 31, 2010				
Available-for-sale securities				
U.S. Treasury and federal agencies	\$ 25,251	\$	\$ 25,251	\$
State and municipal	131,489		131,489	
Federal agency collateralized mortgage obligations	101,837		101,837	
Federal agency mortgage-backed pools	117,895		117,895	
Private labeled mortgage-backed pools	5,323		5,323	
Corporate notes	549	456	20	
Total available-for-sale securities	382,344	456	381,815	

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

Hedged loans	50,088	50,088
Forward sale commitments	407	407
Interest rate swap agreements	(3,415)	(3,415)
Commitments to originate loans		

27

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):

	Hedged Loans	Forward Sale Commitments	Interest Rate Swaps	Commitments to Originate Loans
Beginning balance December 31, 2010	\$ 50,088	\$ 407	\$ (3,415)	\$
Total realized and unrealized gains and losses				
Included in net income	(410)	(126)	410	(56)
Included in other comprehensive income, gross			451	
Purchases, issuances, and settlements	(352)			
Principal payments	(915)			
Ending balance March 31, 2011	48,411	281	(2,554)	(56)
Total realized and unrealized gains and losses				
Included in net income	351	174	(351)	(8)
Included in other comprehensive income, gross			(941)	
Purchases, issuances, and settlements	1,200			
Principal payments	(344)			
Ending balance June 30, 2011	49,618	455	(3,846)	(64)
Total realized and unrealized gains and losses				
Included in net income	393	294	(393)	64
Included in other comprehensive income, gross			(3,001)	
Purchases, issuances, and settlements	1,797			
Principal payments	(628)			
Ending balance September 30, 2011	\$ 51,180	\$ 749	\$ (7,240)	\$

	Hedged Loans	Forward Sale Commitments	Interest Rate Swaps	Commitments to Originate Loans
Beginning balance December 31, 2009	\$ 31,153	\$ 265	\$ (715)	\$ (135)
Total realized and unrealized gains and losses				
Included in net income	403	141	(403)	97
Included in other comprehensive income, gross			(420)	
Purchases, issuances, and settlements	7,991			
Principal payments	(216)			
Ending balance March 31, 2010	39,331	406	(1,538)	(38)
Total realized and unrealized gains and losses				
Included in net income	810	324	(810)	38
Included in other comprehensive income, gross			(2,186)	
Purchases, issuances, and settlements	4,041			
Principal payments	(284)			

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

Ending balance June 30, 2010	43,898	730	(4,534)	
Total realized and unrealized gains and losses				
Included in net income	560	(40)	(560)	
Included in other comprehensive income, gross			(1,385)	
Purchases, issuances, and settlements	7,135			
Principal payments	(235)			
Ending balance September 30, 2010	\$ 51,358	\$ 690	\$ (6,479)	\$

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

	Three Months Ended September 30		Nine Months Ended September 30	
	2011	2010	2011	2010
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
Non Interest Income				
Total gains and losses from:				
Hedged loans	\$ 394	\$ 560	\$ 335	\$ 1,773
Fair value interest rate swap agreements	(394)	(560)	(335)	(1,773)
Derivative loan commitments	359	(40)	1,157	560
	\$ 359	\$ (40)	\$ 1,157	\$ 560

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

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

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

	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
September 30, 2011 (Unaudited)				
Impaired loans	\$ 12,115	\$	\$	\$ 12,115
December 31, 2010				
Impaired loans	\$ 9,919	\$	\$	\$ 9,919

Impaired (collateral dependent): 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 net of estimated costs to sell.

Note 8 Fair Value of Financial Instruments

The estimated fair value amounts of the Company's financial instruments 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 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 Horizon's significant financial instruments at September 30, 2011 and December 31, 2010. 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 Due from Banks The 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)

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.

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.

Interest Receivable/Payable The carrying amounts approximate fair value.

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.

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

	September 30, 2011 (Unaudited)		December 31, 2010	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Assets				
Cash and due from banks	\$ 18,462	\$ 18,462	\$ 15,683	\$ 15,683
Investment securities available for sale	430,702	430,702	382,344	382,344
Investment securities held to maturity	10,632	10,632	9,595	9,595
Loans held for sale	12,300	12,300	18,833	18,833
Loans, net	906,730	904,362	863,813	867,054
Stock in FHLB and FRB	12,390	12,390	13,664	13,664
Interest receivable	6,651	6,651	6,519	6,519

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

Liabilities				
Non-interest bearing deposits	\$ 121,483	\$ 121,483	\$ 107,606	\$ 107,606
Interest-bearing deposits	868,266	869,990	877,892	854,617
Borrowings	336,095	364,090	260,741	289,381
Subordinated debentures	30,653	30,473	30,584	30,734
Interest payable	582	582	781	781

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

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

Note 9 Other Comprehensive Income (Loss)

	Three Months Ended		Nine Months Ended	
	September 30 2011 (Unaudited)	September 30 2010 (Unaudited)	September 30 2011 (Unaudited)	September 30 2010 (Unaudited)
Unrealized gains on securities:				
Unrealized holding gains arising during the period	\$ 5,303	\$ 3,494	\$ 13,863	\$ 4,875
Less: reclassification adjustment for gains realized in net income	1,115	336	1,754	467
	4,188	3,158	12,109	4,408
Unrealized gain (loss) on derivative instruments	(3,002)	(1,385)	(3,489)	(3,992)
Net unrealized gains	1,186	1,773	8,620	416
Tax benefit	(415)	(621)	(3,017)	(146)
Other comprehensive income	\$ 771	\$ 1,152	\$ 5,603	\$ 270

	September 30 2011 (Unaudited)	December 31 2010
Unrealized gain on securities available for sale	\$ 17,098	\$ 4,989
Unrealized gain (loss) on derivative instruments	(4,866)	(1,377)
Tax effect	(4,281)	(1,264)
Total accumulated other comprehensive income	\$ 7,951	\$ 2,348

Note 10 Future accounting matters

Goodwill: In September 2011, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2011-08 *Intangibles - Goodwill and Other (Topic 350) - Testing Goodwill for Impairment*. ASU 2011-08 allows an entity the option to make a qualitative evaluation about the likelihood of goodwill impairment to determine whether it should calculate the fair value of the reporting unit. ASU 2011-08 is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Early adoption is permitted. We are assessing the impact of ASU 2011-08 on our goodwill impairment test but do not expect an impact on our financial condition or results of operations.

Comprehensive Income: In June 2011, the FASB issued ASU No. 2011-05 *Comprehensive Income (Topic 220) - Presentation of Comprehensive Income*. ASU 2011-05 requires that all nonowner changes in stockholders' equity be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In both choices, an entity is required to present each component of net income along with total net income, each component of other comprehensive income along with a total for other comprehensive income, and a total amount for comprehensive income. ASU 2011-05 is effective retrospectively for fiscal years, and interim periods within those years, beginning after December 15, 2011. We are assessing the impact of ASU 2011-05 on our comprehensive income presentation.

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

Fair Value Measurements: In May 2011, the FASB issued ASU No. 2011-04 *Fair Value Measurement (Topic 820) - Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs*. ASU 2011-04 changes the wording used to describe many of the requirements in U.S. GAAP for measuring fair value and for disclosing information about fair value measurements. Consequently, the amendments in this update result in common fair value measurement and disclosure requirements in U.S. GAAP and IFRSs (International Financial Reporting Standards). ASU 2011-04 is effective prospectively during interim and annual periods beginning on or after December 15, 2011. Early application by public entities is not permitted. We are assessing the impact of ASU 2011-04 on our fair value disclosures.

Table of Contents

HORIZON BANCORP AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

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

Transfers and Servicing: In April 2011, the FASB issued ASU No. 2011-03 *Transfers and Servicing (Topic 860) - Reconsideration of Effective Control for Repurchase Agreement*. ASU 2011-03 removes from the assessment of effective control the criterion relating to the transferor's ability to repurchase or redeem financial assets on substantially the agreed terms, even in the event of default by the transferee. ASU 2011-03 is effective for the first interim or annual period beginning on or after December 15, 2011. The guidance should be applied prospectively to transactions or modifications of existing transactions that occur on or after the effective date. Early adoption is not permitted. We are assessing the impact of ASU 2011-03 on our financial condition, results of operations, and disclosures.

Receivables: In April 2011, the FASB issued ASU No. 2011-02 *Receivables (Topic 310) - A Creditor's Determination of Whether a Restructuring is a Troubled Debt Restructuring*. ASU 2011-02 clarifies whether loan modifications constitute troubled debt restructurings. In evaluating whether a restructuring constitutes a troubled debt restructuring, a creditor must separately conclude that both of the following exist: (a) the restructuring constitutes a concession; and (b) the debtor is experiencing financial difficulties. ASU 2011-02 was effective for the first interim and annual period beginning on or after June 15, 2011, and should be applied retrospectively to the beginning of the annual period of adoption. The impact of ASU 2011-02 on our disclosures is reflected in Note 5 Non-performing Assets and Impaired Loans.

Note 11 SBLF Offering and TARP Repurchase

On August 25, 2011, we completed the sale of 12,500 shares of Senior Non-Cumulative Perpetual Preferred Stock, Series B (Series B Preferred Stock), for aggregate consideration of \$12.5 million, to the U.S. Treasury pursuant to the Small Business Lending Fund program. Concurrently with this transaction, we redeemed all 18,750 shares of our Fixed Rate Cumulative Perpetual Preferred Stock, Series A (Series A Preferred Stock), that remained outstanding under the TARP Capital Purchase Program. The redemption of the Series A Preferred stock was funded by the \$12.5 million in proceeds from the sale of the Series B Preferred Stock together with other available funds.

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, 2011

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 the Company) and Horizon Bank, N.A. (the 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. Statements in this report should be considered in conjunction with the other information available about Horizon, including the information in the other filings we make with the Securities and Exchange Commission. The forward-looking statements are based on management's expectations and are subject to a number of risks and uncertainties. We have tried, wherever possible, to identify such statements by using words such as anticipate, expect, estimate, project, intend, plan, believe, could, will and similar expressions in connection with our discussion of future operating or financial performance. Although management believes that the expectations reflected in such forward-looking statements are reasonable, actual results may differ materially from those expressed or implied in such statements.

Actual results may differ materially, and adversely or positively, from the expectations of the Company that are expressed or implied by any forward-looking statement. Risks, uncertainties, and factors that could cause the Company's actual results to vary materially from those expressed or implied by any forward-looking statement include but not limited to:

the use of proceeds of future offerings of securities;

the unknown future direction of interest rates and the timing and magnitude of any changes in interest rates;

changes in competitive conditions;

the introduction, withdrawal, success and timing of asset/liability management strategies or of mergers and acquisitions and other business initiatives and strategies;

changes in customer borrowing, repayment, investment and deposit practices;

changes in fiscal, monetary and tax policies;

changes in financial and capital markets;

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

deterioration in general economic conditions, either nationally or locally, resulting in, among other things, credit quality deterioration;

capital management activities, including possible future sales of new securities, or possible repurchases or redemptions by the Company of outstanding debt or equity securities;

risks of expansion through acquisitions and mergers, such as unexpected credit quality problems of the acquired loans or other assets, unexpected attrition of the customer base of the acquired institution or branches, and difficulties in integration of the acquired operations;

factors that may cause the Company to incur impairment charges on its investment securities;

the impact, extent and timing of technological changes

electronic, cyber and physical security breaches;

claims and litigation liabilities, including related costs, expenses, settlements and judgments, or the outcome of matters before regulatory agencies, whether pending or commencing in the future;

actions of the Federal Reserve Board;

changes in accounting principles and interpretations;

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, 2011

potential increases of federal deposit insurance premium expense, and possible future special assessments of FDIC premiums, either industry wide or specific to the Company's banking subsidiary;

actions of the regulatory authorities under the Dodd-Frank Wall Street Reform and Consumer Protection Act and the Federal Deposit Insurance Act and other possible legislative and regulatory actions and reforms;

the continued availability of earnings and excess capital sufficient for the lawful and prudent declaration and payment of cash dividends; and

other factors and risks described under the caption "Risk Factors" in this report and in any of our subsequent reports that we have made or make with the Securities and Exchange Commission ("SEC").

Because such forward-looking statements are subject to risks and uncertainties, actual results may differ materially from those expressed or implied by such statements. The foregoing list of important factors is not exclusive and you are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of this document or, in the case of documents incorporated by reference, the dates of those documents. We do not undertake to update any forward-looking statements, whether written or oral, that may be made from time to time by or on behalf of us. For a detailed discussion of the risks and uncertainties that may cause our actual results or performance to differ materially from the results or performance expressed or implied by forward-looking statements, see "Risk Factors" in this report and in the subsequent reports we file with the SEC.

Overview

Horizon 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 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 economic and banking environment. Within the Company's primary market areas of Northwest Indiana and Southwest Michigan, unemployment rates increased during 2009 and have remained at high levels during 2010 and the first nine months of 2011. This rise in unemployment has been driven by factors including slowdowns in the steel and recreational vehicle industries as well as a continued lower activity in the housing industry. The Company's higher than historical levels of non-performing loans at September 30, 2011 and over the past two years can be attributed to the continued slow economy and continued high local unemployment causing lower business revenues and increased bankruptcies. Despite these economic factors, Horizon continued to post record positive results through the first nine months of 2011.

Following are some highlights of Horizons financial performance through the third quarter of 2011:

Third quarter 2011 net income was \$3.4 million or \$.80 diluted earnings per share, a 4.2% increase in net income from the same period in 2010 and the highest quarterly net income in the Company's history.

For the first nine months of 2011, net income was \$9.3 million or \$2.37 diluted earnings per share, a 22.3% increase in net income from the same period in 2010 and the highest year-to-date nine-month net income in the Company's history.

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, 2011

Total loans increased \$86.8 million during the quarter to \$925.8 million at September 30, 2011.

Total assets grew to a record \$1.49 billion at September 30, 2011 compared to \$1.41 billion at June 30, 2011.

Net interest income, after provisions for loan losses, for the nine months of 2011 was \$30.1 million compared with \$25.7 million for the same period in the prior year.

The provision for loan losses decreased to \$4.4 million for the first nine months of 2011 compared to \$8.9 million for the same period in 2010.

In August, the Company redeemed all of the US Treasury's preferred stock investment under the TARP Capital Purchase Program using \$6.25 million in cash and a \$12.5 million investment by the US Treasury under the Small Business Lending Fund.

The Company increased its quarterly dividend to \$0.18 per share, its 103rd consecutive quarterly cash dividend to Horizon's shareholders.

Horizon's tangible book value per share rose to \$29.68 compared with \$26.50 at the close of the third quarter of 2010.

Horizon's capital ratios, including Tier 1 Capital to total risk weighted assets of 12.37%, continue to be well 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 2010 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.

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, 2011, Horizon had core deposit intangibles of \$2.4 million subject to amortization and \$5.9 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

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, 2011

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, 2011 was \$26.50 per share compared to a book value of \$32.20 per common share. Horizon reported record earnings for the eleventh consecutive year in 2010 and the first nine months of 2011 were the highest first nine months of net income in the Company's history, therefore, the Company believes the below book market price relates to an overall decline in the financial industry sector and is not specific to Horizon.

The financial markets are currently reflecting significantly lower valuations for the stocks of financial institutions, when compared to historic valuation metrics, largely driven by the constriction in available credit and losses suffered related to residential mortgage markets. The Company's stock activity, as well as the price, has been affected by the economic conditions affecting the banking industry. Management believes this downturn has impacted the Company's stock and has concluded that the recent stock price is not indicative or reflective of fair value (per ASC Topic 820 Fair Value).

Horizon has concluded that, based on its own internal evaluation 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 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 interest rates, loan prepayment speeds, and other factors, could impact Horizon's financial condition and results of operations either positively or negatively.

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. In addition, on a quarterly basis Horizon engages a third party to independently test the value of its servicing asset.

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, 2011

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 extent, to which related assets may be impaired, management makes assumptions and estimates related to discount rates, asset returns, prepayment speeds 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.

Financial Condition

On September 30, 2011, Horizon's total assets were a record high at \$1.5 billion, an increase of \$89.9 million from December 31, 2010. Total assets increased primarily due to the increase in investment securities as excess liquidity was invested and the increase in net loans from higher balances in commercial, real estate, and mortgage warehouse loans compared to December 31, 2010.

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, 2011**

Investment securities were comprised of the following as of:

	September 30, 2011 (Unaudited)		December 31, 2010	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Available for sale				
U.S. Treasury and federal agencies	\$ 10,818	\$ 11,176	\$ 24,727	\$ 25,251
State and municipal	136,147	143,750	132,380	131,489
Federal agency collateralized mortgage obligations	87,688	90,095	100,106	101,837
Federal agency mortgage-backed pools	175,090	181,723	114,390	117,895
Private labeled mortgage-backed pools	3,817	3,933	5,197	5,323
Corporate notes	42	25	555	549
Total available for sale investment securities	\$ 413,602	\$ 430,702	\$ 377,355	\$ 382,344
Held to maturity, State and Municipal	\$ 10,632	\$ 10,632	\$ 9,595	\$ 9,595

Investment securities increased by approximately \$48.4 million compared to the end of 2010. This growth was the result of the Company deploying excess cash that was held during the first nine months in cash and due from banks into investment securities.

Net loans increased \$42.9 million since December 31, 2010. This increase was the result of an increase in commercial, real estate, and mortgage warehouse loans of \$15.3 million, \$3.0 million, and \$27.4 million, respectively. These increases were offset by a decrease in consumer loans of \$2.8 million. The increase in commercial loans is the direct result of increased calling efforts and market expansion allowing opportunities to increase Horizon's market share within the Company's footprint. Real estate and mortgage warehouse loans increased as a result of market expansion and refinancing activity. Horizon's consumer loans decreased during the first nine months of 2011 as new loan production has not completely replaced all of the loan run-off from scheduled amortization and pay-offs.

Total deposits increased \$4.3 million during the first nine months of 2011 primarily due to consumer deposit growth.

The Company's borrowings increased \$75.4 million since December 31, 2010. At September 30, 2011 the Company had \$128.1 million in short-term funds borrowed compared to \$31.5 million at December 31, 2010. The Company uses short-term borrowings to fund the increase in mortgage warehouse lending when it is determined that the loan demand may fluctuate as a result of refinancing activity which was the primary reason for the increase in borrowings. In addition, the current Company's balance sheet strategy is to utilize a reasonable level of short-term borrowing during extended low rate environments in addition to what is needed for the fluctuations in mortgage warehouse lending.

Stockholders' equity totaled \$118.7 million at September 30, 2011 compared to \$112.3 million at December 31, 2010. The increase in stockholders' equity during the period was the result of generating net income and an increase in accumulated other comprehensive income, net of dividends declared and the redemption of \$6.25 million of preferred stock. At September 30, 2011, the ratio of average stockholders' equity to average assets was 8.60% compared to 8.22% for December 31, 2010. Book value per common share at September 30, 2011 increased to \$32.20 compared to \$28.68 at December 31, 2010.

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, 2011

Results of Operations

Overview

Consolidated net income for the three-month period ended September 30, 2011 was \$3.4 million, an increase of 4.2% from the \$3.3 million for the same period in 2010. Earnings per common share for the three months ended September 30, 2011 decreased to \$0.82 basic and \$0.80 diluted, compared to \$0.89 basic and \$0.88 diluted for the same three-month period in 2010. Earnings per share decreased \$.13 per share in the third quarter of 2011 compared to the same period in 2010 from redeeming the US Treasury's preferred stock investment from the TARP Capital Purchase Program (CPP) during the third quarter which required that the discount on the preferred stock be completely recognized, resulting in a reduction in net income available to common shareholders of \$449,000, or \$0.13 per diluted share. This was a one time event and had no net impact on the equity of the Company.

On August 25, 2011, the Company redeemed all of the U.S. Treasury's preferred stock investment from the CPP using \$6.25 million in cash and a \$12.5 million investment from the U.S. Treasury under the Small Business Lending Fund (SBLF) in a new series of our preferred stock. The total preferred stock dividends and accretion of the discount for the third quarter was \$710,000, representing \$261,000 in preferred stock dividends and \$449,000 in discount accretion.

Consolidated net income for the nine-month period ended September 30, 2011 was \$9.3 million, an increase of 22.3% from the \$7.6 million for the same period in 2010. Earnings per common share for the nine months ended September 30, 2011 increased to \$2.44 basic and \$2.37 diluted, compared to \$1.99 basic and \$1.96 diluted for the same nine-month period in 2010.

Diluted earnings per share were reduced by \$0.21 and \$0.36, respectively, for the three and nine months ending September 30, 2011, compared to \$0.11 and \$0.32, respectively, for the three and nine months ending September 30, 2010. The reduction to diluted earnings per share was greater in 2011 due to the recognition of the remaining discount on the CPP preferred stock in the third quarter of 2011 but offset by a decrease in preferred stock dividends. The reduction in 2011 on the preferred stock dividend was due to the repurchase of \$6.25 million of CPP preferred stock during the fourth quarter of 2010.

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 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 has influenced the yields received on the Company's interest earning assets more significantly than the reduction in the cost of the Company's interest bearing liabilities, resulting in a decrease of the net interest margin. 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 significant 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, 2011 was \$12.0 million, a decrease of \$629,000 over the \$12.6 million earned during the same period in 2010. Yields on the Company's interest-earning assets decreased by 42 basis points to 4.97% from 5.39% for the three months ended September 30, 2011 and 2010, respectively. Interest income decreased \$1.9 million from \$17.9 million for the three months ended

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

September 30, 2010 to \$16.0 million for the same period in 2011. This decrease was primarily due to a decrease in the yield on new and repriced earning assets in addition to a decrease in 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 \$329.8 million of the Company's \$468.1 million of adjustable rate loans.

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, 2011

Rates paid on interest-bearing liabilities decreased by 36 basis points for the three months ended September 30, 2011 compared to the same period in 2010 due to the lower interest rate environment. Interest expense decreased \$1.3 million from \$5.3 million for the three-months ended September 30, 2010 to \$4.0 million for the same period in 2011. This decrease was due to the lower rates being paid on the Company's interest bearing liabilities in addition to a reduction in interest bearing liabilities. Due to a more significant decrease in the yields received on the Company's interest-earning assets compared to the decrease in the rates paid on the Company's interest-bearing liabilities the net interest margin decreased 8 basis points from 3.84% for the three months ended September 30, 2010 to 3.76% for the same period in 2011.

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, 2011**

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

	Three Months Ended			Three Months Ended		
	September 30, 2011			September 30, 2010		
	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate
ASSETS						
Interest-earning assets						
Federal funds sold	\$ 2,265	\$ 1	0.18%	\$ 12,273	\$ 4	0.13%
Interest-earning deposits	14,868	1	0.03%	15,349	4	0.10%
Investment securities - taxable	336,027	2,540	3.00%	298,152	2,423	3.22%
Investment securities - non-taxable (1)	109,875	988	5.41%	102,885	979	5.32%
Loans receivable (2)	855,938	12,481	5.79%	918,930	14,466	6.25%
Total interest-earning assets (1)	1,318,973	16,011	4.97%	1,347,589	17,876	5.39%
Noninterest-earning assets						
Cash and due from banks	17,169			16,518		
Allowance for loan losses	(18,823)			(17,137)		
Other assets	99,560			97,460		
	\$ 1,416,879			\$ 1,444,430		
LIABILITIES AND SHAREHOLDERS' EQUITY						
Interest-bearing liabilities						
Interest-bearing deposits	\$ 871,621	\$ 1,978	0.90%	\$ 913,473	\$ 2,769	1.20%
Borrowings	259,783	1,583	2.42%	258,476	2,026	3.11%
Subordinated debentures	31,446	459	5.79%	34,946	461	5.23%
Total interest-bearing liabilities	1,162,850	4,020	1.37%	1,206,895	5,256	1.73%
Noninterest-bearing liabilities						
Demand deposits	121,034			106,152		
Accrued interest payable and other liabilities	11,158			11,204		
Shareholders' equity	121,837			120,179		
	\$ 1,416,879			\$ 1,444,430		
Net interest income/spread		\$ 11,991	3.60%		\$ 12,620	3.66%
Net interest income as a percent of average interest earning assets (1)			3.76%			3.84%

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

- (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.
- Net interest income during the nine months ended September 30, 2011 was \$34.5 million which was approximately the same when compared to the same period in 2010. Yields on the Company's interest-earning assets decreased by 45 basis points to 4.96% for the nine months ended September 30, 2011 from 5.41% for the same period in 2010. Interest income decreased \$3.6 million from \$50.8 million for the nine months ended September 30, 2010 to \$47.2 million for the same period in 2011. This decrease was due to the reduction in the yield on interest earning assets offset by an increase in interest earning 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, 2011**

Rates paid on interest-bearing liabilities decreased by 42 basis points for the nine months ended September 30, 2011 compared to the same period in 2010 due to the lower interest rate environment. Interest expense decreased \$3.7 million from \$16.3 million for the nine-months ended September 30, 2010 to \$12.6 million for the same period in 2011. This decrease was due to the lower rates being paid on the Company's interest bearing liabilities partially offset with a higher volume of interest bearing liabilities. Due to a more significant decrease in the yields received on the Company's interest-earning assets compared to the decrease in the rates paid on the Company's interest-bearing liabilities the net interest margin decreased 5 basis points from 3.72% for the nine months ended September 30, 2010 to 3.67% for the same period in 2011.

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

	Nine Months Ended			Nine Months Ended		
	September 30, 2011			September 30, 2010		
	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate
ASSETS						
Interest-earning assets						
Federal funds sold	\$ 26,448	\$ 49	0.25%	\$ 30,279	\$ 13	0.06%
Interest-earning deposits	8,837	2	0.03%	9,213	38	0.55%
Investment securities - taxable	329,903	7,777	3.15%	278,790	7,343	3.52%
Investment securities - non-taxable (1)	112,133	3,066	5.22%	108,666	3,138	5.36%
Loans receivable (2)	830,432	36,260	5.85%	860,253	40,283	6.27%
Total interest-earning assets (1)	1,307,753	47,154	4.96%	1,287,201	50,815	5.41%
Noninterest-earning assets						
Cash and due from banks	15,756			15,101		
Allowance for loan losses	(18,992)			(16,625)		
Other assets	97,540			91,630		
	\$ 1,402,057			\$ 1,377,307		
LIABILITIES AND SHAREHOLDERS' EQUITY						
Interest-bearing liabilities						
Interest-bearing deposits	\$ 889,531	\$ 6,510	0.98%	\$ 861,296	\$ 8,238	1.28%
Borrowings	237,491	4,760	2.68%	264,333	6,807	3.44%
Subordinated debentures	31,446	1,363	5.80%	31,014	1,229	5.30%
Total interest-bearing liabilities	1,158,468	12,633	1.46%	1,156,643	16,274	1.88%
Noninterest-bearing liabilities						
Demand deposits	115,454			93,123		
Accrued interest payable and other liabilities	9,989			9,627		
Shareholders' equity	118,146			117,914		
	\$ 1,402,057			\$ 1,377,307		

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

Net interest income/spread	\$ 34,521	3.50%	\$ 34,541	3.53%
Net interest income as a percent of average interest earning assets (1)		3.67%		3.72%

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, 2011

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 2011, a provision for loan losses of \$1.6 million was required to adequately fund the ALLL compared to a provision of \$2.7 million for the third quarter of 2010. The provision for the current quarter was the amount required to bring the ALLL to the amount determined to be adequate. Commercial loan net charge-offs during the third quarter of 2011 were \$269,000, residential mortgage loan net charge-offs were \$86,000, and installment loans net charge-offs were \$685,000. The ALLL balance at September 30, 2011 was \$19.1 million or 2.04% of total loans. This compares to an ALLL balance of \$19.1 million at December 31, 2010 or 2.11% of total loans and \$18.0 million at September 30, 2010 or 1.85% of total loans.

For the nine months ended September 30, 2011, the provision for loan losses totaled \$4.4 million compared to \$8.9 million in the prior year for the same period. Commercial loan net charge-offs during the first nine months of 2011 were \$694,000, real estate loan net charge-offs were \$827,000, and installment loan net charge-offs were \$2.9 million. The \$2.9 million in installment loan net charge-offs were comprised of \$712,000 of indirect automobile loans, \$1.2 million of home equity lines, and \$1.0 million primarily of direct home equity installment loans.

No assurance can be given that Horizon will not, in any particular period, sustain loan losses that are significant in relation to the amount reserved, or that subsequent evaluations of the loan portfolio, in light of factors then prevailing, including economic conditions and management's ongoing quarterly assessments of the portfolio, will not require increases in the allowance for loan losses. Horizon considers the allowance for loan losses to be appropriate to cover probable incurred losses in the loan portfolio as of September 30, 2011.

Non-performing loans totaled \$23.6 million on September 30, 2011, up from \$20.6 million on June 30, 2011, and from \$21.7 million on September 30, 2010. As a percentage of total loans, non-performing loans were 2.52% on September 30, 2011, up from 2.44% on June 30, 2011, and 2.22% on September 30, 2010.

The increase of non-performing loans from the prior quarter was primarily due to higher non-performing commercial loans, which increased from \$9.6 million on June 30, 2011, to \$12.1 million on September 30, 2011. This increase resulted primarily from the addition of two loans totaling \$2.1 million secured by a retail income property. Non-performing mortgage loans increased from \$7.0 million on June 30, 2011 to \$7.2 million on September 30, 2011. Non-performing installment loans increased from \$4.0 million on June 30, 2011 to \$4.3 million on September 30, 2011.

Real estate and installment non-performing loans on September 30, 2011 included \$1.5 million and \$1.9 million respectively, of loans in bankruptcy. This compares to \$1.7 million and \$2.7 million, respectively, on June 30, 2011. These loans are not considered troubled debt restructures (TDR's) while they are going through bankruptcy, a process that can take six to eighteen months. The Company's experience with loans in bankruptcy has demonstrated that some debtors continue to make payments during the bankruptcy process, many reaffirm their obligation to the Company when they come out of bankruptcy, and some loans are discharged or restructured by the court. The Company has been accumulating historical data on the performance of loans going through the bankruptcy process and utilizes that data in the calculation of the allowance for loan losses. The recent trend is for fewer loans to be involved in the bankruptcy process. There were three non-performing loans, totaling \$235,000, to commercial borrowers in bankruptcy on September 30, 2011.

TDR's are also included in the non-performing loan totals. TDR's declined from \$6.1 million on June 30, 2011 to \$5.7 million on September 30, 2011. Of these, \$3.7 million were mortgage loans, \$1.2 million were commercial loans, and \$849,000 were consumer installment loans.

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, 2011**

Non-accrual loans totaled \$17.8 million on September 30, 2011 up from \$14.4 million on June 30, 2011, and \$16.8 million on September 30, 2010. The increase in the most recent quarter was primarily due to the aforementioned addition of two large commercial loans secured by retail income property. Non-accrual commercial loans were the largest component at \$10.9 million. Non-accrual commercial loans to a hotel owner totaled \$4.2 million, and loans secured by retail strip malls totaled \$2.3 million. The hotel is under contract to sell with little or no additional loss expected. Loans 90 days delinquent but still on accrual totaled \$97,000 on September 30, 2011, up from \$55,000 on June 30, 2011, but down from \$833,000 on September 30, 2010. Horizon's policy is to place loans over 90 days delinquent on non-accrual unless they are in the process of collection and a full recovery is expected.

Other Real Estate Owned (OREO) totaled \$3.6 million on September 30, 2011, down from \$4.1 million on June 30, 2011, and \$4.1 million on September 30, 2010. During the quarter, ten properties with a book value of \$869,000 as of June 30, 2011 were sold. Another ten with a book value of \$461,000 were transferred into OREO status. Three properties were reduced through partial sales or payments by \$119,000. On September 30, 2011, OREO was comprised of 28 properties. Of these, five totaling \$1.1 million were commercial properties and 23 totaling \$2.5 million were residential real estate.

Non-Interest Income

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

	Three Months Ended		Amount Change	Percent Change
	September 30 2011	September 30 2010		
Non-interest income				
Service charges on deposit accounts	\$ 802	\$ 921	\$ (119)	-12.9%
Wire transfer fees	167	211	(44)	-20.9%
Interchange fees	721	649	72	11.1%
Fiduciary activities	1,016	934	82	8.8%
Gain (loss) on sale of securities	1,115	336	779	231.8%
Gain on sale of mortgage loans	2,145	2,473	(328)	-13.3%
Mortgage servicing net of impairment	(172)	(331)	159	-48.0%
Increase in cash surrender value of bank owned life insurance	245	246	(1)	-0.4%
Death benefit on officer life insurance	453		453	100.0%
Other income	46	209	(163)	-78.0%
Total non-interest income	\$ 6,538	\$ 5,648	\$ 890	15.8%

Service charges on deposit accounts were \$119,000 lower during the third quarter of 2011 compared to the same period in 2010 due to the regulatory changes on overdraft fees. Horizon recognized a \$1.1 million gain on the sale of securities during the third quarter of 2011 as the result of restructuring a portion of the investment portfolio, utilizing the gains to offset a \$798,000 pre-payment penalty, included in other losses, for the repayment of an FHLB advance before its scheduled maturity. The residential mortgage loan activity during the third quarter of 2011 generated \$2.1 million of income from the gain on sale of mortgage loans, down \$328,000 from the same period in 2010. This decrease was primarily due to less favorable pricing on loans sold. In addition, competition has increased for purchase transactions which drove down pricing and reduced gain. The company also recognized a \$453,000 death benefit on officer life insurance during the third quarter. Other income was \$163,000 less for the three months ended September 30, 2011 compared to the same period in 2010 as OREO losses were included in 2011 and one-time income items were included in the 2010 results.

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, 2011**

	Nine Months Ended			
	September 30 2011	September 30 2010	Amount Change	Percent Change
Non-interest income				
Service charges on deposit accounts	\$ 2,422	\$ 2,750	\$ (328)	-11.9%
Wire transfer fees	412	536	(124)	-23.1%
Interchange fees	1,905	1,663	242	14.6%
Fiduciary activities	2,911	2,936	(25)	-0.9%
Gain (loss) on sale of securities	1,754	467	1,287	275.6%
Gain on sale of mortgage loans	3,986	5,529	(1,543)	-27.9%
Mortgage servicing net of impairment	691	(363)	1,054	-290.4%
Increase in cash surrender value of bank owned life insurance	661	599	62	10.4%
Death benefit on officer life insurance	453		453	100.0%
Other income	105	828	(723)	-87.3%
Total non-interest income	\$ 15,300	\$ 14,945	\$ 355	2.4%

Service charges on deposit accounts were \$328,000 lower during the first nine months of 2011 compared to the same period in 2010 due to the regulatory changes on overdraft fees. Interchange fees increase \$242,000 during the first nine months of 2011 compared to the same period of 2010 due to increased activity. Horizon recognized a \$1.8 million gain on the sale of securities of during the first nine months of 2011 as the result of restructuring a portion of the investment portfolio, utilizing the gains to offset a \$798,000 pre-payment penalty, included in other losses, for the repayment of an FHLB advance before its scheduled maturity during the third quarter. The residential mortgage loan activity during the first nine months of 2011 generated \$4.0 million of income from the gain on sale of mortgage loans, down \$1.5 million from the same period in 2010. This decrease was primarily due to less favorable pricing on loans sold as interest rates abruptly increased at the end of the fourth quarter of 2010 negatively impacting gain-on-sale. In addition competition increased for purchase transactions which drove down pricing and reduced gain. This reduction in gain on sale of mortgage loans was partially offset by impairment recovered on the Company's mortgage servicing asset. The company also recognized a \$453,000 death benefit on officer life insurance during the third quarter. Other income was \$723,000 less for the nine months ended September 30, 2011 compared to the same period in 2010 as OREO losses were included in 2011 and one-time income items were included in the 2010 results.

Non-Interest Expense

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

	Three Months Ended			
	September 30 2011	September 30 2010	Amount Change	Percent Change
Non-interest expense				
Salaries	\$ 3,975	\$ 3,838	\$ 137	3.6%
Commission and bonuses	942	1,231	(289)	-23.5%
Employee benefits	1,164	916	248	27.1%
Net occupancy expenses	1,056	1,036	20	1.9%
Data processing	549	502	47	9.4%
Professional fees	359	417	(58)	-13.9%

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

Outside services and consultants	454	374	80	21.4%
Loan expense	820	855	(35)	-4.1%
FDIC deposit insurance	254	423	(169)	-40.0%
Other losses	1,088	143	945	660.8%
Other expenses	1,652	1,522	130	8.5%
Total non-interest expense	\$ 12,313	\$ 11,257	\$ 1,056	9.4%

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, 2011**

Total non-interest expenses were \$1.1 million higher in the third quarter of 2011 compared to the third quarter of 2010. Salaries, commissions and bonuses, and employee benefits increased \$96,000 compared to the same quarter in 2010. This increase is the result of annual merit pay increases. FDIC deposit insurance expense decreased during the third quarter of 2011 compared to 2010 as the new assessment calculation resulted in lower expense for the Bank. Other losses for the three months ending September 30, 2011 included a \$798,000 pre-payment penalty from the early repayment of an FHLB advance and \$210,000 for the settlement of a lawsuit. The increase in other expenses compared to the same period in 2010 included increases primarily in reoccurring items due to higher costs and growth.

	Nine Months Ended			
	September 30 2011	September 30 2010	Amount Change	Percent Change
Non-interest expense				
Salaries	\$ 11,509	\$ 10,776	\$ 733	6.8%
Commission and bonuses	2,158	2,329	(171)	-7.3%
Employee benefits	3,245	2,868	377	13.1%
Net occupancy expenses	3,176	3,077	99	3.2%
Data processing	1,450	1,474	(24)	-1.6%
Professional fees	1,039	1,418	(379)	-26.7%
Outside services and consultants	1,221	1,163	58	5.0%
Loan expense	2,276	2,376	(100)	-4.2%
FDIC deposit insurance	944	1,219	(275)	-22.6%
Other losses	1,365	180	1,185	658.3%
Other expenses	4,675	4,115	560	13.6%
Total non-interest expense	\$ 33,058	\$ 30,995	\$ 2,063	6.7%

Total non-interest expenses were \$2.1 million higher in the first nine months of 2011 compared to the same period in 2010. Salaries, commissions and bonuses, and employee benefits increased \$939,000 compared to the same period in 2010. This increase is the result of additional payroll expense from the consolidation of the American Trust & Savings Bank transaction that closed at the end of the second quarter of 2010, the expansion into Portage, Michigan, annual merit pay increases, and an increase in employee health insurance expense. Professional fees decreased during the first nine months of 2011 as transaction costs associated with the American Trust & Savings Bank transaction were included in the 2010 results. FDIC deposit insurance expense decreased during the first nine months of 2011 compared to 2010 as the new assessment calculation resulted in lower expense for the Bank. Other losses for the nine months ending September 30, 2011 included a \$798,000 pre-payment penalty from the early repayment of an FHLB advance, a \$210,000 settlement of a lawsuit, and write downs on bank owned property. The increase in other expenses compared to the same period in 2010 included increases primarily in reoccurring items due to higher costs and growth.

Income Taxes

Income tax expense for the third quarter of 2011 was \$1.2 million compared to \$1.1 million of tax expense for the third quarter of 2010. The effective tax rate for the third quarter of 2011 was 26.5% compared to 24.7% in 2010. The increase in the effective tax rate is primarily due to higher income before income tax for the third quarter of 2011 compared to the same period in 2010 with a similar level of tax exempt income.

Income tax expense for the first nine months of 2011 was \$3.0 million compared to \$2.0 million of tax expense for the first nine months of 2010. The effective tax rate for the first half of 2011 was 24.7% compared to 21.0% in 2010. The increase in the effective tax rate is primarily due to

higher income before income tax for the first half of 2011 compared to the same period in 2010 with a similar level of tax exempt income.

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, 2011

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, proceeds from the sale of residential mortgage loans, and borrowing relationships with correspondent banks, including the FHLB. During the nine months ended September 30, 2011, cash and cash equivalents increased by approximately \$2.8 million. At September 30, 2011, in addition to liquidity available from the normal operating, funding, and investing activities of Horizon, the Bank had approximately \$211.8 million in unused credit lines with various money center banks, including the FHLB at September 30, 2011 compared to \$380.8 million at December 31, 2010 and \$405.1 million at September 30, 2010.

Capital Resources

The capital resources of Horizon and the Bank exceeded regulatory capital ratios for well capitalized banks at September 30, 2011. Stockholders equity totaled \$118.7 million as of September 30, 2011, compared to \$112.3 million as of December 31, 2010. At September 30, 2011, the quarter's ratio of average stockholders' equity to average assets was 8.60% compared to 8.22% at December 31, 2010. Horizon's capital increased during the nine months as a result of increased earnings and an increase in accumulated other comprehensive income, net of dividends declared, the amortization of unearned compensation, and the redemption of \$18.75 million of the US Treasury's preferred stock investment under the TARP Capital Purchase Program using \$6.25 million in cash and a \$12.5 million investment by the US Treasury under the Small Business Lending Fund.

Horizon declared dividends in the amount of \$0.52 per share during the first nine months of 2011 compared to \$0.51 for the same period of 2010. The dividend payout ratio (dividends as a percent of basic earnings per share) was 21.4% and 25.6% for the first nine months of 2011 and 2010, respectively. For additional information regarding dividend conditions, see Horizon's Annual Report on Form 10-K for 2010.

SBLF Offering and TARP Repurchase

On August 25, 2011, we completed the sale of 12,500 shares of Senior Non-Cumulative Perpetual Preferred Stock, Series B (Series B Preferred Stock), for aggregate consideration of \$12.5 million, to the U.S. Treasury pursuant to the Small Business Lending Fund program. Concurrently with this transaction, we redeemed all 18,750 shares of our Fixed Rate Cumulative Perpetual Preferred Stock, Series A (Series A Preferred Stock), that remained outstanding under the TARP Capital Purchase Program. The redemption of the Series A Preferred stock was funded by the \$12.5 million in proceeds from the sale of the Series B Preferred Stock together with other available funds.

Table of Contents

HORIZON BANCORP AND SUBSIDIARIES

Quantitative and Qualitative Disclosures About Market Risk

For the Three and Nine Months Ended September 30, 2011

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Refer to Horizon's 2010 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 2010 Annual Report on Form 10-K.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation Of Disclosure Controls And Procedures

Based on an evaluation of disclosure controls and procedures as of September 30, 2011, 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 Control Over Financial Reporting

Horizon's management, including its Chief Executive Officer and Chief Financial Officer, also have concluded that during the fiscal quarter ended September 30, 2011, 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 Three and Nine Months Ended September 30, 2011

ITEM 1. LEGAL PROCEEDINGS

On August 31, 2011, Horizon reached a settlement with respect to claims made by Capitol Bancorp and one of its subsidiaries, Michigan Commerce Bank, in a Verified Complaint filed in Kalamazoo County Circuit Court, Case No. 2010-0300-CK, on September 1, 2010. Horizon paid \$210,000 to settle the claims without admitting any liability or wrongdoing.

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

An investment in Horizon's securities is subject to risks inherent to our business. The material risks and uncertainties that management believes currently affect Horizon are described below. Before making an investment decision, you should carefully consider these risks as well as information we include or incorporate by reference in this report and other filings we make with the SEC. The risks and uncertainties we have described are not the only ones facing our company. Additional risks and uncertainties not presently known to us or that we currently deem immaterial may also affect our business operations.

If any of these risks or uncertainties materializes or any of these assumptions proves incorrect, our results could differ materially from the forward-looking statements. All forward-looking statements in this report are current only as of the date on which the statements were made. We do not undertake any obligation to publicly update any forward-looking statement to reflect events or circumstances after the date on which any statement is made or to reflect the occurrence of unanticipated events.

Risks Related to Our Business

As a financial institution, we are subject to a number of risks relating to our day-to-day business.

As a financial institution, we are subject to a number of risks relating to our daily business. Although we undertake a variety of efforts to manage and control those risks, many of the risks are outside of our control. Among the risks we face are the following:

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 our 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 our 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 our regulators or additional regulation could hinder our ability to do business profitably.

Table of Contents

HORIZON BANCORP AND SUBSIDIARIES

Part II Other Information

For the Three and Nine Months Ended September 30, 2011

The current economic environment poses significant challenges for us and could adversely affect our financial condition and results of operations.

We are operating in a challenging and uncertain economic environment, including generally uncertain national conditions and local conditions in our markets. The capital and credit markets have been experiencing volatility and disruption since 2008. This presents financial institutions with unprecedented circumstances and challenges which in some cases have resulted in large declines in the fair values of investments and other assets, constraints on liquidity and significant credit quality problems, including severe volatility in the valuation of real estate and other collateral supporting loans. Our financial statements have been prepared using values and information currently available to us, but given this volatility, the values of assets and liabilities recorded in the financial statements could change rapidly, resulting in material future adjustments in asset values and the allowance for loan losses, which could negatively impact our ability to meet regulatory capital requirements and maintain sufficient liquidity. The risks associated with our business become more acute in periods of a slowing economy or slow growth such as we began experiencing in the latter half of 2008 and which have continued in 2011. Financial institutions continue to be affected by sharp declines in the real estate market and constrained financial markets. While we continue to take steps to decrease and limit our exposure to residential construction and land development loans and home equity loans, we nonetheless retain direct exposure to the residential and commercial real estate markets, and we are affected by these events.

Continued declines in real estate values, home sales volumes and financial stress on borrowers as a result of the uncertain economic environment, including job loss, could have an adverse effect on our borrowers or their customers, which could adversely affect our financial condition and results of operations. In addition, the national economic recession or further deterioration in local economic conditions in our markets could drive losses beyond that which is provided for in our allowance for loan losses and result in the following other consequences: increases in loan delinquencies, problem assets and foreclosures; demand for our products and services may decline; deposits may decrease, which would adversely impact our liquidity position; and collateral for our loans, especially real estate, may decline in value, in turn reducing customers' borrowing power, and reducing the value of assets and collateral associated with our existing loans.

Our financial performance may be adversely impacted if we are unable to continue to grow our commercial and consumer loan portfolios, obtain low-cost funds and compete with other providers of financial services.

Our ability to maintain our history of record earnings year after year will depend, in large part, on our ability to continue to grow our loan portfolios and obtain low-cost funds. For the past five years, we focused on increasing consumer loans, and we intend to continue to emphasize and grow consumer, as well as commercial loans in the foreseeable future. This represented a shift in our emphasis from prior years when we focused on mortgage banking services, which generated a large portion of our income during those years.

We have also funded our growth with low-cost consumer deposits, and our ability to sustain our growth will depend in part on our continued success in attracting and retaining such deposits or finding other sources of low-cost funds.

Another factor in maintaining our history of record earnings will be our ability to expand our scope of available financial services to our customers in an increasingly competitive environment. In addition to other banks, our competitors include credit unions, securities brokers and dealers, mortgage brokers, mortgage bankers, investment advisors, and finance and insurance companies. Competition is intense in most of our markets. We compete on price and service with our competitors. Competition could intensify in the future as a result of industry consolidation, the increasing availability of products and services from non-banks, greater technological developments in the industry, and banking reform.

The recent repeal of federal prohibitions on payment of interest on demand deposits could increase our interest expense.

All federal prohibitions on the ability of financial institutions to pay interest on demand deposit accounts were repealed as part of the Dodd-Frank Act. As a result, since July 21, 2011, financial institutions can offer interest on demand deposits to compete for customers. We are offering interest on demand deposits, but we do not expect this change to have a material adverse effect on our financial condition and results of operations.

Table of Contents

HORIZON BANCORP AND SUBSIDIARIES

Part II Other Information

For the Three and Nine Months Ended September 30, 2011

Our commercial and consumer loans expose us to increased credit risks.

We have a large percentage of commercial and consumer loans. Commercial loans generally have greater credit risk than residential mortgage loans because repayment of these loans often depends on the successful business operations of the borrowers. These loans also typically have much larger loan balances than residential mortgage loans. Consumer loans generally involve greater risk than residential mortgage loans because they are unsecured or secured by assets that depreciate in value. Although we undertake a variety of underwriting, monitoring and reserving protections with respect to these types of loans, there can be no guarantee that we will not suffer unexpected losses, and recently, we have experienced an increase in the default rates in our consumer loan portfolio, particularly relating to indirect auto loans.

Our holdings of construction, land and home equity loans, may pose more credit risk than other types of mortgage loans.

In light of current economic conditions, construction loans, loans secured by commercial real estate and home equity loans are considered more risky than other types of mortgage loans. Due to the disruptions in credit and housing markets, real estate values have decreased in most areas of the U.S., and many of the developers to whom we lend experienced a decline in sales of new homes from their projects. As a result of this market disruption, some of our land and construction loans have become non-performing as developers are unable to build and sell homes in volumes large enough for orderly repayment of loans and as other owners of such real estate (including homeowners) were unable to keep up with their payments. We believe we have established adequate reserves on our financial statements to cover the credit risk of these loan portfolios. However, there can be no assurance that losses will not exceed our reserves, and ultimately result in a material level of charge-offs, which could adversely impact our results of operations, liquidity and capital.

The allowance for loan losses may prove inadequate or be negatively affected by credit risk exposures.

Our business depends on the creditworthiness of our customers. We periodically review the allowance for loan and lease losses for adequacy considering economic conditions and trends, collateral values, and credit quality indicators, including past charge-off experience and levels of past due loans and non-performing assets. There is no certainty that the allowance for loan losses will be adequate over time to cover credit losses in the portfolio because of unanticipated adverse changes in the economy, market conditions or events adversely affecting specific customers, industries or markets. If the credit quality of the customer base materially decreases, if the risk profile of a market, industry or group of customers changes materially, or if the allowance for loan losses is not adequate, our business, financial condition, liquidity, capital, and results of operations could be materially adversely affected.

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.

Table of Contents

HORIZON BANCORP AND SUBSIDIARIES

Part II Other Information

For the Three and Nine Months Ended September 30, 2011

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 (and other loans), which could result in a significant decline in our revenue stream.

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.

A continued economic slowdown in Northwestern Indiana and Southwestern Michigan could affect our business.

Our primary market area for deposits and loans consists of LaPorte and Porter Counties in Northwestern Indiana and Berrien County in Southwestern Michigan. During 2011, unemployment rates have remained at or near record levels in our primary market area, resulting in continued high levels of consumer delinquencies and bankruptcy filings. The continued economic slowdown could hurt our business. The possible consequences of such a continued downturn could include the following:

increases in loan delinquencies and foreclosures;

declines in the value of real estate and other collateral for loans;

an increase in loans charged off;

a decline in the demand for our products and services;

an increase in non-accrual loans and other real estate owned.

The loss of key members of our senior management team could affect our ability to operate effectively.

We depend heavily on the services of our existing senior management team, particularly our CEO Craig M. Dwight, to carry out our business and investment strategies. As we continue to grow and expand our business and our locations, products and services, we will increasingly need to rely on Mr. Dwight's experience, judgment and expertise as well as that of the other members of our senior management team and will also need to continue to attract and retain qualified banking personnel at all levels. Competition for such personnel is intense in our geographic market areas. If we are unable to attract and retain talented people, our business could suffer. The loss of the services of any senior management personnel, particularly Mr. Dwight or the inability to recruit and retain qualified personnel in the future, could have a material adverse effect on our consolidated results of operations, financial condition and prospects.

We may need to raise additional capital in the future, and such capital may not be available when needed or at all.

We may need to raise additional capital in the future to fund acquisitions and to provide us with sufficient capital resources and liquidity to meet our commitments, regulatory capital requirements and business needs, particularly if our asset quality or earnings were to deteriorate

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

significantly. Although we are currently, and have historically been, well capitalized for regulatory purposes, our capital levels are not far in excess of the well capitalized threshold, and we have been required to maintain increased levels of capital in the past in connection with certain acquisitions. Additionally, we periodically explore acquisition opportunities with other financial institutions, some of which are in distressed financial condition. Any future acquisition, particularly the acquisition of a significantly troubled institution or an institution of comparable size to us, may require us to raise additional capital in order to obtain regulatory approval and/or to remain well capitalized.

Table of Contents

HORIZON BANCORP AND SUBSIDIARIES

Part II Other Information

For the Three and Nine Months Ended September 30, 2011

Our ability to raise additional capital, if needed, will depend on, among other things, conditions in the capital markets at that time, which are outside of our control, and our financial performance. Economic conditions and the loss of confidence in financial institutions may increase our cost of funding and limit access to certain customary sources of capital, including inter-bank borrowings, repurchase agreements and borrowings from the discount window of the Federal Reserve.

We cannot guaranty that such capital will be available on acceptable terms or at all. Any occurrence that may limit our access to the capital markets, such as a decline in the confidence of debt purchasers, our depositors or counterparties participating in the capital markets may adversely affect our capital costs and our ability to raise capital and, in turn, our liquidity. Moreover, if we need to raise capital in the future, we may have to do so when many other financial institutions are also seeking to raise capital and would have to compete with those institutions for investors. An inability to raise additional capital on acceptable terms when needed could have a materially adverse effect on our businesses, financial condition and results of operations and may restrict our ability to grow.

Potential acquisitions may disrupt our business and dilute stockholder value.

We periodically evaluate merger and acquisition opportunities and conduct due diligence activities related to possible transactions with other financial institutions and financial services companies. We generally seek merger or acquisition partners that are culturally similar and possess either significant market presence or have potential for improved profitability through financial management, economies of scale or expanded services. Acquiring other banks, businesses, or branches involves various risks commonly associated with acquisitions, including, among other things:

Potential exposure to unknown or contingent liabilities of the target company,

Exposure to potential asset quality issues of the target company,

Potential disruption to our business,

Potential diversion of our management's time and attention away from day-to-day operations,

The possible loss of key employees, business and customers of the target company,

Difficulty in estimating the value of the target company, and

Potential problems in integrating the target company's systems, customers and employees with ours.

As a result, merger or acquisition discussions and, in some cases, negotiations may take place and future mergers or acquisitions involving the payment of cash or the issuance of our debt or equity securities may occur at any time. Acquisitions typically involve the payment of a premium over book and market values, and, therefore, some dilution of our tangible book value and net income per common share may occur in connection with any future transaction. To the extent we were to issue additional common shares in any such transaction, our current shareholders would be diluted and such an issuance may have the effect of decreasing our stock price, perhaps significantly. Furthermore, failure

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

to realize the expected revenue increases, cost savings, increases in geographic or product presence, and/or other projected benefits from an acquisition could have a material adverse effect on our financial condition and results of operations.

The preparation of our financial statements requires the use of estimates that may vary from actual results.

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make significant estimates that affect the financial statements. One of our most critical estimates is the level of the allowance for loan losses. Due to the inherent nature of these estimates, we cannot provide absolute assurance that we will not have to increase the allowance for loan losses and/or sustain loan losses that are significantly higher than the provided allowance.

Table of Contents

HORIZON BANCORP AND SUBSIDIARIES

Part II Other Information

For the Three and Nine Months Ended September 30, 2011

Our mortgage warehouse and indirect lending operations are subject to a higher fraud risk than our other lending operations.

We buy loans originated by mortgage bankers and automobile dealers. Because we must rely on the mortgage bankers and automobile dealers in making and documenting these loans, there is an increased risk of fraud to us on the part of the third-party originators and the underlying borrowers. In order to guard against this increased risk, we perform investigations on the loan originators with whom we do business, and we review the loan files and loan documents we purchase to attempt to detect any irregularities or legal noncompliance. However, there is no guarantee that our procedures will detect all cases of fraud or legal noncompliance.

Our mortgage lending profitability could be significantly reduced if we are not able to resell mortgages or experience other problems with this process.

Currently, we sell a substantial portion of the mortgage loans we originate. The profitability of our mortgage banking operations depends in large part upon our ability to aggregate a high volume of loans and to sell them in the secondary market at a gain. Thus, we are dependent upon the existence of an active secondary market and our ability to profitably sell loans into that market.

Our ability to sell mortgage loans readily is dependent upon the availability of an active secondary market for single-family mortgage loans, which in turn depends in part upon the continuation of programs currently offered by Fannie Mae, Freddie Mac and Ginnie Mae (the Agencies) and other institutional and non-institutional investors. These entities account for a substantial portion of the secondary market in residential mortgage loans. Some of the largest participants in the secondary market, including the Agencies, are government-sponsored enterprises whose activities are governed by federal law. Any future changes in laws that significantly affect the activity of such government-sponsored enterprises could, in turn, adversely effect our operations.

In September 2008, Fannie Mae and Freddie Mac were placed into conservatorship by the U.S. government. Although to date, the conservatorship has not had a significant or adverse effect on our operations, it is currently unclear whether further changes would significantly and adversely affect our operations. In addition, our ability to sell mortgage loans readily is dependent upon our ability to remain eligible for the programs offered by the Agencies and other institutional and non-institutional investors. Our ability to remain eligible may also depend on having an acceptable peer-relative delinquency ratio for Federal Housing Authority (FHA) and maintaining a delinquency rate with respect to Ginnie Mae pools that are below Ginnie Mae guidelines. In the case of Ginnie Mae pools, we have repurchased delinquent loans from them in the past to maintain compliance with the minimum required delinquency ratios. Although these loans are typically insured as to principal by the FHA, such repurchases increase our capital and liquidity needs, and there can be no assurance that we will have sufficient capital or liquidity to continue to purchase such loans out of the Ginnie Mae pools if required to do so.

Any significant impairment of our eligibility with any of the Agencies could materially and adversely affect our operations. Further, the criteria for loans to be accepted under such programs may be changed from time-to-time by the sponsoring entity which could result in a lower volume of corresponding loan originations. The profitability of participating in specific programs may vary depending on a number of factors, including our administrative costs of originating and purchasing qualifying loans and our costs of meeting such criteria.

We are exposed to intangible asset risk; specifically, our goodwill may become impaired.

As of September 30, 2011, we had \$8.3 million of goodwill and other intangible assets. A significant and sustained decline in our stock price and market capitalization, a significant decline in our expected future cash flows, a significant adverse change in the business climate, or slower growth rates could result in further impairment of goodwill. If we were to conclude that a future write-down of our goodwill is necessary, then

Table of Contents

HORIZON BANCORP AND SUBSIDIARIES

Part II Other Information

For the Three and Nine Months Ended September 30, 2011

we would record the appropriate charge, which could be materially adverse to our operating results and financial position. For further discussion, see Notes 1 and 9, *Nature of Operations and Summary of Significant Accounting Policies* and *Intangible Assets*, to the Consolidated Financial Statements included in Item 8 of our Annual Report on Form 10-K for the year ended December 31, 2010.

We are subject to extensive regulation and changes in laws, regulations and policies could adversely affect our business.

Our operations are subject to extensive regulation by federal agencies. See *Supervision and Regulation* in the description of our Business in Part I of our 2010 Form 10-K for detailed information on the laws and regulations to which we are subject. As apparent from the recent Emergency Economic Stabilization Act (EESA), Troubled Asset Relief Program (TARP), the American Recovery and Reinvestment Act of 2009 (ARRA) and the Dodd-Frank Act of 2010 legislation, changes in applicable laws, regulations or regulator policies can materially affect our business. The likelihood of any major changes in the future and their effects are impossible to determine.

In addition to the EESA, TARP, ARRA and Dodd-Frank mentioned above, federal and state governments could pass additional legislation responsive to current credit conditions. As an example, the Bank could experience higher credit losses because of federal or state legislation or regulatory action that reduces the amount the Bank's borrowers are otherwise contractually required to pay under existing loan contracts. Also, the Bank could experience higher credit losses because of federal or state legislation or regulatory action that limits its ability to foreclose on property or other collateral or makes foreclosure less economically feasible.

The new laws described above, together with additional actions announced by the U.S. Treasury and other regulatory agencies continue to develop. It is not clear at this time what impact, EESA, TARP, Dodd-Frank other liquidity and funding initiatives of the U.S. Treasury and other bank regulatory agencies that have been previously announced, and any additional programs that may be initiated in the future, will have on the financial markets and the financial services industry. The extreme levels of volatility and limited credit availability currently being experienced could continue to effect the U.S. banking industry and the broader U.S. and global economies, which will have an affect on all financial institutions, including Horizon.

Our inability to continue to accurately process large volumes of transactions could adversely impact our business and financial results.

In the normal course of business, we process large volumes of transactions. If systems of internal control should fail to work as expected, if systems are used in an unauthorized manner, or if employees subvert the system of internal controls, significant losses could result.

We process large volumes of transactions on a daily basis and are exposed to numerous types of operational risk. Operational risk resulting from inadequate or failed internal processes, people and systems includes the risk of fraud by persons inside or outside Horizon, the execution of unauthorized transactions by employees, errors relating to transaction processing and systems, and breaches of the internal control system and compliance requirements. This risk of loss also includes the potential legal actions that could arise as a result of the operational deficiency or as a result of noncompliance with applicable regulatory standards.

We establish and maintain systems of internal operational controls that are designed to provide us with timely and accurate information about our level of operational risk. While not foolproof, these systems have been designed to manage operational risk at appropriate, cost-effective levels. Procedures also exist that are designed to ensure that policies relating to conduct, ethics and business practices are followed. From time to time, losses from operational risk may occur, including the effects of operational errors.

While we continually monitor and improve the system of internal controls, data processing systems and corporate-wide processes and procedures, there can be no assurance that future losses will not occur.

Table of Contents

HORIZON BANCORP AND SUBSIDIARIES

Part II Other Information

For the Three and Nine Months Ended September 30, 2011

Our information systems may experience an interruption or breach in security.

We rely heavily on communications and information systems to conduct our business. Any failure, interruption or breach in security of these systems could result in failures or disruptions in our customer relationship management, general ledger, deposit, loan and other systems. While we have policies and procedures designed to prevent or limit the effect of the failure, interruption or security breach of our information systems, there can be no assurance that any such failures, interruptions or security breaches will not occur or, if they do occur, that they will be adequately or timely addressed. The occurrence of any failures, interruptions or security breaches of our information systems could damage our reputation, result in a loss of customer business, subject us to additional regulatory scrutiny, or expose us to civil litigation and possible financial liability, any of which could have a material adverse effect on our financial condition and results of operations.

We continually encounter technological changes.

The financial services industry is continually undergoing rapid technological change with frequent introductions of new technology-driven products and services. The effective use of technology increases efficiency and enables financial institutions to better serve customers and to reduce costs. Our future success depends, in part, upon our ability to address the needs of our customers by using technology to provide products and services that will satisfy customer demands, as well as to create additional efficiencies in our operations. Many of our competitors have substantially greater resources to invest in technological improvements, and we may not be able to effectively implement new technology-driven products and services or be successful in marketing these products and services to our customers. Failure to successfully keep pace with technological change affecting the financial services industry could have a material adverse impact on our business and, in turn, our financial condition and results of operations.

The soundness of other financial institutions could adversely affect us.

Financial services institutions are interrelated as a result of trading, clearing, counterparty, or other relationships. We have exposure to many different industries and counterparties, and we routinely execute transactions with counterparties in the financial services industry, including brokers and dealers, commercial banks, investment banks, mutual and hedge funds, and other institutional clients. Many of these transactions expose us to credit risk in the event of default by our counterparty or client. In addition, our credit risk may be exacerbated when the collateral held by us cannot be realized or is liquidated at prices not sufficient to recover the full amount of the loan or derivative exposure due us. There is no assurance that any such losses would not materially and adversely affect our results of operations or earnings.

The Standard & Poor's downgrade in the U.S. government's sovereign credit rating, and in the credit ratings of instruments issued, insured or guaranteed by certain related institutions, agencies and instrumentalities, could result in risks to Horizon and general economic conditions that we are not able to predict.

On August 5, 2011, Standard & Poor's downgraded the United States long-term debt rating from its AAA rating to AA+. On August 8, 2011, Standard & Poor's downgraded the credit ratings of certain long-term debt instruments issued by Fannie Mae and Freddie Mac and other U.S. government agencies linked to long-term U.S. debt. Instruments of this nature are key assets on the balance sheets of financial institutions, including the Bank. These downgrades could adversely affect the market value of such instruments, and could adversely impact our ability to obtain funding that is collateralized by affected instruments, as well as affecting the pricing of that funding when it is available. We cannot predict if, when or how these changes to the credit ratings will affect economic conditions. These ratings downgrades could result in a significant adverse impact to Horizon and could exacerbate the other risks to which Horizon is subject.

Risks Related to our Common Stock

The price of our common stock may fluctuate significantly, and this may make it difficult for you to resell our common stock at times or at prices you find attractive.

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

Although our common stock is listed on the NASDAQ Global Market, our stock price constantly changes (sometimes dramatically), and we expect our stock price to continue to fluctuate in the future. Our stock price is impacted by a variety of factors, some of which are beyond our control.

Table of Contents

HORIZON BANCORP AND SUBSIDIARIES

Part II Other Information

For the Three and Nine Months Ended September 30, 2011

These factors include:

variations in our operating results or the quality of our assets;

operating results that vary from the expectations of management, securities analysts and investors;

increase in loan losses, non-performing loans and other real estate owned;

changes in expectations as to our future financial performance;

announcements of new products, strategic developments, acquisitions and other material events by us or our competitors;

the operating and securities price performance of other companies that investors believe are comparable to us;

actual or anticipated sales of our equity or equity-related securities;

our past and future dividend practice;

our creditworthiness;

interest rates;

the credit, mortgage and housing markets, the markets for securities relating to mortgages or housing;

developments with respect to financial institutions generally; and

economic, financial, geopolitical, regulatory, congressional or judicial events that affect us or the financial markets.

In addition the stock market in general has recently experienced extreme price and volume fluctuations. This volatility has had a significant effect on the market price of securities issued by many companies and particularly those in the financial services and banking sector, including for reasons unrelated to their operating performance. These broad market fluctuations may adversely affect our stock price, notwithstanding our

operating results.

Because our stock is thinly traded, it may be more difficult for you to sell your shares or buy additional shares when you desire to do so and the price may be volatile.

Although our common stock has been listed on the NASDAQ stock market since December 2001, our common stock is thinly traded. The prices of thinly traded stocks, such as ours, are typically more volatile than stocks traded in a large, active public market and can be more easily impacted by sales or purchases of large blocks of stock. Thinly traded stocks are also less liquid, and because of the low volume of trades, you may be unable to sell your shares when you desire to do so.

Table of Contents

HORIZON BANCORP AND SUBSIDIARIES

Part II Other Information

For the Three and Nine Months Ended September 30, 2011

Our participation in the Small Business Lending Fund program restricts our ability to pay dividends to repurchase our securities and could have other negative effects.

On August 25, 2011, we sold 12,500 shares of Senior Non-Cumulative Perpetual Preferred Stock, Series B (Series B Preferred Stock), to the U.S. Treasury pursuant to the Small Business Lending Fund program, a \$30 billion fund established under the Small Business Jobs Act of 2010 that encourages lending to small businesses by providing capital to qualified community banks with assets of less than \$10 billion. The terms of the Series B Preferred Stock impose limits on our ability to pay dividends and repurchase shares of common stock. Under the terms of the Series B Preferred Stock, no repurchases may be effected, and no dividends may be declared or paid on preferred shares ranking *pari passu* with the Series B Preferred Stock, junior preferred shares, or other junior securities (including our common stock) during the current quarter and for the next three quarters following the failure to declare and pay dividends on the Series B Preferred Stock, except that, in any such quarter in which the dividend is paid, dividend payments on shares ranking *pari passu* may be paid to the extent necessary to avoid any resulting material covenant breach. In addition, we may declare and pay a dividend on our common stock or other stock junior to the Series B Preferred Stock, or repurchase shares of any such class or series of stock, only if, after payment of such dividend, the dollar amount of the Company's Tier 1 Capital would be at least 90% of the Signing Date Tier 1 Capital, which was \$118,724,000, excluding any subsequent net charge-offs and any redemption of the Series B Preferred Stock.

Provisions in our articles of incorporation, our by-laws, and Indiana law may delay or prevent an acquisition of us by a third party.

Our articles of incorporation and by-laws and Indiana law contain provisions which have certain anti-takeover effects. While the purpose of these provisions is to strengthen the negotiating position of the board in the event of a hostile takeover attempt, the overall effects of these provisions may be to render more difficult or discourage a merger, tender offer or proxy contest, the assumption of control by a holder of a larger block of our shares, and the removal of incumbent directors and key management.

Our articles of incorporation provide for a staggered board, which means that only one-third of our board can be replaced by shareholders at any annual meeting. Our articles also provide that our directors may only be removed without cause by shareholders owning 70% or more of our outstanding common stock. Furthermore, our articles provide that only our board of directors, and not our shareholders, may adopt, alter, amend and repeal our by-laws.

Our articles also preempt Indiana law with respect to business combinations with a person who acquires 10% or more of our common stock and provide that such transactions are subject to independent and super-majority shareholder approval requirements unless certain pricing and board pre-approval requirements are satisfied.

Our by-laws do not permit cumulative voting of shareholders in the election of directors, allowing the holders of a majority of our outstanding shares to control the election of all our directors, and our directors are elected by plurality (not majority) voting. Our by-laws also establish detailed procedures that shareholders must follow if they desire to nominate directors for election or otherwise present issues for consideration at a shareholders' meeting. We also have a mandatory retirement age for directors.

These and other provisions of our governing documents and Indiana law are intended to provide the board of directors with the negotiating leverage to achieve a more favorable outcome for our shareholders in the event of an offer for the company. However, there is no assurance that these same anti-takeover provisions could not have the effect of delaying, deferring or preventing a transaction or a change in control that might be in the best interest of our shareholders.

Table of Contents

HORIZON BANCORP AND SUBSIDIARIES

Part II Other Information

For the Three and Nine Months Ended September 30, 2011

Risks Related to the Series B Preferred Stock

The Series B Preferred Stock is equity and is subordinate to all of our existing and future indebtedness; regulatory and contractual restrictions may limit or prevent us from paying dividends on the Series B Preferred Stock; and the Series B Preferred Stock places no limitations on the amount of indebtedness we and our subsidiaries may incur in the future.

Shares of the Series B Preferred Stock are equity interests in Horizon and do not constitute indebtedness. As such, the Series B Preferred Stock, like our common stock, ranks junior to all indebtedness and other non-equity claims against Horizon with respect to assets available to satisfy claims against Horizon, including in a liquidation of Horizon. Additionally, unlike indebtedness, where principal and interest would customarily be payable on specified due dates, in the case of preferred stock like the Series B Preferred Stock, dividends are payable only when, as and if authorized and declared by, our Board of Directors and depend on, among other things, our results of operations, financial condition, debt service requirements, other cash needs and any other factors our Board of Directors deems relevant.

Horizon is an entity separate and distinct from the Bank, our principal subsidiary, and derives a significant portion of its revenue in the form of dividends from the Bank. Accordingly, Horizon is and will be dependent upon dividends from the Bank to pay the principal of and interest on its indebtedness, to satisfy its other cash needs and to pay dividends on the Series B Preferred Stock. Horizon's ability to pay dividends is subject to its ability to earn net income and to meet certain regulatory requirements while maintaining its required capital. In the event the Bank is unable to pay dividends to Horizon, Horizon may not be able to pay dividends on the Series B Preferred Stock. In addition, the Series B Preferred Stock does not limit the amount of debt or other obligations we or our subsidiaries may incur in the future. Accordingly, we and our subsidiaries may incur substantial amounts of additional debt and other obligations that will rank senior to the Series B Preferred Stock or to which the Series B Preferred Stock will be structurally subordinated.

An active trading market for the Series B Preferred Stock does not currently exist and is unlikely to develop.

The Series B Preferred Stock is not currently listed on any national securities exchange, and we do not intend to list the Series B Preferred Stock on a national securities exchange unless we are requested to do so by the U.S. Treasury. Even if requested to do so by the U.S. Treasury, it is not certain that such a listing can be achieved given the current exchange listing requirements, and even if listing is achieved, it is unlikely that an active trading market for the Series B Preferred Stock will develop, or, if developed, that an active trading market will be maintained. If an active trading market does not develop, the market value and liquidity of the Series B Preferred Stock may be adversely affected.

Dividends on the Series B Preferred Stock are non-cumulative.

Dividends on the shares of Series B Preferred Stock are non-cumulative. If our Board of Directors does not authorize and declare a dividend on the Series B Preferred Stock for any dividend period, such unpaid dividend will not accrue and will not be payable to holders of the Series B Preferred Stock even if dividends are declared for any subsequent dividend period.

Initially the dividend rate on the Series Preferred Stock will fluctuate based on our level of Qualified Small Business Lending as compared to our Small Business Lending Baseline.

The per annum dividend rate on the shares of Series B Preferred Stock applicable to the first quarter is five percent. For the second through tenth quarters, the rate will be adjusted quarterly to reflect the percent of change in our Qualified Small Business Lending from our Small Business Lending baseline and may fluctuate between one percent and five percent per annum. The dividend rate will be a fixed rate for the eleventh quarter through the date that is four-and-a-half years from the issuance date of the shares of Series B Preferred Stock and will be based on the rate in effect for the tenth quarter. Depending on the percentage increase in our Qualified Small Business Lending over our Small Business Lending baseline, the fixed rate will be between one percent and five percent per annum. If there has been no increase (or a decrease) in our Qualified Small Business Lending over our Small Business Lending baseline, the fixed rate will be seven percent per annum. For all quarters subsequent to the four-and-one-half anniversary of issuance, the rate will be nine percent per annum.

Table of Contents

HORIZON BANCORP AND SUBSIDIARIES

Part II Other Information

For the Three and Nine Months Ended September 30, 2011

Holders of the Series B Preferred Stock have limited voting rights.

Holders of the Series B Preferred Stock only have the right to vote as a separate class on certain matters relating to the rights of holders of Series B Preferred Stock and on certain corporate transactions. Except with respect to such matters, the Series B Preferred Stock does not have voting rights. The matters on which the holders of Series B Preferred Stock would have the right to vote include amendments to Horizon's Articles of Incorporation adversely affecting the Series B Preferred Stock or certain fundamental transactions affecting the Series B Preferred Stock, and in connection with the authorization of stock senior to the Series B Preferred Stock. If Horizon misses five dividend payments on the Series B Preferred Stock, whether or not consecutive, the holder of the Series B Preferred Stock will have the right, but not the obligation, to appoint a representative as an observer who will attend all meetings of Horizon's Board of Directors, but such observer will not have the right to vote.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Unregistered Sales of Equity Securities

On August 25, 2011, Horizon issued and sold to the Secretary of the U.S. Treasury 12,500 shares of Senior Non-Cumulative Perpetual Preferred Stock, Series B (Series B Preferred Stock), par value \$0.01 per share, having a liquidation value of \$1,000 per share, for a capital contribution of \$12,500,000. The sale was made in conjunction with the U.S. Treasury's SBLF program established under the Small Business Jobs Act of 2010. Horizon issued the shares of Series B Preferred Stock in reliance upon the exemption from registration provided by Section 4(2) of the Securities Act of 1933, as amended. There was no underwriter associated with this transaction. Proceeds from the transaction were used to redeem 12,500 shares of Horizon's Fixed-Rate Cumulative Perpetual Preferred Stock, Series A (Series A Preferred Stock). On August 25, 2011, Horizon used the proceeds from the issuance of the Series B Preferred Stock, together with other available funds, to repurchase from the U.S. Treasury the remaining 18,750 shares of its Series A Preferred Stock at a liquidation amount of \$1,000 per share for a redemption price of \$18,750,000, plus accrued but unpaid dividends to the redemption date. The Series A Preferred Stock was issued to the U.S. Treasury in December 2008 in connection with Horizon's participation in the TARP Capital Purchase Program. Additional information on the Series A Preferred Stock redemption and the Series B Preferred Stock issuance, including terms of the SBLF program, are included in our Form 8-K, filed with the SEC on August 26, 2011.

Table of Contents**HORIZON BANCORP AND SUBSIDIARIES****Part II Other Information****For the Three and Nine Months Ended September 30, 2011****Issuer Purchases of Equity Securities**

The following table presents information with respect to purchases that we made of our common stock during the quarter ended September 30, 2011:

Issuer Purchases of Equity Securities

	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Minimum Number of Shares That may yet be Purchased Under the Plan or Program
July 1 31, 2011		\$		
August 1 31, 2011		\$		
September 1 30, 2011	16,064(1)	\$ 26.30		

- (1) The 16,064 shares purchases were not part of a publicly announced repurchase plan or program. The repurchased shares were formerly restricted shares that had been issued to certain employees who were subject to restrictions on the receipt of cash bonuses and other payments under the TARP Capital Purchase Program. The restrictions lapsed on August 15, 2011, when Horizon redeemed the 18,750 shares of Series A Preferred Stock that remained outstanding under the TARP Capital Purchase Program.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not Applicable

ITEM 4. (REMOVED AND RESERVED)

Not Applicable

ITEM 5. OTHER INFORMATION

Not Applicable

Table of Contents

HORIZON BANCORP AND SUBSIDIARIES

Part II Other Information

For the Three and Nine Months Ended September 30, 2011

ITEM 6. EXHIBITS

(a) Exhibits

Exhibit No.	Description
3.1	Articles of Incorporation of Horizon Bancorp, as amended
4.1	Form of Certificate for Senior Non-Cumulative Perpetual Preferred Stock, Series B. Incorporated by reference to Exhibit 4.2 in the Registrants Form 8-K filed on August 26, 2011.
10.1	Securities Purchase Agreement, dated August 25, 2011, between the Secretary of the U.S. Treasury and Horizon Bancorp. Incorporated by reference to Exhibit 10.1 in the Registrants Form 8-K filed on August 26, 2011.
10.2	Repurchase Letter Agreement, dated August 25, 2011, between the Secretary of the U.S. Treasury and Horizon Bancorp. Incorporated by reference to Exhibit 10.2 in the Registrants Form 8-K filed on August 26, 2011.
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
Exhibit 101	Interactive Data File*

* Pursuant to Rule 406T of Regulation S-T, the Interactive Data Files in Exhibit 101 hereto are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, are deemed not filed for purposes of Section 18 of the Securities and Exchange Act of 1934, as amended, and otherwise are not subject to liability under those sections.

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 14, 2011

/s/ CRAIG M. DWIGHT
Craig M. Dwight
Chief Executive Officer

Dated: November 14, 2011

/s/ MARK E. SECOR
Mark E. Secor
Chief Financial Officer

Table of Contents**INDEX TO EXHIBITS**

Exhibit No.	Description	Location
3.1	Articles of Incorporation of Horizon Bancorp, as amended	Attached
4.1	Form of Certificate for Senior Non-Cumulative Perpetual Preferred Stock, Series B.	Incorporated by reference to Exhibit 4.2 in the Registrants Form 8-K filed on August 26, 2011
10.1	Securities Purchase Agreement, dated August 25, 2011, between the Secretary of the U.S. Treasury and Horizon Bancorp.	Incorporated by reference to Exhibit 10.1 in the Registrants Form 8-K filed on August 26, 2011.
10.2	Repurchase Letter Agreement, dated August 25, 2011, between the Secretary of the U.S. Treasury and Horizon Bancorp.	Incorporated by reference to Exhibit 10.2 in the Registrants Form 8-K filed on August 26, 2011
Exhibit 31.1	Certification of Craig M. Dwight	Attached
Exhibit 31.2	Certification of Mark E. Secor	Attached
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	Attached
Exhibit 101	Interactive Data File*	Attached

* Pursuant to Rule 406T of Regulation S-T, the Interactive Data Files in Exhibit 101 hereto are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, are deemed not filed for purposes of Section 18 of the Securities and Exchange Act of 1934, as amended, and otherwise are not subject to liability under those sections.