HORIZON BANCORP /IN/
Form 10-Q
August 08, 2012
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HORIZON BANCORP

FORM 10-Q

United States

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

QUARTERLY REPORT UNDER SECTION 13 OR 15 (d) OF

THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2012

Commission file number 0-10792

HORIZON BANCORP

(Exact name of registrant as specified in its charter)

Indiana	**35-1562417**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
515 Franklin Square, Michigan City, Indiana	**46360**
(Address of principal executive offices)	**(Zip Code)**

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

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x 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 x 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	x
Non-accelerated Filer	¨ Do not check if 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 x

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date: 5,790,327 shares of Common Stock, no par value, at August 8, 2012.

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PART 1 FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

HORIZON BANCORP AND SUBSIDIARIES

Condensed Consolidated Balance Sheets

(Dollar Amounts in Thousands)

	June 30 2012 (Unaudited)	December 31 2011
Assets		
Cash and due from banks	$ 23,743	$ 20,447
Investment securities, available for sale	435,615	431,045
Investment securities, held to maturity	6,100	7,100
Loans held for sale	9,300	14,090
Loans, net of allowance for loan losses of $18,374 and $18,882	978,765	964,311
Premises and equipment	35,980	34,665
Federal Reserve and Federal Home Loan Bank stock	12,390	12,390
Goodwill	5,910	5,910
Other intangible assets	2,072	2,292
Interest receivable	6,685	6,671
Cash value life insurance	30,649	30,190
Other assets	16,056	18,051
Total assets	$ 1,563,265	$ 1,547,162
Liabilities		
Deposits		
Non-interest bearing	$ 136,979	$ 130,673
Interest bearing	908,810	879,192
Total deposits	1,045,789	1,009,865
Borrowings	339,880	370,111
Subordinated debentures	30,722	30,676
Interest payable	911	596
Other liabilities	15,351	14,449
Total liabilities	1,432,653	1,425,697
Commitments and contingent liabilities Stockholders Equity		
Preferred stock, $.01 par value, $1,000 liquidation value Authorized, 1,000,000 Series B shares Issued 12,500 and 12,500 shares	12,500	12,500
Common stock, $.3333 stated value Authorized, 22,500,000 shares Issued, 5,002,517 and 4,967,196 shares Outstanding, 4,957,347 and 4,947,696 shares	1,135	1,126
Additional paid-in capital	10,853	10,610
Retained earnings	97,349	89,387
Accumulated other comprehensive income	8,775	7,842
Total stockholders equity	130,612	121,465

Total liabilities and stockholders equity	**$ 1,563,265**	$ 1,547,162

See notes to condensed consolidated financial statements

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HORIZON BANCORP AND SUBSIDIARIES

Condensed Consolidated Statements of Income

(Dollar Amounts in Thousands, Except Per Share Data)

	Three Months Ended June 30		Six Months Ended June 30	
	2012 (Unaudited)	2011 (Unaudited)	2012 (Unaudited)	2011 (Unaudited)
Interest Income				
Loans receivable	**$ 13,327**	$ 11,891	**$ 26,859**	$ 23,779
Investment securities				
Taxable	**2,246**	2,786	**4,560**	5,286
Tax exempt	**950**	1,035	**1,930**	2,078
Total interest income	**16,523**	15,712	**33,349**	31,143
Interest Expense				
Deposits	**1,526**	2,195	**3,165**	4,532
Borrowed funds	**1,519**	1,600	**3,038**	3,177
Subordinated debentures	**472**	454	**942**	904
Total interest expense	**3,517**	4,249	**7,145**	8,613
Net Interest Income	**13,006**	11,463	**26,204**	22,530
Provision for loan losses	**209**	1,332	**768**	2,880
Net Interest Income after Provision for Loan Losses	**12,797**	10,131	**25,436**	19,650
Other Income				
Service charges on deposit accounts	**763**	825	**1,475**	1,620
Wire transfer fees	**213**	137	**395**	245
Interchange fees	**714**	639	**1,342**	1,184
Fiduciary activities	**982**	932	**1,957**	1,895
Gain on sale of securities		365		639
Gain on sale of mortgage loans	**3,411**	1,308	**5,685**	1,841
Mortgage servicing income net of impairment	**170**	99	**260**	863
Increase in cash value of bank owned life insurance	**235**	211	**460**	416
Other income	**67**	(68)	**123**	59
Total other income	**6,555**	4,448	**11,697**	8,762
Other Expenses				
Salaries and employee benefits	**6,539**	5,470	**12,502**	10,831
Net occupancy expenses	**976**	1,039	**2,030**	2,120
Data processing	**603**	494	**1,129**	901
Professional fees	**583**	331	**1,117**	680
Outside services and consultants	**526**	386	**997**	767
Loan expense	**866**	694	**1,568**	1,456
FDIC insurance expense	**250**	303	**507**	690
Other losses	**162**	246	**192**	277
Other expenses	**1,675**	1,524	**3,298**	3,023

Total other expenses	**12,180**	10,487	**23,340**	20,745
Income Before Income Tax	**7,172**	4,092	**13,793**	7,667
Income tax expense	**2,262**	999	**4,270**	1,809
Net Income	**4,910**	3,093	**9,523**	5,858
Preferred stock dividend and discount accretion	**(106)**	(277)	**(263)**	(553)
Net Income Available to Common Shareholders	**$ 4,804**	$ 2,816	**$ 9,260**	$ 5,305
Basic Earnings Per Share	**$ 0.97**	$ 0.57	**$ 1.87**	$ 1.08
Diluted Earnings Per Share	**0.93**	0.56	**1.81**	1.05

See notes to condensed consolidated financial statements

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HORIZON BANCORP AND SUBSIDIARIES

Condensed Consolidated Statements of Comprehensive Income

(Dollar Amounts in Thousands)

	Three Months Ended June 30		Six Months Ended June 30	
	2012 (Unaudited)	**2011 (Unaudited)**	**2012 (Unaudited)**	**2011 (Unaudited)**
Net Income	**$ 4,910**	$ 3,093	**$ 9,523**	$ 5,858
Other Comprehensive Income				
Change in fair value of derivative instruments, net of taxes of $(423) and $(226) for three and six months ended 2012 and $2,006 and $2,772, for three and six months ended 2011, respectively	**(785)**	3,725	**(419)**	5,148
Unrealized appreciation (depreciation) on available-for-sale securities, net of taxes of $424 and $728, for three and six months ended 2012 and $(201) and $53 for the three and six months ended 2011, respectively	**787**	(373)	**1,352**	98
Less: reclassification adjustment for realized gains included in net income, net of taxes of $0 for three and six months ended 2012, and $128 and $224, for three and six months ended 2011, respectively		237		415
	2	3,115	**933**	4,831
Comprehensive Income	**$ 4,912**	$ 6,208	**$ 10,456**	$ 10,689

See notes to condensed consolidated financial statements

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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	Retained Earnings	Accumulated Other Comprehensive Income	Total
Balances, January 1, 2012	**$ 12,500**	**$ 1,126**	**$ 10,610**	**$ 89,387**	**$ 7,842**	**$ 121,465**
Net income				9,523		9,523
Other comprehensive income, net of tax					933	933
Amortization of unearned compensation			69			69
Issuance of restricted shares		8	108			116
Exercise of stock options		1	49			50
Stock option expense			17			17
Cash dividends on preferred stock				(263)		(263)
Cash dividends on common stock ($.26 per share)				(1,298)		(1,298)
Balances, June 30, 2012	**$ 12,500**	**$ 1,135**	**$ 10,853**	**$ 97,349**	**$ 8,775**	**$ 130,612**

See notes to condensed consolidated financial statements

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HORIZON BANCORP AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows

(Dollar Amounts in Thousands)

	Six Months Ended June 30 2012 (Unaudited)	2011 (Unaudited)
Operating Activities		
Net income	**$ 9,523**	$ 5,858
Items not requiring (providing) cash		
Provision for loan losses	**768**	2,880
Depreciation and amortization	**1,298**	1,227
Share based compensation	**17**	20
Mortgage servicing rights impairment (recovery)	**(64)**	(728)
Premium amortization on securities available for sale, net	**1,410**	1,026
Gain on sale of investment securities		(639)
Gain on sale of mortgage loans	**(5,685)**	(1,841)
Proceeds from sales of loans	**184,317**	109,902
Loans originated for sale	**(178,632)**	(108,061)
Change in cash value of life insurance	**(459)**	(416)
(Gain) loss on sale of other real estate owned	**26**	86
Net change in		
Interest receivable	**(14)**	(259)
Interest payable	**315**	(76)
Other assets	**(464)**	1,977
Other liabilities	**260**	(812)
Net cash provided by operating activities	**12,616**	10,144
Investing Activities		
Purchases of securities available for sale	**(54,618)**	(108,989)
Proceeds from sales, maturities, calls, and principal repayments of securities available for sale	**50,718**	49,049
Purchase of securities held to maturity		(2,437)
Proceeds from maturities of securities held to maturity	**1,000**	1,400
Net change in loans	**(11,431)**	50,962
Proceeds on the sale of OREO and repossessed assets	**2,991**	1,069
Purchases of premises and equipment	**(2,324)**	(13)
Net cash used in by investing activities	**(13,664)**	(7,685)
Financing Activities		
Net change in		
Deposits	**35,924**	34,778
Borrowings	**(30,185)**	(30,554)
Proceeds from issuance of stock	**166**	55
Tax benefit from issuance of stock		8
Dividends paid on common shares	**(1,298)**	(1,128)
Dividends paid on preferred shares	**(263)**	(469)
Net cash provided by financing activities	**4,344**	2,690
Net Change in Cash and Cash Equivalent	**3,296**	5,149

Cash and Cash Equivalents, Beginning of Period	**20,447**	15,683
Cash and Cash Equivalents, End of Period	**$ 23,743**	$ 20,832
Additional Cash Flows Information		
Interest paid	**$ 6,829**	$ 8,689
Income taxes paid	**3,925**	100
Transfer of loans to other real estate owned	**1,224**	3,717

See notes to condensed consolidated financial statements

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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 June 30, 2012 and June 30, 2011 are not necessarily indicative of the operating results for the full year of 2012 or 2011. 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 2011 filed with the Securities and Exchange Commission on March 12, 2012. The consolidated condensed balance sheet of Horizon as of December 31, 2011 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 December 31 June 30		Six months ended June 30	
	2012 (Unaudited)	2011 (Unaudited)	2012 (Unaudited)	2011 (Unaudited)
Basic earnings per share				
Net income	**$ 4,910**	$ 3,093	**$ 9,523**	$ 5,858
Less: Preferred stock dividends and accretion of discount	**106**	277	**263**	553
Net income available to common shareholders	**$ 4,804**	$ 2,816	**$ 9,260**	$ 5,305
Weighted average common shares outstanding(1)	**4,956,358**	4,937,750	**4,952,466**	4,930,887
Basic earnings per share	**$ 0.97**	$ 0.57	**$ 1.87**	$ 1.08
Diluted earnings per share				
Net income available to common shareholders	**$ 4,804**	$ 2,816	**$ 9,260**	$ 5,305
Weighted average common shares outstanding(1)	**4,956,358**	4,937,750	**4,952,466**	4,930,887
Effect of dilutive securities:				
Warrants	**159,008**	110,509	**136,513**	113,219
Restricted stock	**17,582**	7,139	**12,374**	14,709
Stock options	**19,398**	10,056	**14,829**	10,373
Weighted average shares outstanding	**5,152,346**	5,065,454	**5,116,182**	5,069,188
Diluted earnings per share	**$ 0.93**	$ 0.56	**$ 1.81**	$ 1.05

(1) Adjusted for 3:2 stock split on December 9, 2011

HORIZON BANCORP AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

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

At June 30, 2012 and 2011, there were 8,500 shares and 51,176 shares, respectively that were not included in the computation of diluted earnings per share because they were non-dilutive.

Horizon has share-based employee compensation plans, which are described in the notes to the financial statements included in the December 31, 2011 Annual Report on Form 10-K.

Reclassifications

Certain reclassifications have been made to the 2011 consolidated financial statements to be comparable to 2012. These reclassifications had no effect on net income.

Note 2 Securities

The fair value of securities is as follows:

June 30, 2012	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**
Available for sale				
U.S. Treasury and federal agencies	$ 16,889	$ 327	$	$ 17,216
State and municipal	131,305	9,990	(70)	141,225
Federal agency collateralized mortgage obligations	92,554	1,886	(82)	94,358
Federal agency mortgage-backed pools	172,991	6,913	(20)	179,884
Private labeled mortgage-backed pools	2,786	106		2,892
Corporate notes	32	8		40
Total available for sale investment securities	$ 416,557	$ 19,230	$ (172)	$ 435,615
Held to maturity, State and Municipal	$ 6,100	$	$	$ 6,100

December 31, 2011	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**
Available for sale				
U.S. Treasury and federal agencies	$ 12,693	$ 329	$	$ 13,022
State and municipal	135,011	8,950	(71)	143,890
Federal agency collateralized mortgage obligations	89,016	2,106		91,122
Federal agency mortgage-backed pools	173,797	5,669	(115)	179,351
Private labeled mortgage-backed pools	3,518	118		3,636
Corporate notes	32		(8)	24

Total available for sale investment securities	$ 414,067	$ 17,172	$ (194)	$ 431,045
Held to maturity, State and Municipal	$ 7,100	$ 34	$	$ 7,134

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 June 30, 2012, no individual investment security had an unrealized loss that was determined to be other-than-temporary.

The unrealized losses on the Company s investments in securities of state and municipal 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

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HORIZON BANCORP AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

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

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 June 30, 2012.

The amortized cost and fair value of securities available for sale and held to maturity at June 30, 2012 and December 31, 2011, 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.

	June 30, 2012		December 31, 2011	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Available for sale				
Within one year	$ 1,141	$ 1,147	$ 931	$ 940
One to five years	28,475	29,658	30,796	31,910
Five to ten years	60,633	65,160	51,476	55,053
After ten years	57,977	62,516	64,533	69,033
	148,226	158,481	147,736	156,936
Federal agency collateralized mortgage obligations	92,554	94,358	89,016	91,122
Federal agency mortgage-backed pools	172,991	179,884	173,797	179,351
Private labeled mortgage-backed pools	2,786	2,892	3,518	3,636
Total available for sale investment securities	$ 416,557	$ 435,615	$ 414,067	$ 431,045
Held to maturity				
Within one year	$ 6,100	$ 6,100	$ 7,100	$ 7,134
One to five years				
Total held to maturity investment securities	$ 6,100	$ 6,100	$ 7,100	$ 7,134

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	
June 30, 2012	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
State and municipal	$ 3,393	$ (70)	$	$	$ 3,393	$ (70)
Federal agency collateralized mortgage obligations	13,674	(82)			13,674	(82)
Federal agency mortgage-backed pools	3,176	(20)			3,176	(20)

Total temporarily impaired securities	$ 20,243	$ (172)	$	$	$ 20,243	$ (172)

	Less than 12 Months		12 Months or More		Total	
December 31, 2011	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**
State and municipal	$ 1,550	$ (44)	$ 1,948	$ (27)	$ 3,498	$ (71)
Federal agency mortgage-backed pools	23,442	(115)	23		23,465	(115)
Corporate notes	24	(8)			24	(8)
Total temporarily impaired securities	$ 25,016	$ (167)	$ 1,971	$ (27)	$ 26,987	$ (194)

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HORIZON BANCORP AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

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

	Three months ended June 30		Six months ended June 30	
	2012	**2011**	**2012**	**2011**
Sales of securities available for sale (Unaudited)				
Proceeds	$	$ 8,116	$	$ 17,390
Gross gains		365		639
Gross losses				

Note 3 Loans

	June 30 2012	December 31 2011
Commercial		
Working capital and equipment	**$ 166,300**	$ 170,325
Real estate, including agriculture	**180,371**	172,910
Tax exempt	**3,587**	3,818
Other	**6,291**	5,323
Total	**356,549**	352,376
Real estate		
1 4 family	**152,953**	153,039
Other	**3,722**	4,102
Total	**156,675**	157,141
Consumer		
Auto	**138,006**	134,686
Recreation	**4,766**	4,737
Real estate/home improvement	**28,580**	27,729
Home equity	**91,128**	92,249
Unsecured	**3,209**	3,183
Other	**2,748**	2,793
Total	**268,437**	265,377
Mortgage warehouse	**215,478**	208,299
Total	**215,478**	208,299
Total loans	**997,139**	983,193
Allowance for loan losses	**(18,374)**	(18,882)
Loans, net	**$ 978,765**	$ 964,311

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, 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

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HORIZON BANCORP AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

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

business conducted on the property securing the loan. Commercial real estate loans may be more adversely 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 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 pay off 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, which 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 purchase 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.

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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.

June 30, 2012	Loan Balance	Interest Due	Deferred Fees / (Costs)	Recorded Investment
Owner occupied real estate	$ 133,700	$ 412	$ 22	$ 134,134
Non owner occupied real estate	152,707	399	95	153,201
Residential spec homes	4,038	5		4,043
Development & spec land loans	7,064	20		7,084
Commercial and industrial	58,920	185	3	59,108
Total commercial	356,429	1,021	120	357,570
Residential mortgage	147,916	529	84	148,529
Residential construction	8,675	13		8,688
Mortgage warehouse	215,478	427		215,905
Total real estate	372,069	969	84	373,122
Direct installment	25,526	82	(368)	25,240
Direct installment purchased	587			587
Indirect installment	130,928	381	(201)	131,108
Home equity	112,726	541	(761)	112,506
Total consumer	269,767	1,004	(1,330)	269,441
Total loans	998,265	2,994	(1,126)	1,000,133
Allowance for loan losses	(18,374)			(18,374)
Net loans	$ 979,891	$ 2,994	$ (1,126)	$ 981,759

December 31, 2011	Loan Balance	Interest Due	Deferred Fees / (Costs)	Recorded Investment
Owner occupied real estate	$ 131,893	$ 383	$ 30	$ 132,306
Non owner occupied real estate	142,269	360	94	142,723
Residential spec homes	3,574	6		3,580
Development & spec land loans	8,739	16		8,755
Commercial and industrial	65,774	169	3	65,946
Total commercial	352,249	934	127	353,310
Residential mortgage	150,893	513	68	151,474
Residential construction	6,181	8		6,189
Mortgage warehouse	208,299	427		208,726
Total real estate	365,373	948	68	366,389

Direct installment	24,252	94	(360)	23,986
Direct installment purchased	981			981
Indirect installment	127,751	420	(56)	128,115
Home equity	113,561	559	(752)	113,368
Total consumer	266,545	1,073	(1,168)	266,450
Total loans	984,167	2,955	(973)	986,149
Allowance for loan losses	(18,882)			(18,882)
Net loans	$ 965,285	$ 2,955	$ (973)	$ 967,267

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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. The actual allowance for loan loss activity is provided below.

	Three Months Ended		Six Months Ended	
	June 30 2012 (Unaudited)	June 30 2011 (Unaudited)	June 30 2012 (Unaudited)	June 30 2011 (Unaudited)
Balance at beginning of the period	$ 19,412	$ 19,090	$ 18,882	$ 19,064
Loans charged-off:				
Commercial				
Owner occupied real estate	3	113	3	124
Non owner occupied real estate	28	114	28	114
Residential development				
Development & Spec Land Loans				
Commercial and industrial	327	160	327	210
Total commercial	358	387	358	448
Real estate				
Residential mortgage	115	669	204	751
Residential construction				
Mortgage warehouse				
Total real estate	115	669	204	751
Consumer				
Direct Installment	58	217	171	402
Direct Installment Purchased				
Indirect Installment	271	331	609	786
Home Equity	754	552	887	1,529
Total consumer	1,083	1,100	1,667	2,717
Total loans charged-off	1,556	2,156	2,229	3,916
Recoveries of loans previously charged-off:				
Commercial				
Owner occupied real estate	52	18	352	18
Non owner occupied real estate			7	
Residential development				
Development & Spec Land Loans				
Commercial and industrial	28	3	53	5

Total commercial	80	21	412	23
Real estate				
Residential mortgage	2	10	32	10
Residential construction				
Mortgage warehouse				
Total real estate	2	10	32	10
Consumer				
Direct Installment	20	19	35	67
Direct Installment Purchased				
Indirect Installment	189	220	390	389
Home Equity	18	50	84	69
Total consumer	227	289	509	525
Total loan recoveries	309	320	953	558
Net loans charged-off	1,247	1,836	1,276	3,358
Provision charged to operating expense				
Commercial	(391)	(1,165)	(305)	(51)
Real estate	35	106	646	153
Consumer	565	2,391	427	2,778
Total provision charged to operating expense	209	1,332	768	2,880
Balance at the end of the period	$ 18,374	$ 18,586	$ 18,374	$ 18,586

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Certain loans are individually evaluated for impairment, and the Company s general practice is to proactively charge down impaired loans 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 or specific allocation of 1-4 family first and junior lien mortgages to the net realizable value less costs to sell when the value is known but no later than when a loan is 180 days past due. Pursuant to such guidelines, the Company also charges-off unsecured open-end loans when the loan is 90 days past due, and charges down to the net realizable value other secured loans when they 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 are not 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:

June 30, 2012	**Commercial**	**Real Estate**	**Mortgage Warehousing**	**Consumer**	**Total**
Allowance For Loan Losses					
Ending allowance balance attributable to loans:					
Individually evaluated for impairment	$ 2,463	$	$	$	$ 2,463
Collectively evaluated for impairment	5,303	2,946	1,695	5,967	15,911
Total ending allowance balance	$ 7,766	$ 2,946	$ 1,695	$ 5,967	$ 18,374
Loans:					
Individually evaluated for impairment	$ 8,796	$	$	$	$ 8,796
Collectively evaluated for impairment	348,774	157,217	215,905	269,441	991,337
Total ending loans balance	$ 357,570	$ 157,217	$ 215,905	$ 269,441	$ 1,000,133

December 31, 2011	**Commercial**	**Real Estate**	**Mortgage Warehousing**	**Consumer**	**Total**
Allowance For Loan Losses					
Ending allowance balance attributable to loans:					

Individually evaluated for impairment	$ 2,136	$	$	$	$ 2,136
Collectively evaluated for impairment	5,881	2,472	1,695	6,698	16,746
Total ending allowance balance	$ 8,017	$ 2,472	$ 1,695	$ 6,698	$ 18,882
Loans:					
Individually evaluated for impairment	$ 7,960	$	$	$	$ 7,960
Collectively evaluated for impairment	345,350	157,663	208,726	266,450	978,189
Total ending loans balance	$ 353,310	$ 157,663	$ 208,726	$ 266,450	$ 986,149

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Note 5 Non-performing Loans and Impaired Loans

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

June 30, 2012	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	$ 2,956	$	$	$	$ 2,956
Non owner occupied real estate	3,982		123		4,105
Residential development					
Development & Spec Land Loans	675				675
Commercial and industrial	194		867		1,061
Total commercial	7,807		990		8,797
Real estate					
Residential mortgage	4,624.00		1,720	1,958	8,302
Residential construction				292	292
Mortgage warehouse					
Total real estate	4,624		1,720	2,250	8,594
Consumer					
Direct Installment	103	7	24		134
Direct Installment Purchased					
Indirect Installment	772	6			778
Home Equity	1,619		52	842	2,513
Total Consumer	2,494	13	76	842	3,425
Total	$ 14,925	$ 13	$ 2,786	$ 3,092	$ 20,816

December 31, 2011	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	$ 2,515	$	$	$	$ 2,515
Non owner occupied real estate	3,970		152		4,122
Residential development					

Development & Spec Land Loans	90				90
Commercial and industrial	330		901		1,231
Total commercial	6,905		1,053		7,958
Real estate					
Residential mortgage	4,550		1,120	2,389	8,059
Residential construction	144			293	437
Mortgage warehouse					
Total real estate	4,694		1,120	2,682	8,496
Consumer					
Direct Installment	256	1			257
Direct Installment Purchased		4			4
Indirect Installment	926	29			955
Home Equity	1,587	3	25	858	2,473
Total Consumer	2,769	37	25	858	3,689
Total	$ 14,368	$ 37	$ 2,198	$ 3,540	$ 20,143

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

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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 the amount delinquent in excess of 90 days or the loan has had the accrual of interest discontinued by management. The officer responsible for the loan and the Chief Operating Officer or 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 in accordance with the loan terms. 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 for its collateral, 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 they are 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 TDR s, 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 TDR s are considered impaired loans and included in the allowance methodology using the guidance for impaired loans. At June 30, 2012, 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 June 30, 2012, the Company had $5.9 million in TDR s and $3.1 million were performing according to the restructured terms. The financial statement impact of non-performing TDR s was not material for the three and six months ending June 30, 2012. There was $273,000 of specific reserves allocated to TDR s at June 30, 2012 based on the collateral deficiencies.

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Loans classified as troubled debt restructuring during the six months ended June 30, 2012 and 2011, segregated by class, are shown in the table below.

	June 30, 2012		June 30, 2011	
	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				
Total commercial				
Real estate				
Residential mortgage	**1**	**332**	2	342
Residential construction				
Mortgage warehouse				
Total real estate	**1**	**332**	2	342
Consumer				
Direct Installment				
Direct Installment Purchased				
Indirect Installment				
Home Equity			1	9
Total Consumer			1	9
Total	**1**	**$ 332**	3	$ 351

Troubled debt restructured loans which had payment defaults during the six months ended June 30, 2012 and 2011, segregated by class, are shown in the table below. Default occurs when a loan is 90 days or more past due or has been transferred to nonaccrual.

	June 30, 2012		June 30, 2011	
	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						
Total commercial						
Real estate						
Residential mortgage	**2**		**410**	1		459
Residential construction				1		293
Mortgage warehouse						
Total real estate	**2**		**410**	2		752
Consumer						
Direct Installment						
Direct Installment Purchased						
Indirect Installment						
Home Equity						
Total Consumer						
Total	**2**	**$**	**410**	2	$	752

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The following table presents commercial loans individually evaluated for impairment by class of loan:

				Three Months Ending		Six Months Ending	
June 30, 2012	**Unpaid Principal Balance**	**Recorded Investment**	**Allowance For Loan Loss Allocated**	**Average Balance in Impaired Loans**	**Cash/Accrual Interest Income Recognized**	**Average Balance in Impaired Loans**	**Cash/Accrual Interest Income Recognized**
With no recorded allowance							
Commercial							
Owner occupied real estate	$ 1,350	$ 1,350	$	$ 1,403	$	$ 1,343	$ 2
Non owner occupied real estate	422	422		389	3	392	3
Residential development							
Development & Spec Land Loans	14	14		5	1	2	1
Commercial and industrial	257	257		365		312	5
Total commercial	2,043	2,043		2,162	3	2,049	11
With an allowance recorded							
Commercial							
Owner occupied real estate	1,606	1,606	475	1,161	17	1,127	18
Non owner occupied real estate	3,682	3,684	1,100	3,685		3,524	
Residential development							
Development & Spec Land Loans	661	661	615	676		455	6
Commercial and industrial	804	804	273	806		811	
Total commercial	6,753	6,755	2,463	6,328	17	5,917	24
Total	$ 8,796	$ 8,798	$ 2,463	$ 8,490	$ 20	$ 7,966	$ 35

				Three Months Ending		Six Months Ending	
June 30, 2011	**Unpaid Principal Balance**	**Recorded Investment**	**Allowance For Loan Loss Allocated**	**Average Balance in Impaired Loans**	**Cash/Accrual Interest Income Recognized**	**Average Balance in Impaired Loans**	**Cash/Accrual Interest Income Recognized**
With no recorded allowance							
Commercial							
Owner occupied real estate	$ 1,003	$ 1,006	$	$ 818	$ 1	$ 1,403	$ 1
Non owner occupied real estate	1,254	1,254		1,037	4	389	4
Residential development	16	16		16			
Development & Spec Land Loans	124	124		83		5	
Commercial and industrial	191	191		154		7,878	
Total commercial	2,588	2,591		2,107	5	9,675	5
With an allowance recorded							

Commercial							
Owner occupied real estate	1,538	1,537	585	1,141		1,161	18
Non owner occupied real estate	4,849	4,888	665	4,884		3,685	
Residential development							
Development & Spec Land Loans	250	250	125	250		676	6
Commercial and industrial	251	251	115	251	1	806	
Total commercial	6,888	6,926	1,490	6,526	1	6,328	24
Total	$ 9,476	$ 9,517	$ 1,490	$ 8,633	$ 6	$ 16,003	$ 29

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The following table presents the payment status by class of loan:

June 30, 2012	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	$ 72	$	$	$ 72	$ 133,628	$ 133,700
Non owner occupied real estate	34			34	152,673	152,707
Residential development					4,038	4,038
Development & Spec Land Loans					7,064	7,064
Commercial and industrial	294			294	58,626	58,920
Total commercial	400			400	356,029	356,429
Real estate						
Residential mortgage	1,092			1,092	146,824	147,916
Residential construction	292			292	8,383	8,675
Mortgage warehouse					215,478	215,478
Total real estate	1,384			1,384	370,685	372,069
Consumer						
Direct Installment	131	44	7	182	25,344	25,526
Direct Installment Purchased	8	2		10	577	587
Indirect Installment	1,113	90	6	1,209	129,719	130,928
Home Equity	576	25		601	112,125	112,726
Total consumer	1,828	161	13	2,002	267,765	269,767
Total	$ 3,612	$ 161	$ 13	$ 3,786	$ 994,479	$ 998,265

December 31, 2011	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	$ 89	$ 168	$	$ 257	$ 131,636	$ 131,893
Non owner occupied real estate	228			228	142,041	142,269
Residential development					3,574	3,574
Development & Spec Land Loans					8,739	8,739
Commercial and industrial	34	22		56	65,718	65,774
Total commercial	351	190		541	351,708	352,249
Real estate						
Residential mortgage	411			411	150,482	150,893

Residential construction					6,181	6,181
Mortgage warehouse					208,299	208,299
Total real estate	411			411	364,962	365,373
Consumer						
Direct Installment	164	22	1	187	24,065	24,252
Direct Installment Purchased	7	14	4	25	956	981
Indirect Installment	1,333	335	29	1,697	126,054	127,751
Home Equity	363	92	3	458	113,103	113,561
Total consumer	1,867	463	37	2,367	264,178	266,545
Total	$ 2,629	$ 653	$ 37	$ 3,319	$ 980,848	$ 984,167

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 being 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.

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).

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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.

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 meets with 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 are classified as 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.

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Risk Grade 3: Satisfactory (Pass)

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. 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.

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.

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.

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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.

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June 30, 2012	Pass	Special Mention	Substandard	Doubtful	Total
Commercial					
Owner occupied real estate	$ 118,396	$ 4,633	$ 10,671	$	$ 133,700
Non owner occupied real estate	130,034	15,443	7,230		152,707
Residential development	2,364	341	1,333		4,038
Development & Spec Land Loans	4,096	415	2,553		7,064
Commercial and industrial	55,924	1,166	1,830		58,920
Total commercial	310,814	21,998	23,617		356,429
Real estate					
Residential mortgage	139,614		8,302		147,916
Residential construction	8,383		292		8,675
Mortgage warehouse	215,478				215,478
Total real estate	363,475		8,594		372,069
Consumer					
Direct Installment	25,392		134		25,526
Direct Installment Purchased	587				587
Indirect Installment	130,150		778		130,928
Home Equity	110,213		2,513		112,726
Total Consumer	266,342		3,425		269,767
Total	$ 940,630	$ 21,998	$ 35,636	$	$ 998,265

December 31, 2011	Pass	Special Mention	Substandard	Doubtful	Total
Commercial					
Owner occupied real estate	$ 107,155	$ 4,101	$ 20,637	$	$ 131,893
Non owner occupied real estate	118,446	11,423	12,400		142,269
Residential development	1,677	529	1,368		3,574
Development & Spec Land Loans	3,778	860	4,101		8,739
Commercial and industrial	55,964	3,012	6,798		65,774
Total commercial	287,020	19,925	45,304		352,249
Real estate					
Residential mortgage	142,834		8,059		150,893
Residential construction	5,744		437		6,181
Mortgage warehouse	208,299				208,299
Total real estate	356,877		8,496		365,373
Consumer					
Direct Installment	23,995		257		24,252
Direct Installment Purchased	977		4		981

Indirect Installment	126,796		955		127,751
Home Equity	111,088		2,473		113,561
Total Consumer	262,856		3,689		266,545
Total	$ 906,753	$ 19,925	$ 57,489	$	$ 984,167

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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 $30.5 million at June 30, 2012. 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 June 30, 2012, 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 June 30, 2012, 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 $63.5 million at June 30, 2012.

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 June 30, 2012, the Company s fair value of these derivatives was recorded and over the next 12 months, this activity 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.

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

	Asset Derivative June 30, 2012		Liability Derivatives June 30, 2012	
Derivatives designated as hedging instruments (Unaudited)	**Balance Sheet Location**	**Fair Value**	**Balance Sheet Location**	**Fair Value**
Interest rate contracts	Loans	$ 594	Other liabilities	$ 2,411
Interest rate contracts	Other Assets	1,817	Other liabilities	5,559
Total derivatives designated as hedging instruments		2,411		7,970
Derivatives not designated as hedging instruments				
Mortgage loan contracts	Other assets	942	Other liabilities	
Total derivatives not designated as hedging instruments		942		
Total derivatives		$ 3,353		$ 7,970

	Asset Derivative December 31, 2011		Liability Derivatives December 31, 2011	
Derivatives designated as hedging instruments (Unaudited)	**Balance Sheet Location**	**Fair Value**	**Balance Sheet Location**	**Fair Value**
Interest rate contracts	Loans	$ 754	Other liabilities	$ 2,187
Interest rate contracts	Other Assets	1,433	Other liabilities	4,914
Total derivatives designated as hedging instruments		2,187		7,101
Derivatives not designated as hedging instruments				
Mortgage loan contracts	Other assets	662	Other liabilities	
Total derivatives not designated as hedging instruments		662		
Total derivatives		$ 2,849		$ 7,101

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

Derivative in cash flow hedging relationship	Amount of Loss Recognized in Other Comprehensive Income on Derivative (Effective Portion) Three Months Ended June 30 2012 (Unaudited)	2011 (Unaudited)	Amount of Loss Recognized in Other Comprehensive Income on Derivative (Effective Portion) Six Months Ended June 30 2012 (Unaudited)	2011 (Unaudited)
Interest rate contracts	$ (785)	$ (611)	$ (418)	$ (318)

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.

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Derivative in fair value hedging relationship	**Location of gain (loss) recognized on derivative**	**Amount of Gain (Loss) Recognized on Derivative Three Months Ended June 30 2012 (Unaudited)**	**2011 (Unaudited)**	**Amount of Gain (Loss) Recognized on Derivative Six Months Ended June 30 2012 (Unaudited)**	**2011 (Unaudited)**
Interest rate contracts	Interest income -loans	$ 298	$ 351	$ 224	$ (59)
Interest rate contracts	Interest income -loans	(298)	(351)	(224)	59
Total		$	$	$	$

Derivative not designated as hedging relationship	**Location of gain (loss) recognized on derivative**	**Amount of Gain (Loss) Recognized on Derivative Three Months Ended June 30 2012 (Unaudited)**	**2011 (Unaudited)**	**Amount of Gain (Loss) Recognized on Derivative Six Months Ended June 30 2012 (Unaudited)**	**2011 (Unaudited)**
Mortgage contracts	Other income -gain on sale of loans	$ 503	$ 165	$ 280	$ 799

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. There have been no significant changes in the valuation techniques during the period ended June 30, 2012. For assets classified within Level 3 of the fair value hierarchy, the process used to develop the reported fair value is described below.

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

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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 2 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 including a yield curve, adjusted for liquidity and credit risk, contracted terms and discounted cash flow analysis, therefore, are classified within Level 2 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)
June 30, 2012				
Available-for-sale securities				
U.S. Treasury and federal agencies	$ 17,216	$	$ 17,216	$
State and municipal	141,225		141,225	
Federal agency collateralized mortgage obligations	94,358		94,358	
Federal agency mortgage-backed pools	179,884		179,884	
Private labeled mortgage-backed pools	2,892		2,892	
Corporate notes	40		40	
Total available-for-sale securities	435,615		435,615	
Hedged loans	65,921		65,921	
Forward sale commitments	942		942	
Interest rate swap agreements	(7,969)		(7,969)	
Commitments to originate loans				
December 31, 2011				
Available-for-sale securities				
U.S. Treasury and federal agencies	$ 13,022	$	$ 13,022	$
State and municipal	143,890		143,890	
Federal agency collateralized mortgage obligations	91,122		91,122	
Federal agency mortgage-backed pools	179,351		179,351	
Private labeled mortgage-backed pools	3,636		3,636	

Corporate notes	24		24	
Total available-for-sale securities	431,045		431,045	
Hedged loans	54,362			54,362
Forward sale commitments	662			662
Interest rate swap agreements	(7,102)			(7,101)
Commitments to originate loans				

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Transfers between Levels

Transfers between Levels 1, 2 and 3 and the reasons for those transfers are as follows:

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Reason for Transfer
Transfers to level:				
Hedged loans	$	$ 65,921	$	(a)
Forward sale commitments		942		(b)
Interest rate swap agreements		(7,969)		(a)
Commitments to originate loans				(b)
Total transfers to level	$	$ 58,894	$	

(a) - Valuation determined by widely accepted techniques including discounted cash flow analysis on expected cash flows of each derivative and observable market rate inputs such as yield curves and contractual terms on each instrument.
(b) - Valuation determined by quoted prices for similar loans in the secondary market with an expected fallout rate (interest rate locked pipeline loans not expected to close). Fallout rate is not considered a significant input to the fair value in its entirety.

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, 2011	$ 54,362	$ 662	$ (7,101)	$
Total realized and unrealized gains and losses				
Included in net income	(74)	(152)	74	(71)
Included in other comprehensive income, gross			563	
Purchases, issuances, and settlements	6,114			
Principal payments	(491)			
Transfers out to Level 2	(59,911)	(510)	6,464	71

Ending balance March 31, 2012	$	$	$	$

	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)

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

Non Interest Income	Three Months Ended June 30 2012 (Unaudited)	Three Months Ended June 30 2011 (Unaudited)	Six Months Ended June 30 2012 (Unaudited)	Six Months Ended June 30 2011 (Unaudited)
Total gains and losses from:				
Hedged loans	$ 298	$ 351	$ 224	$ (59)
Fair value interest rate swap agreements	(298)	(351)	(224)	59
Derivative loan commitments	503	165	280	(16)
	$ 503	$ 165	$ 280	$ (16)

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)
June 30, 2012				
Impaired loans	$ 6,333	$	$	$ 6,333
Mortgage servicing rights	4,720			4,720
December 31, 2011				
Impaired loans	$ 5,822	$	$	$ 5,822
Mortgage servicing rights	4,193			4,193

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 timely 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. Fair value adjustments on impaired loans were $2.5 million at June 30, 2012 and $2.1 million at December 31, 2011.

Mortgage Servicing Rights (MSRs): MSRs do not trade in an active market with readily observable prices. Accordingly, the fair value of these assets is classified as Level 3. The Company determines the fair value of MSRs using an income approach model based upon the Company s month-end interest rate curve and prepayment assumptions. The model utilizes assumptions to estimate future net servicing income cash flows, including estimates of time decay, payoffs and changes in valuation inputs and assumptions. The Company reviews the valuation assumptions against this market data for reasonableness and adjusts the assumptions if deemed appropriate.

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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 June 30, 2012 and December 31, 2011. 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.

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

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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 following table presents estimated fair values of the Company s financial instruments and the level within the fair value hierarchy in which the fair value measurements fall (unaudited).

	June 30, 2012			
	Carrying Amount	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets				
Cash and due from banks	$ 23,743	$ 23,743	$	$
Investment securities held to maturity	6,100		6,100	
Loans held for sale	9,300			9,300
Loans, net	978,765			1,002,105
Stock in FHLB and FRB	12,390		12,390	
Interest receivable	6,685		6,685	
Liabilities				
Non-interest bearing deposits	$ 136,979	$ 136,979	$	$
Interest-bearing deposits	908,810		908,836	
Borrowings	339,880		372,795	
Subordinated debentures	30,722		30,389	
Interest payable	911		911	

	December 31, 2011			
	Carrying Amount	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets				
Cash and due from banks	$ 20,447	$ 20,447	$	$
Investment securities held to maturity	7,100		7,134	
Loans held for sale	14,090			14,090
Loans, net	964,311			979,401
Stock in FHLB and FRB	12,390		12,390	
Interest receivable	6,671		6,671	
Liabilities				

Non-interest bearing deposits	$ 130,673	$ 130,673	$	$
Interest-bearing deposits	879,192		874,160	
Borrowings	370,111		398,789	
Subordinated debentures	30,676		30,083	
Interest payable	596		596	

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Note 9 Other Comprehensive Income

	Three Months Ended		Six Months Ended	
	June 30 2012 (Unaudited)	June 30 2011 (Unaudited)	June 30 2012 (Unaudited)	June 30 2011 (Unaudited)
Unrealized gains (losses) on securities:				
Unrealized holding gains arising during the period	$ 1,211	$ (574)	$ 2,080	$ 151
Less: reclassification adjustment for gains realized in net income		365		639
	1,211	(939)	2,080	(488)
Unrealized gain (loss) on derivative instruments	(1,208)	5,731	(645)	7,920
Net unrealized gains	3	4,792	1,435	7,432
Tax effect	(1)	(1,677)	(502)	(2,601)
Other comprehensive income	$ 2	$ 3,115	$ 933	$ 4,831

	June 30 2012	December 31 2011
Unrealized gain on securities available for sale	$ 19,058	$ 16,978
Unrealized gain (loss) on derivative instruments	(5,559)	(4,914)
Tax effect	(4,724)	(4,222)
Total accumulated other comprehensive income	$ 8,775	$ 7,842

Note 10 Future accounting matters

ASU No. 2011-03, Transfers and Servicing (Topic 860) Reconsideration of Effective Control for Repurchase Agreements. ASU 2011-03 is intended to improve financial reporting of repurchase agreements and other agreements that both entitle and obligate a transferor to repurchase or redeem financial assets before their maturity. ASU 2011-03 removes from the assessment of effective control (i) the criterion requiring the transferor to have the ability to repurchase or redeem the financial assets on substantially the agreed terms, even in the event of default by the transferee, and (ii) the collateral maintenance guidance related to that criterion. ASU 2011-03 became effective for the Company on January 1, 2012 and did not have a significant impact on the Company s financial statements.

ASU 2011-04, Fair Value Measurement (Topic 820) Amendments to Achieve Common Fair Value Measurements and Disclosure Requirements in U.S. GAAP and IFRSs. ASU 2011-04 amends Topic 820, Fair Value Measurements and Disclosures, to converge the fair value measurement guidance in U.S. generally accepted accounting principles and International Financial Reporting Standards. ASU 2011-04 clarifies the application of existing fair value measurement requirements, changes certain principles in Topic 820 and requires additional fair value disclosures. ASU 2011-04 became effective for the Company on January 1, 2012 and, aside from new disclosures included in Note 8 Fair Value of Financial Instruments, did not have a significant impact on the Company s financial statements.

ASU 2011-05, Comprehensive Income (Topic 220) Presentation of Comprehensive Income. ASU 2011-05 amends Topic 220, Comprehensive Income, to require that all non-owner changes in stockholders equity be presented in either a single continuous statement of comprehensive income or in two separate but consecutive statements. Additionally, ASU 2011-05 requires entities to present, on the face of the financial statements, reclassification adjustments for items that are reclassified from other comprehensive income to net income in the statement or statements where the components of net income and the components of other comprehensive income are presented. The option to present components of other comprehensive income as part of the statement of changes in stockholders equity was eliminated. ASU 2011-05 became effective for the Company on January 1, 2012; however, certain provisions related to the presentation of reclassification adjustments have been deferred by ASU 2011-12 Comprehensive Income (Topic 220) Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05, as further

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discussed below. In connection with the application of ASU 2011-05, the Company s financial statements now include separate statements of comprehensive income and additional footnote disclosures (see Note 9 Other Comprehensive Income).

ASU 2011-08, Intangibles Goodwill and Other (Topic 350) Testing Goodwill for Impairment. ASU 2011-08 amends Topic 350, Intangibles Goodwill and Other, to give entities the option to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If, after assessing the totality of events or circumstances, an entity determines it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then performing the two-step impairment test is unnecessary. However, if an entity concludes otherwise, then it is required to perform the first step of the two-step impairment test by calculating the fair value of the reporting unit and comparing the fair value with the carrying amount of the reporting unit. ASU 2011-08 became effective for the Company on January 1, 2012 and did not have a significant impact on the Company s financial statements.

ASU 2011-11, Balance Sheet (Topic 210) Disclosures about Offsetting Assets and Liabilities. ASU 2011-11 amends Topic 210, Balance Sheet, to require an entity to disclose both gross and net information about financial instruments, such as sales and repurchase agreements and reverse sale and repurchase agreements and securities borrowing/lending arrangements, and derivative instruments that are eligible for offset in the statement of financial position and/or subject to a master netting arrangement or similar agreement. ASU 2011-11 is effective for annual and interim periods beginning on January 1, 2013, and is not expected to have a significant impact on the Company s financial statements.

ASU 2011-12 Comprehensive Income (Topic 220) Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05. ASU 2011-12 defers changes in ASU No. 2011-05 that relate to the presentation of reclassification adjustments to allow the FASB time to redeliberate whether to require presentation of such adjustments on the face of the financial statements to show the effects of reclassifications out of accumulated other comprehensive income on the components of net income and other comprehensive income.

ASU 2011-12 allows entities to continue to report reclassifications out of accumulated other comprehensive income consistent with the presentation requirements in effect before ASU No. 2011-05. All other requirements in ASU No. 2011-05 are not affected by ASU No. 2011-12. ASU 2011-12 became effective for the Company on January 1, 2012 and did not have a significant impact on the Company s financial statements.

Note 11 Business Combination

On February 9, 2012, Horizon entered into an Agreement and Plan of Merger (the Merger Agreement) providing for Horizon s acquisition of Heartland Bancshares, Inc., an Indiana corporation (Heartland). Pursuant to the Merger Agreement, Heartland would merge with and into Horizon, with Horizon surviving the merger (the Merger), and Heartland Community Bank, an Indiana-chartered commercial bank and wholly owned subsidiary of Heartland, would merge with and into a wholly owned subsidiary of Horizon, Horizon Bank, N.A. (Horizon Bank), with Horizon Bank as the surviving bank.

On July 17, 2012 Horizon closed its acquisition of Heartland Bancshares, Inc. and Horizon Bank N.A. s acquisition of Heartland Community Bank, through mergers effective July 17, 2012. Under the final terms of the acquisition, the exchange ratio was 0.54 shares of Horizon s common stock for each share of Heartland common stock outstanding. Heartland shares outstanding at the closing were 1,442,449, and the shares of HBNC common stock issued to Heartland shareholders totaled 778,922. Horizon s stock price was $25.25 per share at the close of business on

July 17, 2012. Based upon these numbers, the total value of the consideration for the acquisition was $19,667,792.

As of March 31, 2012, Heartland Community Bank reported total assets of approximately $238.1 million, total deposits of approximately $211.2 million and total loans of approximately $134.9 million.

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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 connecti 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;

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;

- 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 Item 1A of Part I of our 2011 Annual Report on Form 10-K 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 and Central 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 and Central Indiana and Southwest Michigan, unemployment rates increased during 2009 and have remained elevated through the first six months of 2012. This rise in unemployment has been driven by multiple factors including slowdowns in commercial industries as well as a continued lower activity in the housing and construction industries. The Company s higher than historical levels of non-performing loans at June 30, 2012 and over the past two years can be attributed to the continued slow economy and continued high local unemployment, which have resulted in lower business revenues and increased bankruptcies. Despite these economic factors, Horizon continued to post record positive results through the first six months of 2012.

Following are some highlights of Horizon s financial performance through the second quarter of 2012:

- Second quarter 2012 net income was $4.9 million or $.93 diluted earnings per share, a 66% increase in diluted earnings per share compared to the same period in 2011. In addition, this represents the highest quarterly net income and diluted earnings per share in the Company s 139-year history.

- Horizon s net income for the first half of 2012 was $9.5 million or $1.81 diluted earnings per share, a 72% increase in diluted earnings per share compared to the same period in 2011 and the highest six-month net income in the Company s history.

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- Total loans increased $8.6 million during the quarter and $157.9 million over the previous twelve months to $997.1 million at June 30, 2012.

- Net interest income, after provisions for loan losses, for the first six months of 2012 was $25.4 million compared with $19.7 million for the same period in the prior year.

- The provision for loan losses decreased to $768,000 for the first six months of 2012 compared to $2.9 million for the same period in 2011.

- Net charge-offs for the first six months of 2012 were $1.3 million compared to $3.4 million for the same period in 2011.

- Total substandard loans have decreased by $21.9 million in the first six months of 2012.

- Return on average assets was 1.31% for the second quarter of 2012 and 1.27% for the first six months of 2012.

- Return on average common equity was 16.43% for the second quarter of 2012 and 16.13% for the first six months of 2012.

- The merger with Heartland Bancshares, Inc (Heartland) based in Franklin, Indiana closed on July 17, 2012.

- Horizon s tangible book value per share rose to $22.22 compared to $21.35 and $19.17 at March 31, 2012 and June 30, 2011, respectively.

- Horizon Bank s capital ratios, including Tier 1 Capital to total risk weighted assets of 12.03% as of June 30, 2012, 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 2011 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, mortgage servicing rights and hedge accounting, and valuation measurements 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 June 30, 2012, Horizon had core deposit intangibles of $2.1 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

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quality, cost effective banking services in a competitive marketplace. The goodwill value is supported by revenue that is in part driven by the volume of business transacted. A decrease in earnings resulting from a decline in the customer base or the inability to deliver cost effective services over sustained periods can lead to impairment of goodwill that could adversely affect earnings in future periods. FASB ASC 350-10 requires an annual evaluation of goodwill for impairment. The evaluation of goodwill for impairment requires the use of estimates and assumptions. Market price at the close of business on June 30, 2012 was $26.30 per share compared to a book value of $23.83 per common share. Horizon reported record earnings for the twelfth consecutive year in 2011, and the first six months of 2012 were the highest first six 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, particularly as it relates to community banks, and is not specific to Horizon.

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.

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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.

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Financial Condition

On June 30, 2012, Horizon s total assets were $1.6 billion, a slight increase compared to December 31, 2011.

Investment securities were comprised of the following as of:

	June 30, 2012		December 31, 2011	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Available for sale				
U.S. Treasury and federal agencies	$ 16,889	$ 17,216	$ 12,693	$ 13,022
State and municipal	131,305	141,225	135,011	143,890
Federal agency collateralized mortgage obligations	92,554	94,358	89,016	91,122
Federal agency mortgage-backed pools	172,991	179,884	173,797	179,351
Private labeled mortgage-backed pools	2,786	2,892	3,518	3,636
Corporate notes	32	40	32	24
Total available for sale investment securities	$ 416,557	$ 435,615	$ 414,067	$ 431,045
Held to maturity, State and Municipal	$ 6,100	$ 6,100	$ 7,100	$ 7,134

Investment securities increased by approximately $3.6 million compared to the end of 2011. This growth was the result of the Company deploying excess cash that was held during the first six months in cash and due from banks into investment securities.

Net loans increased $14.5 million since December 31, 2011. This increase was the result of an increase in commercial, consumer and mortgage warehouse loans of $4.2 million, $3.1 million and $7.2 million, respectively. These increases were partially offset by a decrease in real estate loans of $467,000. The increase in commercial and consumer 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. Mortgage warehouse loans increased as a result of market expansion and refinancing activity.

Other assets decreased $2.0 million during the six months of 2012 primarily due to a $1.8 million decrease in OREO.

Total deposits increased $35.9 million during the first six months of 2012. Non-interest bearing deposit accounts increased $6.3 million due to increased calling and marketing efforts, interest bearing deposit accounts increased $96.8 million primarily due to increased municipal deposits, and time deposits decreased $67.2 million due a decrease in brokered deposits and movement of funds from consumer certificates of deposits to interest bearing deposit accounts during the first six months of 2012.

The Company s borrowings decreased $30.2 million since December 31, 2011. At June 30, 2012, the Company had $133.0 million in short-term funds borrowed compared to $157.0 million at December 31, 2011. 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. In addition, the Company s current 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 $130.6 million at June 30, 2012 compared to $121.5 million at December 31, 2011. 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. At June 30, 2012, the ratio of average stockholders equity to average assets was 8.61% compared to 7.96% for December 31, 2011.

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Book value per common share at June 30, 2012 increased to $23.83 compared to $22.02 at December 31, 2011.

Results of Operations

Overview

Consolidated net income for the three-month period ended June 30, 2012 was $4.9 million, an increase of 58.8% from the $3.1 million for the same period in 2011. Earnings per common share for the three months ended June 30, 2012 increased to $0.97 basic and $0.93 diluted, compared to $0.57 basic and $0.56 diluted for the same three-month period in 2011. Dividends paid on preferred shares reduced diluted earnings per share by $0.02 and $0.05 per share for the three-month periods ended June 30, 2012 and 2011, respectively.

Consolidated net income for the six-month period ended June 30, 2012 was $9.5 million, an increase of 62.6% from the $5.9 million for the same period in 2011. Earnings per common share for the six months ended June 30, 2012 increased to $1.87 basic and $1.81 diluted, compared to $1.08 basic and $1.05 diluted for the same six-month period in 2011. Dividends paid on preferred shares reduced diluted earnings per share by $0.05 and $0.11 per share for the six-month periods ended June 30, 2012 and 2011, respectively.

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 cost of the Company s interest bearing liabilities more significantly than the reduction in the yields received on the Company s interest earning assets, resulting in an increase 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 June 30, 2012 was $13.0 million, an increase of $1.5 million over the $11.5 million earned during the same period in 2011. Yields on the Company s interest-earning assets decreased by 19 basis points to 4.79% from 4.98% for the three months ended June 30, 2012 and 2011, respectively. Interest income increased $811,000 from $15.7 million for the three months ended June 30, 2011 to $16.5 million for the same period in 2012. This increase was due to an increase in interest earning assets offset by the lower yield on new and repriced 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 $387.5 million of the Company s $522.3 million of adjustable rate loans.

Rates paid on interest-bearing liabilities decreased by 33 basis points for the three months ended June 30, 2012 compared to the same period in 2011 due to the lower interest rate environment. Interest expense decreased $732,000 from $4.2 million for the three-months ended June 30, 2011 to $3.5 million for the same period in 2012. This decrease was due to the lower rates being paid on the Company s interest bearing liabilities. Due to a more significant decrease in the rates paid on the Company s interest-bearing liabilities compared to the decrease in yields received on the Company s interest-earning assets the net interest margin increased 12 basis points from 3.67% for the three months ended June 30, 2011 to 3.79% for the same period in 2012.

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For the Three and Six Months Ended June 30, 2012

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

	Three Months Ended June 30, 2012			Three Months Ended June 30, 2011		
	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate
ASSETS						
Interest-earning assets						
Federal funds sold	$ 1,348	$ 1	0.30%	$ 14,529	$ 5	0.14%
Interest-earning deposits	1,908	1	0.21%	8,333	5	0.24%
Investment securities - taxable	349,118	2,244	2.59%	351,596	2,776	3.17%
Investment securities - non-taxable (1)	105,822	950	5.01%	112,279	1,035	5.28%
Loans receivable (2)(3)(4)	961,174	13,327	5.58%	814,581	11,891	5.86%
Total interest-earning assets (1)	1,419,370	16,523	4.79%	1,301,318	15,712	4.98%
Noninterest-earning assets						
Cash and due from banks	15,913			15,476		
Allowance for loan losses	(19,295)			(19,089)		
Other assets	95,472			96,056		
	$ 1,511,460			$ 1,393,761		
LIABILITIES AND SHAREHOLDERS EQUITY						
Interest-bearing liabilities						
Interest-bearing deposits	$ 924,464	$ 1,526	0.66%	$ 893,836	$ 2,195	0.98%
Borrowings	278,357	1,519	2.19%	224,864	1,600	2.85%
Subordinated debentures	31,446	472	6.04%	31,446	454	5.79%
Total interest-bearing liabilities	1,234,267	3,517	1.15%	1,150,146	4,249	1.48%
Noninterest-bearing liabilities						
Demand deposits	133,848			115,659		
Accrued interest payable and other liabilities	13,269			9,297		
Shareholders equity	130,076			118,659		
	$ 1,511,460			$ 1,393,761		
Net interest income/spread		$ 13,006	3.64%		$ 11,463	3.50%
Net interest income as a percent of average interest earning assets (1)			3.79%			3.67%

(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 rate 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.
(3) Non-accruing loans for the purpose of the computations above are included in the daily average loan amounts outstanding. Loan totals are shown net of unearned income and deferred loans fees.
(4) Loan fees and late fees included in interest on loans.

Net interest income during the six months ended June 30, 2012 was $26.2 million, an increase of $3.7 million over the $22.5 million earned during the same period in 2011. Yields on the Company s interest-earning assets decreased by 9 basis points to 4.86% for the six months ended June 30, 2012 from 4.95% for the same period in 2011. Interest income increased $2.2 million from $31.1 million for the six months ended June 30, 2011 to $33.3 million for the same period in 2012. This increase was due to an increase in interest earning assets offset partially by the reduction in the yield on interest earning assets.

Rates paid on interest-bearing liabilities decreased by 34 basis points for the six months ended June 30, 2012 compared to the same period in 2011 due to the lower interest rate environment. Interest expense decreased

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$1.5 million from $8.6 million for the six-months ended June 30, 2011 to $7.1 million for the same period in 2012. 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 rates paid on the Company s interest-bearing liabilities compared to the decrease in yields received on the Company s interest-earning assets the net interest margin increased 22 basis points from 3.62% for the six months ended June 30, 2011 to 3.84% for the same period in 2012.

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

	Six Months Ended June 30, 2012			Six Months Ended June 30, 2011		
	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate
ASSETS						
Interest-earning assets						
Federal funds sold	$ 3,340	$ 4	0.24%	$ 38,740	$ 44	0.23%
Interest-earning deposits	2,159	2	0.19%	5,771	6	0.21%
Investment securities - taxable	346,645	4,554	2.64%	326,790	5,236	3.23%
Investment securities - non-taxable (1)(2)	106,857	1,930	5.19%	113,281	2,078	5.07%
Loans receivable (2)(3)(4)	956,701	26,859	5.65%	817,468	23,779	5.88%
Total interest-earning assets (1)	1,415,702	33,349	4.86%	1,302,050	31,143	4.95%
Noninterest-earning assets						
Cash and due from banks	15,849			15,039		
Allowance for loan losses	(19,355)			(19,077)		
Other assets	95,986			96,513		
	$ 1,508,182			$ 1,394,525		
LIABILITIES AND SHAREHOLDERS' EQUITY						
Interest-bearing liabilities						
Interest-bearing deposits	$ 916,889	$ 3,165	0.69%	$ 898,635	$ 4,532	1.02%
Borrowings	285,981	3,038	2.14%	226,161	3,177	2.83%
Subordinated debentures	31,446	942	6.02%	31,446	904	5.80%
Total interest-bearing liabilities	1,234,316	7,145	1.16%	1,156,242	8,613	1.50%
Noninterest-bearing liabilities						
Demand deposits	132,813			112,618		
Accrued interest payable and other liabilities	13,387			9,390		
Shareholders' equity	127,666			116,275		
	$ 1,508,182			$ 1,394,525		

Net interest income/spread	$ 26,204	3.69%	$ 22,530	3.45%
Net interest income as a percent of average interest earning assets (1)		3.84%		3.62%

(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 rate 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.

(3) Non-accruing loans for the purpose of the computations above are included in the daily average loan amounts outstanding. Loan totals are shown net of unearned income and deferred loans fees.

(4) Loan fees and late fees included in interest on loans.

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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 second quarter of 2012, a provision for loan losses of $209,000 was required to adequately fund the ALLL compared to a provision of $1.3 million for the second quarter of 2011. The 2012 second quarter provision was the lowest since the fourth quarter of 2006. Commercial loan net charge-offs during the second quarter of 2012 were $278,000, residential mortgage loan net charge-offs were $113,000, and installment loans net charge-offs were $856,000. Due to the use of specific reserves for a portion of the charge offs during both the three months and six months ending June 30, 2012, the ALLL decreased. The ALLL balance at June 30, 2012 was $18.4 million or 1.83% of total loans. This compares to an ALLL balance of $18.9 million at December 31, 2011 or 1.89% of total loans and $18.6 million at June 30, 2011 or 2.20% of total loans.

For the six months ended June 30, 2012, the provision for loan losses totaled $768,000 compared to $2.9 million in the prior year for the same period. The commercial loans portfolio was at a net recovery position of $54,000 for the first six months of 2012, real estate loans had net charge-offs of $172,000, and installment loans had net charge-offs of $1.2 million.

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 June 30, 2012.

Non-performing loans totaled $20.8 million on June 30, 2012, down from $21.1 million on March 31, 2012, but up slightly from $20.6 million on June 30, 2011. As a percentage of total loans, non-performing loans were 2.09% on June 30, 2012, compared to 2.10% on March 31, 2012, but down from 2.44% on June 30, 2011. The drop in the percentage of non-performing loans to total loans is the direct result of the loan growth that occurred over the last twelve months.

Other Real Estate Owned (OREO) totaled $1.0 million on June 30, 2012, up from $803,000 on March 31, 2012, but down significantly from $4.1 million on June 30, 2011. During the quarter, eight properties with a book value of $435,000 as of March 31, 2011 were sold and seven properties with a book value of $696,000 were transferred into OREO. There was one write down of $29,000 during the quarter. On June 30, 2012, OREO was comprised of 10 properties. Of these, five totaling $599,000 were commercial loans and five totaling $427,000 were residential real estate loans. Horizon currently has contracts to sell two properties with a book value of $197,000.

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Other Income

The following is a summary of changes in other income:

	Three Months Ended June 30 2012	June 30 2011	Amount Change	Percent Change
Other income				
Service charges on deposit accounts	**$ 763**	$ 825	$ (62)	-7.5%
Wire transfer fees	**213**	137	76	55.5%
Interchange fees	**714**	639	75	11.7%
Fiduciary activities	**982**	932	50	5.4%
Gain on sale of securities		365	(365)	-100.0%
Gain on sale of mortgage loans	**3,411**	1,308	2,103	160.8%
Mortgage servicing net of impairment	**170**	99	71	71.7%
Increase in cash surrender value of bank owned life insurance	**235**	211	24	11.4%
Other income	**67**	(68)	135	198.5%
Total other income	**$ 6,555**	$ 4,448	$ 2,107	47.4%

Service charges on deposit accounts were $62,000 lower during the second quarter of 2012 compared to the same period in 2011 primarily due to the regulatory changes on overdraft fees. The residential mortgage loan activity during the second quarter of 2012 generated $3.4 million of income from the gain on sale of mortgage loans, up $2.1 million from the same period in 2011. This increase was primarily due to more favorable pricing on loans sold and additional volume. Loans originated for sale during the second quarter of 2012 were $98.3 million compared to $43.9 million for the same period in 2011.

	Six Months Ended June 30 2012	June 30 2011	Amount Change	Percent Change
Other income				
Service charges on deposit accounts	**$ 1,475**	$ 1,620	$ (145)	-9.0%
Wire transfer fees	**395**	245	150	61.2%
Interchange fees	**1,342**	1,184	158	13.3%
Fiduciary activities	**1,957**	1,895	62	3.3%
Gain on sale of securities		639	(639)	-100.0%
Gain on sale of mortgage loans	**5,685**	1,841	3,844	208.8%
Mortgage servicing net of impairment	**260**	863	(603)	-69.9%
Increase in cash surrender value of bank owned life insurance	**460**	416	44	10.6%
Other income	**123**	59	64	108.5%
Total other income	**$ 11,697**	$ 8,762	$ 2,935	33.5%

Service charges on deposit accounts were $145,000 lower during the first six months of 2012 compared to the same period in 2011 due to the regulatory changes on overdraft fees. Wire transfer fees and interchange fees increased $150,000 and $158,000, respectively, during the first half of 2012 compared to the same six-month period in 2011 due to increased activity. The residential mortgage loan activity during the first six months of 2012 generated $5.7 million of income from the gain on sale of mortgage loans, up $3.8 million from the same period in 2011. This increase was primarily due to more favorable pricing on loans sold and additional volume. Loans originated for sale during the first half of 2012 were $178.6 million compared to $108.1 million for the same period in 2011. In addition, Horizon recovered $728,000 of impairment on the Company s mortgage servicing asset and incurred a gain on the sale of securities of $639,000 during the first half of 2011 compared to $64,000 of impairment recovery and $0 gain on sales of securities for the same period in 2012.

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Other Expense

The following is a summary of changes in other expense:

	Three Months Ended			
	June 30 2012	June 30 2011	Amount Change	Percent Change
Other expense				
Salaries	**$ 4,206**	$ 3,786	$ 420	11.1%
Commission and bonuses	**1,120**	719	401	55.8%
Employee benefits	**1,213**	965	248	25.7%
Net occupancy expenses	**976**	1,039	(63)	-6.1%
Data processing	**603**	494	109	22.1%
Professional fees	**583**	331	252	76.1%
Outside services and consultants	**526**	386	140	36.3%
Loan expense	**866**	694	172	24.8%
FDIC deposit insurance	**250**	303	(53)	-17.5%
Other losses	**162**	246	(84)	-34.1%
Other expenses	**1,675**	1,524	151	9.9%
Total other expense	**$ 12,180**	$ 10,487	$ 1,693	16.1%

Total other expenses were $1.7 million higher in the second quarter of 2012 compared to the second quarter of 2011. Salaries, commissions and bonuses, and employee benefits increased $1.1 million compared to the same quarter in 2011. This increase is the result of annual merit pay increases, increase in staff and higher commission and bonus expense based on the second quarter performance for 2012. Included in the second quarter of 2012 s data processing, professional fees, outside services and consultants and other expenses was $332,000 of transaction costs related to the Heartland merger. The increase in loan expense during the second quarter of 2012 compared to the prior year was related to an increase in loan volume.

	Six Months Ended			
	June 30 2012	June 30 2011	Amount Change	Percent Change
Other expense				
Salaries	**$ 8,140**	$ 7,534	$ 606	8.0%
Commission and bonuses	**1,966**	1,216	750	61.7%
Employee benefits	**2,396**	2,081	315	15.1%
Net occupancy expenses	**2,030**	2,120	(90)	-4.2%
Data processing	**1,129**	901	228	25.3%
Professional fees	**1,117**	680	437	64.3%
Outside services and consultants	**997**	767	230	30.0%
Loan expense	**1,568**	1,456	112	7.7%
FDIC deposit insurance	**507**	690	(183)	-26.5%

Other losses	**192**	277	(85)	-30.7%
Other expenses	**3,298**	3,023	275	9.1%
Total other expense	**$ 23,340**	$ 20,745	$ 2,595	12.5%

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Total other expenses were $2.6 million higher in the first six months of 2012 compared to the same period in 2011. Salaries, commissions and bonuses, and employee benefits increased $1.7 million compared to the same period in 2011. This increase is the result of annual merit pay increases, increase in staff and higher commission and bonus expense based on the first six months of performance for 2012. Included in the first half of 2012 s data processing, professional fees, outside services and consultants and other expenses was $500,000 of transaction costs related to the Heartland merger. The increase in loan expense during the first half of 2012 compared to the prior year was related to an increase in loan volume. FDIC deposit insurance expense decreased during the first half of 2012 compared to 2011 as the assessment calculation has resulted in lower expense for the Company.

Income Taxes

Income tax expense for the second quarter of 2012 was $2.3 million compared to $999,000 of tax expense for the second quarter of 2011. The effective tax rate for the second quarter of 2012 was 31.5% compared to 24.4% in 2011. The increase in the effective tax rate is primarily due to higher income before income tax for the second quarter of 2012 compared to the same period in 2011 with a similar level of tax exempt income.

Income tax expense for the first half of 2012 was $4.3 million compared to $1.8 million of tax expense for the first half of 2011. The effective tax rate for the first half of 2012 was 31.0% compared to 23.6% in 2011. The increase in the effective tax rate is primarily due to higher income before income tax for the first half of 2012 compared to the same period in 2011 with a similar level of tax exempt income.

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 six months ended June 30, 2012, cash and cash equivalents increased by approximately $3.3 million. At June 30, 2012, in addition to liquidity available from the normal operating, funding, and investing activities of Horizon, the Bank had approximately $295.2 million in unused credit lines with various money center banks, including the FHLB and the FRB Discount Window compared to $288.7 million at December 31, 2011 and $304.6 million at June 30, 2011.

Capital Resources

The capital resources of Horizon and the Bank exceeded regulatory capital ratios for well capitalized banks at June 30, 2012. Stockholders equity totaled $130.6 million as of June 30, 2012, compared to $121.5 million as of December 31, 2011. At June 30, 2012, the ratio of average stockholders equity to average assets was 8.61% compared to 7.96% at December 31, 2011. Horizon s capital increased during the six months as a result of increased earnings and an increase in accumulated other comprehensive income, net of dividends declared and the amortization of unearned compensation.

The Company currently intends to continue its participation in the Small Business Lending Fund, pursuant to which it issued preferred stock to the US Treasury, since the growth in the Company s small business lending has reduced the dividend cost. For the three months ending June 30, 2012, the dividend cost was approximately $106,000, or 3.4% annualized. For the third quarter of 2012, the dividend cost will be approximately $62,500, or 2.0% annualized, and for the fourth quarter of 2012, the dividend cost will be approximately $208,000, or 5.0% annualized. The increase in the fourth quarter s dividend cost was due to the reduction of small business loans during the first quarter of 2012, the measurement period for the fourth quarter s dividend cost, primarily due to the Company s reduction in substandard loans which were small business loans. The Company plans to reserve cash for the ability to redeem this preferred stock if and when the cost of this capital exceeds other forms of capital.

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Horizon declared common stock dividends in the amount of $0.26 per share during the first six months of 2012 compared to $0.23 for the same period of 2011. The dividend payout ratio (dividends as a percent of basic earnings per share) was 13.9% and 21.1% for the first six months of 2012 and 2011, respectively. For additional information regarding dividend, see Horizon s Annual Report on Form 10-K for 2011.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Refer to Horizon s 2011 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 2011 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 June 30, 2012, 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 June 30, 2012, 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.

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Part II Other Information

For the Three and Six Months Ended June 30, 2012

ITEM 1. LEGAL PROCEEDINGS

Horizon and its subsidiaries are involved in various legal proceedings incidental to the conduct of their business. Management does not expect that the outcome of any such proceedings will have a material adverse effect on our consolidated financial position or results of operations.

ITEM 1A. RISK FACTORS

There have been no material changes from the factors previously disclosed under Item 1A of Horizon s Annual Report on Form 10-K for 2011.

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

Not Applicable

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not Applicable

ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable

ITEM 5. OTHER INFORMATION

Not Applicable

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ITEM 6. EXHIBITS
(a) Exhibits

Exhibit No.	Description
31.1	Certification of Craig M. Dwight
31.2	Certification of Mark E. Secor
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
101	Interactive Data Files*

* 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.

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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: August 8, 2012	/s/ Craig M. Dwight Craig M. Dwight Chief Executive Officer
Dated: August 8, 2012	/s/ Mark E. Secor Mark E. Secor Chief Financial Officer

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INDEX TO EXHIBITS

Exhibit No.	Description	Location
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 Files*	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.