LAKELAND FINANCIAL CORP
Form 10-K
March 08, 2010

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

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 or 15(d) of the
Securities Exchange Act of 1934

For the fiscal year ended December 31, 2009

Commission file number 0-11487

LAKELAND FINANCIAL CORPORATION

Indiana	35-1559596
(State of incorporation)	(I.R.S. Employer Identification No.)

202 East Center Street, P.O. Box 1387, Warsaw, Indiana 46581-1387
(Address of principal executive offices)

Telephone (574) 267-6144

Securities registered pursuant to Section 12(b) of the Act:

Common Stock, no par value	NASDAQ Global Select Market
(Title of class)	(Name of Each Exchange on which Registered)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes __No X

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes __No X

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 twelve months (or for such other 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 __ No __

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.[ ]

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of “accelerated filer and large accelerated filer” in Rule 12b-2 of the Exchange Act.

Large accelerated filer [ ]	Accelerated filer [X]	Non-accelerated filer [ ]	Smaller reporting company [ ]

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant, based on the last sales price quoted on the Nasdaq Global Select Market on June 30, 2009, the last business day of the registrant’s most recently completed second fiscal quarter, was approximately $219,686,892.

Number of shares of common stock outstanding at February 24, 2010: 16,096,861

DOCUMENTS INCORPORATED BY REFERENCE

Part III - Portions of the Proxy Statement for the Annual Meeting of Shareholders to be held on April 13, 2010 are incorporated by reference into Part III hereof.

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PART I

ITEM 1. BUSINESS

The Company was incorporated under the laws of the State of Indiana on February 8, 1983. As used herein, the term “Company” refers to Lakeland Financial Corporation, or if the context dictates, Lakeland Financial Corporation and its wholly-owned subsidiary, Lake City Bank (the “Bank”), an Indiana state bank headquartered in Warsaw, Indiana. Also included in the consolidated financial statements prior to December 27, 2006 is LCB Investments, Limited, a wholly-owned subsidiary of Lake City Bank, which was a Bermuda corporation that managed a portion of the Bank’s investment portfolio. On December 27, 2006, all securities were transferred to Lake City Bank from LCB Investments, Limited, and LCB Investments, Limited was dissolved. On December 18, 2006, LCB Investments II, Inc. was formed as a wholly-owned subsidiary of Lake City Bank incorporated in Nevada and it began managing a portion of the Bank’s investment portfolio in January 2007. On December 21, 2006, LCB Funding, Inc., a real estate investment trust, incorporated in Maryland, was formed as a wholly-owned subsidiary of LCB Investments II. All intercompany transactions and balances are eliminated in consolidation.

General

Company’s Business. The Company is a bank holding company as defined in the Bank Holding Company Act of 1956, as amended. The Company owns all of the outstanding stock of Lake City Bank, Warsaw, Indiana, a full-service commercial bank organized under Indiana law. The Bank recognizes a wholly-owned subsidiary, LCB Investments II, which manages a portion of the Bank’s investment portfolio. The Company conducts no business except that incident to its ownership of the outstanding stock of the Bank and the operation of the Bank.

The Bank’s deposits are insured by the Federal Deposit Insurance Corporation. The Bank’s activities cover all phases of commercial banking, including checking accounts, savings accounts, time deposits, the sale of securities under agreements to repurchase, commercial, real estate and agricultural lending, direct and indirect consumer lending, commercial and residential real estate mortgage lending, retail and merchant credit card services, corporate treasury management services, retirement services, bond administration, safe deposit box service and trust and brokerage services.

The Bank’s main banking office is located at 202 East Center Street, Warsaw, Indiana. As of December 31, 2009, the Bank had 43 offices in twelve counties throughout Northern Indiana, as well as a loan production office in Indianapolis.

Bank’s Business. The Bank was originally organized in 1872 and has continuously operated under the laws of the State of Indiana since its organization. The Bank’s business strategy is simply focused on maintaining our traditional community banking approach while concurrently leveraging the strength and size of our balance sheet to effectively compete with larger regional and national competitors. We are focused on serving clients in the state of Indiana, with the majority of our business in Northern Indiana. While our strategy encompasses all phases of traditional community banking, including consumer lending and wealth advisory and trust services, we focus on building expansive commercial relationships and developing retail and commercial deposit gathering strategies. Key components of our strategy include: relationship-based services and commercial focused client service. The interest rates for both deposits and loans, as well as the range of services provided, are consistent with those of most banks competing within the Bank’s service area.

The Bank competes for loans principally through a high degree of customer contact, timely loan review and approval, market-driven competitive loan pricing and the Bank’s reputation throughout the region. The Bank believes that its convenience, quality service and high-touch, responsive approach to banking enhances its ability to compete favorably in attracting and retaining individual and business customers. The Bank actively solicits deposit-related customers and competes for customers by offering personal attention, professional service and competitive interest rates.

Market Overview. While the Company operates in thirteen counties, it currently defines operations by four primary geographical markets. They are the South Region, which includes Kosciusko County and portions of contiguous counties; the North Region, which includes portions of Elkhart and St. Joseph Counties; the Central Region, which includes portions of Elkhart County and contiguous counties; and the East Region, which includes Allen and contiguous counties. The South Region includes the city of Warsaw, which is the location of the Company's headquarters. The Company has had a presence in this region since 1872. It has been in the North and Central Regions, which includes the cities of Elkhart, South Bend and Goshen, since 1990. The Company opened its first office in the East Region, which includes the cities of Fort Wayne and Auburn, in 1999. The Company also operates a loan production office in Indianapolis, which is staffed with commercial lending officers and was opened in 2006.

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The Company believes that these are well-established and fairly diverse economic regions. The Company has sought to diversify expansion and industry throughout its markets, which include a mix of industrial and service companies, with no business or industry concentrations within individual markets and combined. Furthermore, no single industry or employer dominates any of the markets. Fort Wayne represents the largest population center served by the Company's full-service branch system with a population of 206,000, according to 2000 U.S. Census Bureau data. South Bend, with a 2000 population of 108,000, is the second largest city served by the Company. Elkhart, with a 2000 population of 52,000, is the third largest city that the Company currently serves. As a result of the presence of offices in twelve counties that are widely dispersed, no single city or industry represents an undue concentration. In addition, the Indianapolis market represents a substantial future opportunity given its position as the largest metropolitan market in the state.

Expansion Strategy. The Company's expansion strategy is driven primarily by the potential for increased penetration in existing markets where opportunities for market share growth exists. Additionally, management considers growth in new markets with a close geographic proximity to its current operations. These markets are considered when the Company believes they would be receptive to its strategic plan to deliver broad-based financial services with a commitment to local communities. When entering new markets, the Company believes it is critical to attract experienced local management with a similar philosophy in order to provide a basis for success.

The Company is an Indiana institution serving Indiana clients. Since 1990, the Company has expanded from 17 offices in four Indiana counties to 43 branches in twelve Indiana counties and one loan production office. During this period, the Company has grown assets from $286 million to $2.6 billion today, an increase of 797%. Mergers and acquisitions have not played a substantive role in this growth as the Company's expansion strategy has been driven primarily by organic growth. Since the decision to expand outside of the four-county home market in 1990, the Company has targeted growth in larger cities located in the Northern Indiana market. In 1990, the Company began an expansion strategy that the Company believes has created a well-established presence in the region directly north of the Company's home market. This expansion was focused on the cities of Elkhart, South Bend and Goshen. In 1999, the Company expanded to the east and opened the first office in the Fort Wayne market. Most recently in 2006, the Company established a loan production office in Indianapolis.

While this overall expansion strategy has been guided by a focus on larger communities in Indiana, it has also been influenced by the competitive landscape in these markets. As the historically prominent community banks in these markets were acquired, in most cases by large out-of-state institutions, the Company believes that Lake City Bank's traditional community banking strategy became highly relevant and provides a competitive advantage to the Company.

The Company believes that another benefit of this geographic expansion strategy into larger population centers is that the Company now serves a more well-established and diverse economic region. While the Company operates within a relatively small geographic region of the state, the Company's expansion strategy has provided borrower diversification within a fairly diverse economic region. Further, the geographical diversification ensures that no single industry or employer dominates the Company's markets. In addition, the Indianapolis market represents a substantial future opportunity given its position as the largest metropolitan market in the state. Like previous market expansions, the Company believes the Indianapolis market will provide future business opportunities as the competitive landscape in the market changes to the Company's advantage.

The Company also considers opportunities beyond current markets when the Company's Board of Directors and management believes that the opportunity will provide a desirable strategic fit without posing undue risk. The Company does not currently have any definitive understandings or agreements for any acquisitions or de novo expansion.

Products and Services. The Company is a full-service commercial bank and provides commercial, retail, wealth advisory and investment management services to its customers. Commercial products include commercial loans and technology-driven solutions to commercial customers’ treasury management needs such as internet business banking and on-line treasury management services in addition to retirement services, bond administration and health savings account services. Retail banking clients are provided a wide array of traditional retail banking services, including lending, deposit and investment services. Retail lending programs are focused on mortgage loans, home equity lines of credit and traditional retail installment loans, including indirect automotive financing. The Company provides credit card services to retail and commercial customers through an outsourced retail card program and merchant processing activity. The Company also has an Honors Private Banking program that is positioned to serve the more financially sophisticated customer with a menu including investment management and trust services, executive mortgage programs and access to financial planning seminars and programs. The Company provides wealth advisory clients with traditional personal and corporate trust and investment services. The Company

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also provides retail brokerage services, including an array of financial and investment products such as annuities and life insurance.

Competition

The Bank competes with other local and regional banks in addition to major banks for large commercial deposit and loan accounts. The Bank is presently subject to an aggregate maximum loan limit to any single account pursuant to Indiana law of $42.5 million. The Bank currently enforces an internal limit of $20.0 million, which is less than the amount permitted by law. This maximum might occasionally limit the Bank from providing loans to those businesses or personal accounts whose borrowings periodically exceed this amount. In the event this were to occur, the Bank maintains correspondent relationships with other financial institutions. The Bank may participate with other banks in the placement of large borrowings in excess of its lending limit, although the Bank typically does not participate in such arrangements. The Bank is also a member of the Federal Home Loan Bank of Indianapolis in order to provide additional funding, as necessary, to support funding requests and to broaden its mortgage lending and investment activities

In addition to the banks located within its service area, the Bank also competes with savings and loan associations, credit unions, farm credit services, finance companies, personal loan companies, insurance companies, money market funds, and other non-depository financial intermediaries. Also, financial intermediaries such as money market mutual funds and large retailers are not subject to the same regulations and laws that govern the operation of traditional depository institutions and accordingly may have an advantage in competing for funds.

Foreign Operations

The Company has no investments with any foreign entity other than one nominal demand deposit account, which is maintained with a Canadian bank in order to facilitate the clearing of checks drawn on banks located in other countries. There are no foreign loans.

Employees

At December 31, 2009, the Company, including its subsidiaries, had 461 full-time equivalent employees. Benefit programs include a 401(k) plan, group medical insurance, group life insurance and paid vacations. The Company also maintained a defined benefit pension plan which, effective April 1, 2000, was frozen and employees can no longer accrue new benefits under that plan. The Company also has an equity incentive plan under which stock-based incentives and compensation may be granted to employees and directors. The Company also has an employee deferred compensation plan available to certain employees. The Bank is not a party to any collective bargaining agreement, and employee relations are considered good.

Forward-looking Statements

This document (including information incorporated by reference) contains, and future oral and written statements of the Company and its management may contain, forward-looking statements, within the meaning of such term in the Private Securities Litigation Reform Act of 1995, with respect to the financial condition, results of operations, plans, objectives, future performance and business of the Company. Forward-looking statements, which may be based upon beliefs, expectations and assumptions of the Company’s management and on information currently available to management, are generally identifiable by the use of words such as “believe,” “expect,” “anticipate,” “plan,” “intend,” “estimat “may,” “will,” “would,” “could,” “should” or other similar expressions. Additionally, all statements in this document, includin forward-looking statements, speak only as of the date they are made, and the Company undertakes no obligation to update any statement in light of new information or future events.

The Company's ability to predict results or the actual effect of future plans or strategies is inherently uncertain. The factors, which could have a material adverse effect on the operations and future prospects of the Company and its subsidiaries are detailed in the "Risk Factors" section included under Item 1a. of Part I of this Form 10-K. In addition to the risk factors described in that section, there are other factors that may impact any public company, including ours, which could have a material adverse effect on the operations and future prospects of the Company and its subsidiaries. These additional factors include, but are not limited to, the following:

- the effects of future economic, business and market conditions and changes, domestic and foreign, including seasonality;

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- governmental monetary and fiscal policies;
- legislative and regulatory changes, including changes in banking, securities and tax laws and regulations and their application by our regulators, and changes in the scope and cost of Federal Deposit Insurance Corporation, or FDIC, insurance and other coverages;
- changes in accounting policies, rules and practices;
- the risks of changes in interest rates on the levels, composition and costs of deposits, loan demand, and the values and liquidity of loan collateral, securities, and other interest sensitive assets and liabilities;
- the failure of assumptions and estimates underlying the establishment of reserves for possible loan losses and other estimates;
- changes in borrowers' credit risks and payment behaviors;
- changes in the availability and cost of credit and capital in the financial markets;
- changes in the prices, values and sales volumes of residential and commercial real estate;
- the effects of competition from a wide variety of local, regional, national and other providers of financial, investment and insurance services;
- the risks of mergers, acquisitions and divestitures, including, without limitation, the related time and costs of implementing such transactions, integrating operations as part of these transactions and possible failures to achieve expected gains, revenue growth and/or expense savings from such transactions;
- changes in technology or products that may be more difficult, costly, or less effective than anticipated;
- the effects of war or other conflicts, acts of terrorism or other catastrophic events, including storms, droughts, tornados and flooding, that may affect general economic conditions, including agricultural production and demand and prices for agricultural goods and land used for agricultural purposes, generally and in our markets;
- the failure of assumptions and estimates used in our reviews of our loan portfolio and our analysis of our capital position; and
- other factors and risks described under "Risk Factors" herein.

These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements. For additional information regarding these and other risks, uncertainties and other factors, please review the disclosure in this annual report under "Risk Factors."

Internet Website

The Company maintains an internet site at www.lakecitybank.com. The Company makes available free of charge on this site its annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and other reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after it electronically files such material with, or furnishes it to, the Securities and Exchange Commission. The Company's Articles of Incorporation, Bylaws, Code of Conduct and the charters of its various committees of the Board of Directors are also available on the website.

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SUPERVISION AND REGULATION

General

Financial institutions, their holding companies and their affiliates are extensively regulated under federal and state law. As a result, the growth and earnings performance of the Company may be affected not only by management decisions and general economic conditions, but also by the requirements of federal and state statutes and by the regulations and policies of various bank regulatory authorities, including the Indiana Department of Financial Institutions (the “DFI”), the Board of Governors of the Federal Reserve System (the “Federal Reserve”) and the Federal Deposit Insurance Corporation (the “FDIC”). Furthermore, taxation laws administered by the Internal Revenue Service and state taxing authorities and securities laws administered by the Securities and Exchange Commission (the “SEC”) and state securities authorities have an impact on the business of the Company. The effect of these statutes, regulations and regulatory policies may be significant, and cannot be predicted with a high degree of certainty.

Federal and state laws and regulations generally applicable to financial institutions regulate, among other things, the scope of business, the kinds and amounts of investments, reserve requirements, capital levels relative to operations, the nature and amount of collateral for loans, the establishment of branches, mergers and consolidations and the payment of dividends. This system of supervision and regulation establishes a comprehensive framework for the respective operations of the Company and its subsidiaries and is intended primarily for the protection of the FDIC-insured deposits and depositors of the Bank, rather than shareholders. In addition to this generally applicable regulatory framework, turmoil in the credit markets in recent years has prompted the enactment of unprecedented legislation that has allowed the U.S. Treasury to make equity capital available to qualifying financial institutions to help restore confidence and stability in the U.S. financial markets, which imposes additional requirements on institutions in which the U.S. Treasury Department invests.

The following is a summary of the material elements of the regulatory framework that currently applies to the Company and its subsidiaries. It does not describe all of the statutes, regulations and regulatory policies that apply, nor does it restate all of the requirements of those that are described. Additionally, in response to the global financial crisis that began in 2007, various legislative and regulatory proposals have been issued addressing, among other things, the restructuring of the federal bank regulatory system, more stringent regulation of consumer products such as mortgages and credit cards, and safe and sound compensation practices. At this time, the Company is unable to determine whether any of these proposals will be adopted as proposed. As such, the following is qualified in its entirety by reference to applicable law. Any change in statutes, regulations or regulatory policies may have a material effect on the business of the Company and its subsidiaries.

The Company

General. The Company, as the sole shareholder of the Bank, is a bank holding company. As a bank holding company, the Company is registered with, and is subject to regulation by, the Federal Reserve under the Bank Holding Company Act of 1956, as amended (the “BHCA”). In accordance with Federal Reserve policy, the Company is expected to act as a source of financial strength to the Bank and to commit resources to support the Bank in circumstances where the Company might not otherwise do so. Under the BHCA, the Company is subject to periodic examination by the Federal Reserve. The Company is required to file with the Federal Reserve periodic reports of the Company’s operations and such additional information regarding the Company and its subsidiaries as the Federal Reserve may require. The Company is also subject to regulation by the DFI under Indiana law.

Acquisitions, Activities and Change in Control. The primary purpose of a bank holding company is to control and manage banks. The BHCA generally requires the prior approval of the Federal Reserve for any merger involving a bank holding company or any acquisition by a bank holding company of another bank or bank holding company. Subject to certain conditions (including deposit concentration limits established by the BHCA), the Federal Reserve may allow a bank holding company to acquire banks located in any state of the United States. In approving interstate acquisitions, the Federal Reserve is required to give effect to applicable state law limitations on the aggregate amount of deposits that may be held by the acquiring bank holding company and its insured depository institution affiliates in the state in which the target bank is located (provided that those limits do not discriminate against out-of-state depository institutions or their holding companies) and state laws that require that the target bank have been in existence for a minimum period of time (not to exceed five years) before being acquired by an out-of-state bank holding company.

The BHCA generally prohibits the Company from acquiring direct or indirect ownership or control of more than 5% of the voting shares of any company that is not a bank and from engaging in any business other than that of banking, managing and controlling banks or furnishing services to banks and their subsidiaries. This general prohibition is subject to a number of exceptions. The principal exception allows bank holding companies to engage in, and to own shares of companies engaged in, certain businesses found by the Federal Reserve to be "so closely related to banking ... as to be a proper incident thereto." This authority would permit the Company to engage in a variety of banking-related businesses, including the ownership and operation of a thrift, or any entity engaged in consumer finance, equipment leasing, the operation of a computer service bureau (including software development), and mortgage banking and brokerage. The BHCA generally does not place territorial restrictions on the domestic activities of non-bank subsidiaries of bank holding companies.

Additionally, bank holding companies that meet certain eligibility requirements prescribed by the BHCA and elect to operate as financial holding companies may engage in, or own shares in companies engaged in, a wider range of nonbanking activities, including securities and insurance underwriting and sales, merchant banking and any other activity that the Federal Reserve, in consultation with the Secretary of the Treasury, determines by regulation or order is financial in nature, incidental to any such financial activity or complementary to any such financial activity and does not pose a substantial risk to the safety or soundness of depository institutions or the financial system generally. As of the date of this filing, the Company has not applied for approval to operate as a financial holding company.

Federal law also prohibits any person or company from acquiring "control" of an FDIC-insured depository institution or its holding company without prior notice to the appropriate federal bank regulator. "Control" is conclusively presumed to exist upon the acquisition of 25% or more of the outstanding voting securities of a bank or bank holding company, but may arise under certain circumstances between 10% and 24.99% ownership.

Capital Requirements. Bank holding companies are required to maintain minimum levels of capital in accordance with Federal Reserve capital adequacy guidelines. If capital levels fall below the minimum required levels, a bank holding company, among other things, may be denied approval to acquire or establish additional banks or non-bank businesses.

The Federal Reserve's capital guidelines establish the following minimum regulatory capital requirements for bank holding companies: (i) a risk-based requirement expressed as a percentage of total assets weighted according to risk; and (ii) a leverage requirement expressed as a percentage of total assets. The risk-based requirement consists of a minimum ratio of total capital to total risk-weighted assets of 8% and a minimum ratio of Tier 1 capital to total risk-weighted assets of 4%. The leverage requirement consists of a minimum ratio of Tier 1 capital to total assets of 3% for the most highly rated companies, with a minimum requirement of 4% for all others. For purposes of these capital standards, Tier 1 capital consists primarily of permanent stockholders' equity less intangible assets (other than certain loan servicing rights and purchased credit card relationships). Total capital consists primarily of Tier 1 capital plus Tier 2 capital which consists of other non-permanent capital items such as certain other debt and equity instruments that do not qualify as Tier 1 capital and a portion of the company's allowance for loan and lease losses.

The risk-based and leverage standards described above are minimum requirements. Higher capital levels will be required if warranted by the particular circumstances or risk profiles of individual banking organizations. For example, the Federal Reserve's capital guidelines contemplate that additional capital may be required to take adequate account of, among other things, interest rate risk, or the risks posed by concentrations of credit, nontraditional activities or securities trading activities. Further, any banking organization experiencing or anticipating significant growth would be expected to maintain capital ratios, including tangible capital positions (i.e., Tier 1 capital less all intangible assets), well above the minimum levels. As of December 31, 2009, the Company had regulatory capital in excess of the Federal Reserve's minimum requirements.

Emergency Economic Stabilization Act of 2008. Events in the U.S. and global financial markets over the past several years, including deterioration of the worldwide credit markets, have created significant challenges for financial institutions throughout the country. In response to this crisis affecting the U.S. banking system and financial markets, on October 3, 2008, the U.S. Congress passed, and the President signed into law, the Emergency Economic Stabilization Act of 2008 (the "EESA"). The EESA authorized the Secretary of the United States Department of Treasury ("Treasury") to implement various temporary emergency programs designed to strengthen the capital positions of financial institutions and stimulate the availability of credit within the U.S. financial system. Financial institutions participating in certain of the programs established under the EESA are required to adopt Treasury's standards for executive compensation and corporate governance.

The TARP Capital Purchase Program. On October 14, 2008, Treasury announced that it would provide Tier 1 capital (in the form of perpetual preferred stock) to eligible financial institutions. This program, known as the

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TARP Capital Purchase Program (the "CPP"), allocated $250 billion from the $700 billion authorized by the EESA to Treasury for the purchase of senior preferred shares from qualifying financial institutions (the "CPP Preferred Stock"). Under the program, eligible institutions were able to sell equity interests to the Treasury in amounts equal to between 1% and 3% of the institution's risk-weighted assets. The CPP Preferred Stock is non-voting and pays dividends at the rate of 5% per annum for the first five years and thereafter at a rate of 9% per annum. In conjunction with the purchase of the CPP Preferred Stock, the Treasury received warrants to purchase common stock from the participating public institutions with an aggregate market price equal to 15% of the preferred stock investment. Participating financial institutions are required to adopt Treasury's standards for executive compensation and corporate governance for the period during which Treasury holds equity issued under the CPP. These requirements are discussed in more detail in the Compensation Discussion and Analysis section in the Company's proxy statement, which is incorporated by reference in this Form 10-K.

Pursuant to the CPP, on February 27, 2009, the Company entered into a Letter Agreement with Treasury, pursuant to which the Company issued (i) 56,044 shares of the Company's Fixed Rate Cumulative Perpetual Preferred Stock, Series A and (ii) a warrant to purchase 396,538 shares of the Company's common stock, no par value, for an aggregate purchase price of $56,044,000 in cash. Since the Company's participation in the CPP, the Company has raised additional capital through a public offering of common stock and, as a result of that offering, the number of shares of common stock subject to the warrant have been reduced by 50% to 198,269. The Company's federal regulators, the Treasury and the Treasury's Office of the Inspector General maintains significant oversight over the Company as a participating institution, to evaluate how it is using the capital provided and to ensure that it strengthens its efforts to help its borrowers avoid foreclosure, which is one of the core aspects of the EESA.

Dividend Payments. The Company's ability to pay dividends to its shareholders may be affected by both general corporate law considerations and policies of the Federal Reserve applicable to bank holding companies. As an Indiana corporation, the Company is subject to the limitations of the Indiana General Business Corporation Law, which prohibit the Company from paying dividends if the Company is, or by payment of the dividend would become, insolvent, or if the payment of dividends would render the Company unable to pay its debts as they become due in the usual course of business. Additionally, policies of the Federal Reserve caution that a bank holding company should not pay cash dividends unless its net income available to common shareholders over the past year has been sufficient to fully fund the dividends and the prospective rate of earnings retention appears consistent with its capital needs, asset quality, and overall financial condition. The Federal Reserve also possesses enforcement powers over bank holding companies and their non-bank subsidiaries to prevent or remedy actions that represent unsafe or unsound practices or violations of applicable statutes and regulations. Among these powers is the ability to proscribe the payment of dividends by banks and bank holding companies. Further, with respect to the Company's participation in the CPP, the terms of the CPP Preferred Stock provide that no dividends on any common or preferred stock that ranks equal to or junior to the CPP Preferred Stock may be paid unless and until all accrued and unpaid dividends for all past dividend periods on the CPP Preferred Stock have been fully paid.

Federal Securities Regulation. The Company's common stock is registered with the SEC under the Securities Act of 1933, as amended, and the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Consequently, the Company is subject to the information, proxy solicitation, insider trading and other restrictions and requirements of the SEC under the Exchange Act.

The Bank

General. The Bank is an Indiana-chartered bank, the deposit accounts of which are insured by the FDIC's Deposit Insurance Fund ("DIF") to the maximum extent provided under federal law and FDIC regulations. The Bank is also a member of the Federal Reserve System ("member bank"). As an Indiana-chartered, FDIC-insured member bank, the Bank is presently subject to the examination, supervision, reporting and enforcement requirements of the DFI, the chartering authority for Indiana banks, the Federal Reserve, as the primary federal regulator of member banks, and the FDIC, as administrator of the DIF.

Deposit Insurance. As an FDIC-insured institution, the Bank is required to pay deposit insurance premium assessments to the FDIC. The FDIC has adopted a risk-based assessment system whereby FDIC-insured depository institutions pay insurance premiums at rates based on their risk classification. An institution's risk classification is assigned based on its capital levels and the level of supervisory concern the institution poses to the regulators. Under the regulations of the FDIC, as presently in effect, insurance assessments range from 0.07% to 0.78% of total deposits, depending on an institution's risk classification, its levels of unsecured debt and secured liabilities, and, in certain cases, its level of brokered deposits.

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Furthermore, as a result of the increased volume of bank failures in 2008 and 2009, on May 22, 2009, the FDIC approved a final rule imposing a special assessment on all depository institutions whose deposits are insured by the FDIC. This one-time special assessment was imposed on institutions in the second quarter, and was collected on September 30, 2009. Pursuant to the final rule, the FDIC imposed on the Bank a special assessment in the amount of $1.1 million, which was due and payable on September 30, 2009.

On November 12, 2009, the FDIC adopted a final rule that required insured depository institutions to prepay on December 30, 2009, their estimated quarterly risk-based assessments for the fourth quarter of 2009 and for all of 2010, 2011, and 2012. On December 31, 2009, the Bank paid the FDIC $10.1 million in prepaid assessments. An institution's prepaid assessments were calculated based on the institution's actual September 30, 2009 assessment base, adjusted quarterly by an estimated 5 percent annual growth rate through the end of 2012. The FDIC also used the institution's total base assessment rate in effect on September 30, 2009, increasing it by an annualized 3 basis points beginning in 2011. The FDIC will begin to offset prepaid assessments on March 30, 2010, representing payment of the regular quarterly risk-based deposit insurance assessment for the fourth quarter of 2009. Any prepaid assessment not exhausted after collection of the amount due on June 30, 2013, will be returned to the institution.

FDIC Temporary Liquidity Guarantee Program. In conjunction with Treasury's actions to address the credit and liquidity crisis in financial markets, on October 14, 2008, the FDIC announced the Temporary Liquidity Guarantee Program. One component of the Temporary Liquidity Guarantee Program is the Transaction Account Guarantee Program, which temporarily provides participating institutions with unlimited deposit insurance coverage for non-interest bearing and certain low-interest bearing transaction accounts maintained at FDIC insured institutions. All institutions that did not opt out of the Transaction Account Guarantee Program were subject to a 10 basis point per annum assessment on amounts in excess of $250,000 in covered transaction accounts through December 31, 2009. On August 26, 2009, the FDIC extended the Transaction Account Guarantee Program for an additional six months through June 30, 2010. Beginning January 1, 2010, the assessment levels increased to 15 basis points, 20 basis points or 25 basis points per annum, based on the risk category to which an institution is assigned for purposes of the risk-based premium system. The Bank did not opt out of the six-month extension of the Transaction Account Guarantee Program. As a result, the Bank, like every other FDIC-insured depository institution in the United States that did not opt out of the Transaction Account Guarantee Program, is incurring fees on amounts in excess of $250,000 in covered transaction accounts.

FICO Assessments. The Financing Corporation ("FICO") is a mixed-ownership governmental corporation chartered by the former Federal Home Loan Bank Board pursuant to the Federal Savings and Loan Insurance Corporation Recapitalization Act of 1987 to function as a financing vehicle for the recapitalization of the former Federal Savings and Loan Insurance Corporation. FICO issued 30-year non-callable bonds of approximately $8.2 billion that mature by 2019. Since 1996, federal legislation has required that all FDIC-insured depository institutions pay assessments to cover interest payments on FICO's outstanding obligations. These FICO assessments are in addition to amounts assessed by the FDIC for deposit insurance. During the year ended December 31, 2009, the FICO assessment rate was approximately 0.01% of deposits.

Supervisory Assessments. All Indiana banks are required to pay supervisory assessments to the DFI to fund the operations of the DFI. The amount of the assessment is calculated on the basis of the bank's total assets. During the year ended December 31, 2009, the Bank paid supervisory assessments to the DFI totaling $204,000.

Capital Requirements. Banks are generally required to maintain capital levels in excess of other businesses. Under federal regulations, the Bank is subject to the following minimum capital standards: (i) a leverage requirement consisting of a minimum ratio of Tier 1 capital to total assets of 3% for the most highly-rated banks with a minimum requirement of at least 4% for all others; and (ii) a risk-based capital requirement consisting of a minimum ratio of total capital to total risk-weighted assets of 8% and a minimum ratio of Tier 1 capital to total risk-weighted assets of

4%. In general, the components of Tier 1 capital and total capital are the same as those for bank holding companies discussed above.

The capital requirements described above are minimum requirements. Higher capital levels will be required if warranted by the particular circumstances or risk profiles of individual institutions. For example, federal regulations provide that additional capital may be required to take adequate account of, among other things, interest rate risk or the risks posed by concentrations of credit, nontraditional activities or securities trading activities.

Further, federal law and regulations provide various incentives for financial institutions to maintain regulatory capital at levels in excess of minimum regulatory requirements. For example, a financial institution that is “well-capitalized” may qualify for exemptions from prior notice or application requirements otherwise applicable to

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certain types of activities and may qualify for expedited processing of other required notices or applications. Additionally, one of the criteria that determines a bank holding company's eligibility to operate as a financial holding company is a requirement that all of its financial institution subsidiaries be "well-capitalized." Under the regulations of the Federal Reserve, in order to be "well-capitalized" a financial institution must maintain a ratio of total capital to total risk-weighted assets of 10% or greater, a ratio of Tier 1 capital to total risk-weighted assets of 6% or greater and a ratio of Tier 1 capital to total assets of 5% or greater.

Federal law also provides the federal banking regulators with broad power to take prompt corrective action to resolve the problems of undercapitalized institutions. The extent of the regulators' powers depends on whether the institution in question is "adequately capitalized," "undercapitalized," "significantly undercapitalized" or "critically undercapitalized," in each case as defined by regulation. Depending upon the capital category to which an institution is assigned, the regulators' corrective powers include: (i) requiring the institution to submit a capital restoration plan; (ii) limiting the institution's asset growth and restricting its activities; (iii) requiring the institution to issue additional capital stock (including additional voting stock) or to be acquired; (iv) restricting transactions between the institution and its affiliates; (v) restricting the interest rate the institution may pay on deposits; (vi) ordering a new election of directors of the institution; (vii) requiring that senior executive officers or directors be dismissed; (viii) prohibiting the institution from accepting deposits from correspondent banks; (ix) requiring the institution to divest certain subsidiaries; (x) prohibiting the payment of principal or interest on subordinated debt; and (xi) ultimately, appointing a receiver for the institution.

As of December 31, 2009: (i) the Bank was not subject to a directive from the Federal Reserve to increase its capital to an amount in excess of the minimum regulatory capital requirements; (ii) the Bank exceeded its minimum regulatory capital requirements under Federal Reserve capital adequacy guidelines; and (iii) the Bank was "well-capitalized," as defined by Federal Reserve regulations.

Dividend Payments. The primary source of funds for the Company is dividends from the Bank. Indiana law prohibits the Bank from paying dividends in an amount greater than its undivided profits. The Bank is required to obtain the approval of the DFI for the payment of any dividend if the total of all dividends declared by the Bank during the calendar year, including the proposed dividend, would exceed the sum of the Bank's net income for the year to date combined with its retained net income for the previous two years. Indiana law defines "retained net income" to mean the net income of a specified period, calculated under the consolidated report of income instructions, less the total amount of all dividends declared for the specified period. The Federal Reserve Act also imposes limitations on the amount of dividends that may be paid by state member banks, such as the Bank. Without Federal Reserve approval, a state member bank may not pay dividends in any calendar year that, in the aggregate, exceed the bank's calendar year-to-date net income plus the bank's retained net income for the two preceding calendar years.

The payment of dividends by any financial institution is affected by the requirement to maintain adequate capital pursuant to applicable capital adequacy guidelines and regulations, and a financial institution generally is prohibited from paying any dividends if, following payment thereof, the institution would be undercapitalized. As described above, the Bank exceeded its minimum capital requirements under applicable guidelines as of December 31, 2009. As of December 31, 2009, approximately $24.7 million was available to be paid as dividends by the Bank. Notwithstanding the availability of funds for dividends, however, the Federal Reserve may prohibit the payment of any dividends by the Bank if the Federal Reserve determines such payment would constitute an unsafe or unsound practice.

Insider Transactions. The Bank is subject to certain restrictions imposed by federal law on extensions of credit to the Company, on investments in the stock or other securities of the Company and the acceptance of the stock or other securities of the Company as collateral for loans made by the Bank. Certain limitations and reporting requirements are also placed on extensions of credit by the Bank to its directors and officers, to directors and officers of the Company, to principal shareholders of the Company and to “related interests” of such directors, officers and principal shareholders. In addition, federal law and regulations may affect the terms upon which any person who is a director or officer of the Company or the Bank or a principal shareholder of the Company may obtain credit from banks with which the Bank maintains a correspondent relationship.

Safety and Soundness Standards. The federal banking agencies have adopted guidelines that establish operational and managerial standards to promote the safety and soundness of federally insured depository institutions. The guidelines set forth standards for internal controls, information systems, internal audit systems, loan documentation, credit underwriting, interest rate exposure, asset growth, compensation, fees and benefits, asset quality and earnings.

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In general, the safety and soundness guidelines prescribe the goals to be achieved in each area, and each institution is responsible for establishing its own procedures to achieve those goals. If an institution fails to comply with any of the standards set forth in the guidelines, the institution's primary federal regulator may require the institution to submit a plan for achieving and maintaining compliance. If an institution fails to submit an acceptable compliance plan, or fails in any material respect to implement a compliance plan that has been accepted by its primary federal regulator, the regulator is required to issue an order directing the institution to cure the deficiency. Until the deficiency cited in the regulator's order is cured, the regulator may restrict the institution's rate of growth, require the institution to increase its capital, restrict the rates the institution pays on deposits or require the institution to take any action the regulator deems appropriate under the circumstances. Noncompliance with the standards established by the safety and soundness guidelines may also constitute grounds for other enforcement action by the federal banking regulators, including cease and desist orders and civil money penalty assessments.

Branching Authority. Indiana banks, such as the Bank, have the authority under Indiana law to establish branches anywhere in the State of Indiana, subject to receipt of all required regulatory approvals.

Federal law permits state and national banks to merge with banks in other states subject to: (i) regulatory approval; (ii) federal and state deposit concentration limits; and (iii) state law limitations requiring the merging bank to have been in existence for a minimum period of time (not to exceed five years) prior to the merger. The establishment of new interstate branches or the acquisition of individual branches of a bank in another state (rather than the acquisition of an out-of-state bank in its entirety) is permitted only in those states the laws of which expressly authorize such expansion.

State Bank Investments and Activities. The Bank generally is permitted to make investments and engage in activities directly or through subsidiaries as authorized by Indiana law. However, under federal law and FDIC regulations, FDIC-insured state banks are prohibited, subject to certain exceptions, from making or retaining equity investments of a type, or in an amount, that are not permissible for a national bank. Federal law and FDIC regulations also prohibit FDIC-insured state banks and their subsidiaries, subject to certain exceptions, from engaging as principal in any activity that is not permitted for a national bank unless the bank meets, and continues to meet, its minimum regulatory capital requirements and the FDIC determines the activity would not pose a significant risk to the deposit insurance fund of which the bank is a member. These restrictions have not had, and are not currently expected to have, a material impact on the operations of the Bank.

Federal Reserve System. Federal Reserve regulations, as presently in effect, require depository institutions to maintain reserves against their transaction accounts (primarily NOW and regular checking accounts), as follows: for transaction accounts aggregating $55.2 million or less, the reserve requirement is 3% of total transaction accounts; and for transaction accounts aggregating in excess of $55.2 million, the reserve requirement is $1.335 million plus 10% of the aggregate amount of total transaction accounts in excess of $55.2 million. The first $10.7 million of otherwise reservable balances are exempted from the reserve requirements. These reserve requirements are subject to annual adjustment by the Federal Reserve. We will believe the Bank will continue to maintain compliance with the foregoing requirements.

INDUSTRY SEGMENTS

The Company's chief decision-makers monitor and evaluate financial performance on a Company-wide basis. All of the Company's financial service operations are similar and considered by management to be aggregated into one reportable operating segment. While the Company has assigned certain management responsibilities by region and business-line, the Company's chief decision-makers monitor and evaluate financial performance on a Company-wide basis. The majority of the Company's revenue is from the business of banking and the Company's assigned regions have similar economic characteristics, products, services and customers. Accordingly, all of the Company's operations are considered by management to be aggregated in one reportable operating segment.

GUIDE 3 INFORMATION

On the pages that follow are tables that set forth selected statistical information relative to the business of the Company. This data should be read in conjunction with the consolidated financial statements, related notes and "Management's Discussion and Analysis of Financial Condition and Results of Operations" as set forth in Items 7 & 8, below, herein incorporated by reference.

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DISTRIBUTION OF ASSETS, LIABILITIES AND STOCKHOLDERS' EQUITY;
INTEREST RATES AND INTEREST DIFFERENTIAL
(in thousands of dollars)

	2009			2008		
	Average Balance	Interest Income	Yield (1)	Average Balance	Interest Income	Yield (1)
ASSETS						
Earning assets:						
Loans:						
Taxable (2)(3)	$1,897,544	$96,151	5.07 %	$1,662,355	$99,538	5.99 %
Tax exempt (1)	4,202	199	4.74	2,669	147	5.51
Investments: (1)						
Available for sale	399,342	21,179	5.30	368,578	19,731	5.35
Short-term investments	22,540	35	0.16	12,136	171	1.41
Interest bearing deposits	1,631	26	1.59	2,045	49	2.40
Total earning assets	2,325,259	117,590	5.06 %	2,047,783	119,636	5.84 %
Nonearning assets:						
Cash and due from banks	39,616	0		41,302	0	
Premises and equipment	30,208	0		28,200	0	
Other nonearning assets	76,671	0		70,986	0	
Less allowance for loan losses	(24,801)	0		(17,597)	0	
Total assets	$2,446,953	$117,590		$2,170,674	$119,636	

(1) Tax exempt income was converted to a fully taxable equivalent basis at a 35 percent tax rate for 2009 and 2008. The tax equivalent rate for tax exempt loans and tax exempt securities acquired after January 1, 1983 included the TEFRA adjustment applicable to nondeductible interest expenses.

(2) Loan fees, which are immaterial in relation to total taxable loan interest income for the years ended December 31, 2009 and 2008, are included as taxable loan interest income.

(3) Nonaccrual loans are included in the average balance of taxable loans.

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DISTRIBUTION OF ASSETS, LIABILITIES AND STOCKHOLDERS' EQUITY;
INTEREST RATES AND INTEREST DIFFERENTIAL (Cont.)
(in thousands of dollars)

	2008 Average Balance	2008 Interest Income	2008 Yield (1)	2007 Average Balance	2007 Interest Income	2007 Yield (1)
ASSETS						
Earning assets:						
Loans:						
Taxable (2)(3)	$1,662,355	$99,538	5.99 %	$1,401,480	$102,840	7.34 %
Tax exempt (1)	2,669	147	5.51	2,588	166	6.41
Investments: (1)						
Available for sale	368,578	19,731	5.35	306,293	15,140	4.94
Short-term investments	12,136	171	1.41	17,412	863	4.96
Interest bearing deposits	2,045	49	2.40	1,486	68	4.58
Total earning assets	2,047,783	119,636	5.84 %	1,729,259	119,077	6.89 %
Nonearning assets:						
Cash and due from banks	41,302	0		44,565	0	
Premises and equipment	28,200	0		26,042	0	
Other nonearning assets	70,986	0		54,220	0	
Less allowance for loan losses	(17,597)	0		(15,045)	0	
Total assets	$2,170,674	$119,636		$1,839,041	$119,077	

(1) Tax exempt income was converted to a fully taxable equivalent basis at a 35 percent tax rate for 2008 and 2007. The tax equivalent rate for tax exempt loans and tax exempt securities acquired after January 1, 1983 included the TEFRA adjustment applicable to nondeductible interest expenses.

(2) Loan fees, which are immaterial in relation to total taxable loan interest income for the years ended December 31, 2008 and 2007, are included as taxable loan interest income.

(3) Nonaccrual loans are included in the average balance of taxable loans.

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DISTRIBUTION OF ASSETS, LIABILITIES AND STOCKHOLDERS' EQUITY;
INTEREST RATES AND INTEREST DIFFERENTIAL (Cont.)
(in thousands of dollars)

	2009 Average Balance	2009 Interest Expense	2009 Yield		2008 Average Balance	2008 Interest Expense	2008 Yield	
LIABILITIES AND STOCKHOLDERS' EQUITY								
Interest bearing liabilities:								
Savings deposits	$70,202	$100	0.14	%	$64,877	$64	0.10	%
Interest bearing checking accounts	572,539	5,790	1.01		495,057	9,979	2.02	
Time deposits:								
In denominations under $100,000	359,526	15,356	4.27		329,783	13,924	4.22	
In denominations over $100,000	638,956	11,001	1.72		528,316	20,613	3.90	
Miscellaneous short-term borrowings	272,224	1,089	0.40		278,451	5,620	2.02	
Long-term borrowings and subordinated debentures	72,792	2,726	3.74		86,230	5,016	5.82	
Total interest bearing liabilities	1,986,239	36,062	1.82	%	1,782,714	55,216	3.10	%
Noninterest bearing liabilities and stockholders' equity:								
Demand deposits	229,009	0			219,762	0		
Other liabilities	19,354	0			17,138	0		
Stockholders' equity	212,351	0			151,060	0		
Total liabilities and stockholders' equity	$2,446,953	$36,062			$2,170,674	$55,216		
Net interest differential - yield on average daily earning assets		$81,528	3.51	%		$64,420	3.14	%

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DISTRIBUTION OF ASSETS, LIABILITIES AND STOCKHOLDERS' EQUITY;
INTEREST RATES AND INTEREST DIFFERENTIAL (Cont.)
(in thousands of dollars)

	2008 Average Balance	2008 Interest Expense	2008 Yield		2007 Average Balance	2007 Interest Expense	2007 Yield	
LIABILITIES AND STOCKHOLDERS' EQUITY								
Interest bearing liabilities:								
Savings deposits	$64,877	$64	0.10	%	$67,104	$133	0.20	%
Interest bearing checking accounts	495,057	9,979	2.02		425,753	14,854	3.49	
Time deposits:								
In denominations under $100,000	329,783	13,924	4.22		295,328	14,289	4.84	
In denominations over $100,000	528,316	20,613	3.90		462,056	24,338	5.27	
Miscellaneous short-term borrowings	278,451	5,620	2.02		177,343	7,239	4.08	
Long-term borrowings and subordinated debentures (1)	86,230	5,016	5.82		30,972	2,628	8.49	
Total interest bearing liabilities	1,782,714	55,216	3.10	%	1,458,556	63,481	4.35	%
Noninterest bearing liabilities and stockholders' equity:								
Demand deposits	219,762	0			226,484	0		
Other liabilities	17,138	0			16,234	0		
Stockholders' equity	151,060	0			137,767	0		
Total liabilities and stockholders' equity	$2,170,674	$55,216			$1,839,041	$63,481		
Net interest differential - yield on average daily earning assets		$64,420	3.14	%		$55,596	3.22	%

(1)

Long-term borrowings and subordinated debentures interest expense was reduced by interest capitalized on construction in process for 2007.

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ANALYSIS OF CHANGES IN INTEREST DIFFERENTIALS
(fully taxable equivalent basis)
(in thousands of dollars)

YEAR ENDED DECEMBER 31,

	2009 Over (Under) 2008 (1)			2008 Over (Under) 2007 (1)		
	Volume	Rate	Total	Volume	Rate	Total
INTEREST AND LOAN FEE INCOME (2)						
Loans:						
Taxable	$13,045	$(16,432)	$(3,387)	$17,372	$(20,674)	$(3,302)
Tax exempt	75	(23)	52	5	(24)	(19)
Investments:						
Available for sale	1,633	(185)	1,448	3,260	1,331	4,591
Short-term investments	83	(219)	(136)	(206)	(486)	(692)
Interest bearing deposits	(9)	(14)	(23)	20	(39)	(19)
Total interest income	14,827	(16,873)	(2,046)	20,451	(19,892)	559
INTEREST EXPENSE						
Savings deposits	6	30	36	(4)	(65)	(69)
Interest bearing checking accounts	1,376	(5,565)	(4,189)	2,134	(7,009)	(4,875)
Time deposits:						
In denominations under $100,000	1,269	163	1,432	1,566	(1,931)	(365)
In denominations over $100,000	3,659	(13,271)	(9,612)	3,168	(6,893)	(3,725)
Miscellaneous short-term borrowings	(123)	(4,408)	(4,531)	3,021	(4,640)	(1,619)
Long-term borrowings and subordinated debentures	(697)	(1,593)	(2,290)	3,435	(1,047)	2,388
Total interest expense	5,490	(24,644)	(19,154)	13,320	(21,585)	(8,265)
INCREASE (DECREASE) IN INTEREST DIFFERENTIALS	$9,337	$7,771	$17,108	$7,131	$1,693	$8,824

(1) The earning assets and interest bearing liabilities used to calculate interest differentials are based on average daily balances for 2009, 2008 and 2007. The changes in volume represent "changes in volume times the old rate". The

changes in rate represent "changes in rate times old volume". The changes in rate/volume were also calculated by "change in rate times change in volume" and allocated consistently based upon the relative absolute values of the changes in volume and changes in rate.

(2) Tax exempt income was converted to a fully taxable equivalent basis at a 35 percent tax rate for 2009, 2008 and 2007. The tax equivalent rate for tax exempt loans and tax exempt securities acquired after January 1, 1983 included the TEFRA adjustment applicable to nondeductible interest expense.

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ANALYSIS OF SECURITIES
(in thousands of dollars)

The amortized cost and the fair value of securities as of December 31, 2009, 2008 and 2007 were as follows:

	2009 Amortized Cost	2009 Fair Value	2008 Amortized Cost	2008 Fair Value	2007 Amortized Cost	2007 Fair Value
Securities available for sale:						
U.S. Treasury securities	$1,005	$992	$1,001	$1,025	$1,201	$1,206
U.S. Government agencies	4,588	4,610	15,453	15,685	18,539	18,555
Mortgage-backed securities	264,276	270,796	225,892	229,571	205,335	205,202
Non-agency residential mortgage-backed securities	88,382	72,495	106,790	85,098	45,823	45,293
State and municipal securities	59,375	61,135	55,081	55,651	56,613	57,501
Total debt securities available for sale	$417,626	$410,028	$404,217	$387,030	$327,511	$327,757

At year-end 2009, there were no holdings of securities of any one issuer, other than the U.S. Government, government agencies and government sponsored agencies, in an amount greater than 10% of stockholders' equity. At year-end 2008, there were no holdings of securities of any one issuer, other than the U.S. Government, government agencies and government sponsored agencies, in an amount greater than 10% of stockholders' equity with the exception of Residential Accredit Loans, Inc., which had a book value of $21.3 million and a market value of $15.8 million, Countrywide Home Loans Alternative Loan Trust, which had a book value of $19.9 million and a market value of $15.1 million and Chase Mortgage Finance Trust, which had a book value of $17.4 million and a market value of $15.0 million. These are all Alt A or Whole Loan securities in the Super Senior tranches, which are the highest rated tranches with very high credit standards. In addition, the collateral of the Alt A or Whole Loan securities purchased must meet certain criteria set by the Company's Asset Liability Management Committee including maximum loan-to-value and minimum FICO scores, consist of only fixed-rate mortgages and must be AAA rated at the time of purchase. See Note 2 for more information on these investments. At year-end 2007, there were no holdings of securities of any one issuer, other than the U.S. Government, government agencies and government sponsored agencies, in an amount greater than 10% of stockholders' equity with the exception of Residential Accredit Loans, Inc., which had a book value of $22.6 million and a market value of $22.3 million.

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ANALYSIS OF SECURITIES (cont.)
(fully tax equivalent basis)
(in thousands of dollars)

The weighted average yields and maturity distribution for debt securities portfolio at December 31, 2009, were as follows:

	Within One Year	After One Year Within Five Years	After Five Years Within Ten Years	Over Ten Years
Securities available for sale:				
US Treasury securities				
Fair value	$0	$992	$0	$0
Yield	0 %	2.38 %	0 %	0 %
U.S. Government agencies				
Fair value	4,610	0	0	0
Yield	3.88 %	0 %	0 %	0 %
Mortgage-backed securities				
Fair value	0	13,977	70,382	186,437
Yield	0 %	5.14 %	5.00 %	5.09 %
Non-agency residential mortgage-backed securities				
Fair value	0	0	5,648	66,847
Yield	0 %	0 %	5.00 %	5.66 %
State and municipal securities				
Fair value	216	5,341	37,107	18,471
Yield	4.90 %	4.08 %	4.47 %	4.28 %
Total debt securities available for sale:				
Fair value	$4,826	$20,310	$113,137	$271,755
Yield	3.92 %	4.73 %	4.82 %	5.18 %

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ANALYSIS OF LOAN PORTFOLIO
Analysis of Loans Outstanding
(in thousands of dollars)

The Company segregates its loan portfolio into four basic segments: commercial (including agricultural loans), residential real estate mortgages, installment and personal line of credit loans (including credit card loans). The loan portfolio as of December 31, 2009, 2008, 2007, 2006 and 2005 was as follows:

	2009	2008	2007	2006	2005
Commercial loans:					
Taxable	$1,697,449	$1,522,523	$1,238,623	$1,081,420	$960,046
Tax exempt	2,085	10,493	1,971	4,991	4,512
Total commercial loans	1,699,534	1,533,016	1,240,594	1,086,411	964,558
Residential real estate mortgage loans	95,211	117,230	124,107	109,176	74,820
Installment loans	51,878	51,174	49,185	52,548	67,964
Line of credit and credit card loans	167,194	132,147	109,760	105,762	91,426
Subtotal loans	2,013,817	1,833,567	1,523,646	1,353,897	1,198,768
Less: Allowance for loan losses	(32,073)	(18,860)	(15,801)	(14,463)	(12,774)
Net deferred loan (fees)/costs	(1,807)	(233)	74	(60)	(38)
Net loans	$1,979,937	$1,814,474	$1,507,919	$1,339,374	$1,185,956

The residential real estate mortgage loan portfolio included construction loans totaling $5,790, $6,468, $5,252, $8,636 and $7,987 as of December 31, 2009, 2008, 2007, 2006 and 2005. The Bank generally sells conforming mortgage loans which it originates. These loans generally represent mortgage loans that are made to clients with long-term or substantial relationships with the Bank on terms consistent with secondary market requirements. The loan classifications are based on the nature of the loans as of the loan origination date. There were no foreign loans included in the loan portfolio for the periods presented.

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ANALYSIS OF LOAN PORTFOLIO (cont.)
Analysis of Loans Outstanding (cont.)
(in thousands of dollars)

Repricing opportunities of the loan portfolio occur either according to predetermined adjustable rate schedules included in the related loan agreements or upon maturity of each principal payment. The following table indicates the scheduled maturities of the loan portfolio as of December 31, 2009.

	Commercial	Residential Real Estate Mortgage	Installment	Line of Credit	Total	Percent	
Original maturity of one day	$ 0	$ 0	$ 0	$ 106,637	$ 106,637	5.30	%
Other within one year	766,059	18,418	16,489	20,199	$ 821,165	40.78	
After one year, within five years	779,741	20,728	33,245	16,148	$ 849,862	42.20	
Over five years	124,589	54,692	2,144	24,210	$ 205,635	10.21	
Nonaccrual loans	29,145	1,373	0	0	$ 30,518	1.52	
Total loans	$ 1,699,534	$ 95,211	$ 51,878	$ 167,194	$ 2,013,817	100.0	%

At maturity, credits are reviewed and, if renewed, are renewed at rates and conditions that prevail at the time of maturity.

Loans due after one year which have a predetermined interest rate and loans due after one year which have floating or adjustable interest rates as of December 31, 2009 amounted to $680,527 and $374,970.

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ANALYSIS OF LOAN PORTFOLIO (cont.)
Review of Nonperforming Loans
(in thousands of dollars)

The following is a summary of nonperforming loans as of December 31, 2009, 2008, 2007, 2006 and 2005.

	2009	2008	2007	2006	2005
PART A - PAST DUE ACCRUING LOANS (90 DAYS OR MORE)					
Residential real estate mortgage loans	$0	$126	$155	$0	$89
Commercial and industrial loans	0	81	65	154	0
Loans to individuals for household, family and other personal expenditures	190	271	189	145	85
Loans to finance agriculture production and other loans to farmers	0	0	0	0	0
Total past due loans	190	478	409	299	174
PART B - NONACCRUAL LOANS					
Residential real estate mortgage loans	1,373	757	18	132	132
Commercial and industrial loans	28,373	20,053	7,021	13,688	7,189
Loans to individuals for household, family and other personal expenditures	0	0	0	0	0
Loans to finance agriculture production and other loans to farmers	772	0	0	0	0
Total nonaccrual loans	30,518	20,810	7,039	13,820	7,321
PART C - TROUBLED DEBT RESTRUCTURED LOANS	0	0	0	0	0
Total nonperforming loans	$30,708	$21,288	$7,448	$14,119	$7,495

Nonearning assets of the Company include nonperforming loans (as indicated above), nonaccrual investments and other real estate and repossessions, the total of which amounted to $31,582 at December 31, 2009.

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ANALYSIS OF LOAN PORTFOLIO (cont.)
Comments Regarding Nonperforming Assets

PART A - CONSUMER LOANS

Consumer installment loans, except those loans that are secured by real estate, are not placed on nonaccrual status since these loans are charged-off when they have been delinquent from 90 to 180 days, and when the related collateral, if any, is not sufficient to offset the indebtedness. Advances under consumer line of credit programs are charged-off when collection appears doubtful.

PART B - NONPERFORMING LOANS

When a loan is classified as a nonaccrual loan, interest on the loan is no longer accrued and all accrued interest receivable is charged-off. It is the policy of the Bank that all loans for which the collateral is insufficient to cover all principal and accrued interest will be reclassified as nonperforming loans to the extent they are unsecured, on or before the date when the loan becomes 90 days delinquent. Thereafter, interest is recognized and included in income only when received. Interest not recorded on nonaccrual loans is referenced in Footnote 4 in Item 8 below.

As of December 31, 2009, there were $30.5 million of loans on nonaccrual status, some of which were also on impaired status. There were $31.8 million of loans classified as impaired.

PART C - TROUBLED DEBT RESTRUCTURED LOANS

Loans renegotiated as troubled debt restructurings are those loans for which either the contractual interest rate has been reduced and/or other concessions are granted to the borrower because of a deterioration in the financial condition of the borrower which results in the inability of the borrower to meet the terms of the loan.

As of December 31, 2009 there were $6.5 million of loans renegotiated as troubled debt restructurings. These loans were excluded from troubled debt restructured loans in the previous table because they were included in nonaccrual loans. As of December 31, 2008, there were no loans renegotiated as troubled debt restructurings.

PART D - OTHER NONPERFORMING ASSETS

Management is of the opinion that there are no significant foreseeable losses relating to nonperforming assets, as defined in the preceding table, or classified loans, except as discussed above in Part B – Nonperforming Loans and Part C – Troubled Debt Restructured Loans.

PART E - LOAN CONCENTRATIONS

There were no loan concentrations within industries not otherwise disclosed, which exceeded ten percent of total loans except commercial real estate. Commercial real estate was $544.3 million at December 31, 2009. Nearly all of the Bank’s commercial, industrial, agricultural real estate mortgage, real estate construction mortgage and consumer loans are made within its basic service area.

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Basis For Determining Allowance For Loan Losses:

The allowance is an amount that management believes will be adequate to absorb probable incurred credit losses relating to specifically identified loans based on an evaluation, as well as other probable incurred losses inherent in the loan portfolio. The evaluations take into consideration such factors as changes in the nature and volume of the loan portfolio, overall portfolio quality, review of specific problem loans, and current economic conditions that may affect the borrower's ability to repay. Management also considers trends in adversely classified loans based upon a monthly review of those credits. An appropriate level of general allowance is determined after considering the following: application of historical loss percentages, emerging market risk, emerging concentrations, commercial loan focus and large credit concentration, new industry lending activity and general economic conditions. For a more thorough discussion of the allowance for loan losses methodology see the Critical Accounting Policies section of Item 7.

Based upon these policies and objectives, $21.2 million, $10.2 million and $4.3 million were charged to the provision for loan losses and added to the allowance for loan losses in 2009, 2008 and 2007.

The allocation of the allowance for loan losses to the various lending areas is performed by management in relation to perceived exposure to loss in the various loan portfolios. However, the allowance for loan losses is available in its entirety to absorb losses in any particular loan category. Although management believes that the allowance for loan losses is adequate to absorb probable incurred losses on any existing loans, management cannot predict loan losses with any certainty, and the Company cannot guarantee that the allowance for loan losses will prove sufficient to cover actual losses in the future.

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ANALYSIS OF LOAN PORTFOLIO (cont.)
Summary of Loan Loss
(in thousands of dollars)

The following is a summary of the loan loss experience for the years ended December 31, 2009, 2008, 2007, 2006 and 2005.

	2009	2008	2007	2006	2005
Amount of loans outstanding, December 31,	$2,012,010	$1,833,335	$1,523,720	$1,353,837	$1,198,730
Average daily loans outstanding during the year ended December 31,	$1,901,746	$1,665,024	$1,404,068	$1,270,484	$1,088,788
Allowance for loan losses, January 1,	$18,860	$15,801	$14,463	$12,774	$10,754
Loans charged-off:					
Commercial	7,251	6,726	2,381	905	317
Residential real estate	337	72	16	0	8
Installment	674	805	537	145	164
Credit cards and personal credit lines	249	3	458	22	112
Total loans charged-off	8,511	7,606	3,392	1,072	601
Recoveries of loans previously charged-off:					
Commercial	337	147	252	53	37
Residential real estate	0	16	27	0	0
Installment	173	200	124	52	89
Credit cards and personal credit lines	12	95	29	12	15
Total recoveries	522	458	432	117	141
Net loans charged-off	7,989	7,148	2,960	955	460
Provision for loan loss charged to expense	21,202	10,207	4,298	2,644	2,480
Balance, December 31,	$32,073	$18,860	$15,801	$14,463	$12,774
Ratio of net charge-offs during the period to average daily loans outstanding:					
Commercial	0.36 %	0.40 %	0.15 %	0.07 %	0.02 %
Residential real estate	0.02	0.00	0.00	0.00	0.00
Installment	0.03	0.04	0.03	0.01	0.01
Credit cards and personal credit lines	0.01	(0.01)	0.03	0.00	0.01

Total ratio of net charge-offs	0.42	%	0.43	%	0.21	%	0.08	%	0.04	%
Ratio of allowance for loan losses to nonperforming assets	101.55	%	84.23	%	160.27	%	101.67	%	169.87	%

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ANALYSIS OF LOAN PORTFOLIO (cont.)
Allocation of Allowance for Loan Losses
(in thousands of dollars)

The following is a summary of the allocation for loan losses as of December 31, 2009, 2008, 2007, 2006 and 2005.

	2009		2008		2007	
	Allowance For Loan Losses	Loans as Percentage of Gross Loans	Allowance For Loan Losses	Loans as Percentage of Gross Loans	Allowance For Loan Losses	Loans as Percentage of Gross Loans
Allocated allowance for loan losses:						
Commercial	$28,014	84.39 %	$15,738	83.61 %	$13,659	81.42 %
Residential real estate	365	4.73	292	6.39	571	8.15
Installment	453	2.58	384	2.79	421	3.23
Credit cards and personal credit lines	538	8.30	996	7.21	828	7.20
Total allocated allowance for loan losses	29,370	100.00 %	17,410	100.00 %	15,479	100.00 %
Unallocated allowance for loan losses	2,703		1,450		322	
Total allowance for loan losses	$32,073		$18,860		$15,801	

	2006		2005	
	Allowance For Loan Losses	Loans as Percentage of Gross Loans	Allowance For Loan Losses	Loans as Percentage of Gross Loans
Allocated allowance for loan losses:				
Commercial	$12,185	80.24 %	$10,870	80.46 %
Residential real estate	389	8.07	187	6.24
Installment	690	6.20	509	5.67
Credit cards and personal credit lines	561	5.49	688	7.63
Total allocated allowance for loan losses	13,825	100.00 %	12,254	100.00 %
Unallocated allowance for loan losses	638		520	
Total allowance for loan losses	$14,463		$12,774	

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ANALYSIS OF DEPOSITS
(in thousands of dollars)

The average daily deposits for the years ended December 31, 2009, 2008 and 2007, and the average rates paid on those deposits are summarized in the following table:

	2009 Average Daily Balance	2009 Average Rate Paid	2008 Average Daily Balance	2008 Average Rate Paid	2007 Average Daily Balance	2007 Average Rate Paid
Demand deposits	$229,009	0.00 %	$219,762	0.00 %	$226,484	0.00 %
Savings and transaction accounts:						
Regular savings	70,202	0.14	64,877	0.10	67,104	0.20
Interest bearing checking	572,539	1.01	495,057	2.02	425,753	3.49
Time deposits:						
Deposits of $100,000 or more	638,956	1.72	528,316	3.90	462,056	5.27
Other time deposits	359,526	4.27	329,783	4.22	295,328	4.84
Total deposits	$1,870,232	1.72 %	$1,637,795	2.72 %	$1,476,725	3.63 %

As of December 31, 2009, time certificates of deposit will mature as follows:

	$100,000 or more	% of Total	Other	% of Total
Within three months	$147,136	27.31 %	$61,639	18.80 %
Over three months, within six months	82,596	15.33	71,485	21.80
Over six months, within twelve months	206,038	38.24	119,928	36.56
Over twelve months	103,044	19.12	74,897	22.84
Total time certificates of deposit	$538,814	100.00 %	$327,949	100.00 %

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QUALITATIVE MARKET RISK DISCLOSURE

Management’s market risk disclosure appears under the caption “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in Item 7, below, and is incorporated herein by reference in response to this item. The Company’s primary market risk exposure is interest rate risk. The Company does not have a material exposure to foreign currency exchange rate risk, does not own any material derivative financial instruments and does not maintain a trading portfolio.

RETURN ON EQUITY AND OTHER RATIOS

The rates of return on average daily assets and stockholders' equity, the dividend payout ratio, and the average daily stockholders' equity to average daily assets for the years ended December 31, 2009, 2008 and 2007 were as follows:

	2009		2008		2007	
Percent of net income to:						
Average daily total assets	0.78	%	0.91	%	1.04	%
Average daily stockholders' equity	8.94	%	13.04	%	13.94	%
Percentage of dividends declared per common share to basic earnings per weighted average number of common shares outstanding (12,851,845 shares in 2009, 12,271,927 shares in 2008 and 12,188,594 shares in 2007)	48.82	%	37.58	%	34.49	%
Percentage of average daily stockholders' equity to average daily total assets	8.68	%	6.96	%	7.49	%

Cash dividends were declared on April 14, July 14, October 13, 2009 and January 12, 2010 for each quarter of 2009, April 8, July 8, October 14, 2008 and January 13, 2009 for each quarter of 2008 and April 10, July 10 and October 9, 2007 and January 8, 2008 for each quarter of 2007.

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SHORT-TERM BORROWINGS
(in thousands of dollars)

The following is a schedule, at the end of the year indicated, of statistical information relating to securities sold under agreement to repurchase maturing within one year and secured by either U.S. Government agency securities or mortgage-backed securities classified as other debt securities and other short-term borrowings maturing within one year. There were no other categories of short-term borrowings for which the average balance outstanding during the period was 30 percent or more of stockholders' equity at the end of each period.

	2009		2008		2007	
Outstanding at year end:						
Federal funds purchased	$9,600		$19,000		$70,010	
Securities sold under agreements to repurchase	$127,118		$137,769		$154,913	
Other short-term borrowings	$215,000		$45,000		$90,000	
Approximate average interest rate at year end:						
Federal funds purchased	0.50	%	0.50	%	4.07	%
Securities sold under agreements to repurchase	0.42	%	0.43	%	3.20	%
Other short-term borrowings	0.38	%	0.65	%	4.31	%
Highest amount outstanding as of any month end during the year:						
Federal funds purchased	$94,300		$126,700		$96,850	
Securities sold under agreements to repurchase	$133,072		$175,427		$154,913	
Other short-term borrowings	$220,000		$163,700		$90,000	
Approximate average outstanding during the year:						
Federal funds purchased	$25,195		$50,171		$22,950	
Securities sold under agreements to repurchase	$125,195		$153,363		$121,372	
Other short-term borrowings	$119,849		$73,981		$32,247	
Approximate average interest rate during the year:						
Federal funds purchased	0.56	%	2.53	%	5.33	%
Securities sold under agreements to repurchase	0.46	%	1.85	%	3.52	%
Other short-term borrowings	0.39	%	2.09	%	5.09	%

Securities sold under agreements to repurchase include fixed-rate, term transactions initiated by the Bank, as well as corporate sweep accounts. Other short-term borrowings consist of Federal Home Loan Bank advances and Federal Reserve TAF borrowings.

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ITEM 1a. RISK FACTORS

In addition to the other information in this Annual Report on Form 10-K, shareholders or prospective investors should carefully consider the following risk factors:

A continued downturn in the economy, particularly in Northern Indiana, where our business is primarily conducted, could have an adverse effect on our business, results of operations and financial condition.

We operate branch offices in four geographical markets concentrated in Northern Indiana and a loan production office in central Indiana located in Indianapolis. Our most mature market, the South Region, includes Kosciusko County and portions of contiguous counties. The Bank was founded in this market in 1872. Warsaw is this region's primary city. The Bank entered the North Region in 1990, which includes portions of Elkhart and St. Joseph counties. This region includes the cities of Elkhart and South Bend. The Central Region includes portions of Elkhart County and contiguous counties and is anchored by the city of Goshen. The North and Central regions represent relatively mature markets with nearly 20 years of business activity. We entered the East Region in 1999, which includes Allen and DeKalb counties. Fort Wayne represents the primary city in this market. We have experienced rapid commercial loan growth in this market over the past 10 years. We entered the Indianapolis market in 2006 with the opening of a loan production office in Marion County.

Our success depends upon the business activity, population, income levels, deposits and real estate activity in these markets. Although our customers' business and financial interests may extend well beyond these market areas, adverse economic conditions that affect these market areas could reduce our growth rate, affect the ability of our customers to repay their loans to us and generally affect our financial condition and results of operations.

In late 2007 and all of 2008 and 2009, the United States economy experienced a severe downturn. Certain areas of our geographical markets have seen notably worse economic conditions than those suffered by the country at-large. As reported for November 2009, the 13 counties in which we operate had unemployment rates between 9.5% and 14.5%. In particular, Elkhart County has suffered from adverse business and economic conditions that have resulted in a county-wide level of unemployment of approximately 14.5%, which is well above the national average of 9.6%. A continued downturn in economic conditions, particularly within our primary market areas in Northern Indiana, could result in a decrease in demand for our products and services, an increase in loan delinquencies and defaults and high or increased levels of problem assets and foreclosures. Moreover, because of our geographic concentration, we are less able than other regional or national financial institutions to diversify our credit risks across multiple markets.

Difficult economic and market conditions have adversely affected our industry.

Dramatic declines in the housing market, with decreasing home prices and increasing delinquencies and foreclosures, have negatively impacted the credit performance of mortgage and commercial real estate loans and resulted in significant write-downs of assets by many financial institutions across the United States. General downward economic trends, reduced availability of commercial credit and increasing unemployment have negatively impacted the credit performance of commercial and consumer credit, resulting in additional write-downs. Concerns over the stability of the financial markets and the economy have resulted in decreased lending by many financial institutions to their customers and to each other. This market turmoil and tightening of credit has led to increased commercial and consumer deficiencies, lack of customer confidence, increased market volatility and widespread reductions in general business activity. Financial institutions have also generally experienced decreased access to deposits and borrowings. The resulting economic pressure on consumers and businesses and the lack of confidence in the financial markets may adversely affect our business, results of operations and financial condition. A worsening of these conditions would likely exacerbate the adverse effects of these difficult market conditions on us and others in the financial institutions industry. In particular, we may face the following risks in connection with these events:

- we potentially face increased regulation of our industry and compliance with such regulation may increase our costs and limit our ability to pursue business opportunities;

  - customer demand for loans secured by real estate could be reduced due to weaker economic conditions, an increase in unemployment, a decrease in real estate values or an increase in interest rates;

- the process we use to estimate losses inherent in our credit exposure requires difficult, subjective and complex judgments, including forecasts of economic conditions and how these economic conditions might impair the ability of our borrowers to repay their loans. The level of uncertainty concerning economic conditions may adversely affect the accuracy of our estimates which may, in turn, impact the reliability of the process;

- the value of the portfolio of investment securities that we hold may be adversely affected; and
- we may be required to pay significantly higher FDIC premiums because market developments have significantly depleted the insurance fund of the FDIC and reduced the ratio of reserves to insured deposits.

We must effectively manage our credit risk.

There are risks inherent in making any loan, including risks inherent in dealing with individual borrowers, risks of nonpayment, risks resulting from uncertainties as to the future value of collateral and risks resulting from changes in economic and industry conditions. We attempt to minimize our credit risk through prudent loan application approval procedures, careful monitoring of the concentration of our loans within specific industries, a centralized credit administration department and periodic independent reviews of outstanding loans by our loan review department. However, we cannot make assurances that such approval and monitoring procedures will reduce these credit risks.

The majority of the Bank’s loan portfolio is invested in commercial and commercial real estate loans. The Bank focuses on traditional commercial and industrial lending but is also involved in commercial real estate activity in its markets. In general, commercial loans represent higher dollar volumes to fewer customers. As a result, we may assume greater lending risks than other community banking-type financial institutions that have a lesser concentration of such loans and are more retail oriented.

Commercial and industrial and agri-business loans make up a significant portion of our loan portfolio.

Commercial and industrial and agri-business loans were $899.8 million, or approximately 44.7% of our total loan portfolio, as of December 31, 2009. Our commercial loans are primarily made based on the identified cash flow of the borrower and secondarily on the underlying collateral provided by the borrower. Most often, this collateral is accounts receivable, inventory, machinery or real estate. Credit support provided by the borrower for most of these loans and the probability of repayment is based on the liquidation of the pledged collateral and enforcement of a personal guarantee, if any exists. Whenever possible, we require a personal guarantee on commercial loans. As a result, 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. The collateral securing other loans may depreciate over time, may be difficult to appraise and may fluctuate in value based on the success of the business.

Our loan portfolio includes commercial real estate loans, which involve risks specific to real estate value.

Commercial real estate loans were $799.7 million, or approximately 39.7% of our total loan portfolio, as of December 31, 2009. The market value of real estate can fluctuate significantly in a short period of time as a result of market conditions in the geographic area in which the real estate is located. Although a significant portion of such loans are secured by real estate as a secondary form of collateral, continued adverse developments affecting real estate values in one or more of our markets could increase the credit risk associated with our loan portfolio. Additionally, real estate lending typically involves higher loan principal amounts and the repayment of the loans generally is dependent, in large part, on sufficient income from the properties securing the loans to cover operating expenses and debt service. Economic events or governmental regulations outside of the control of the borrower or lender could negatively impact the future cash flow and market values of the affected properties.

If the loans that are collateralized by real estate become troubled and the value of the real estate has been significantly impaired, then we may not be able to recover the full contractual amount of principal and interest that we anticipated at the time of originating the loan, which could cause us to increase our provision for loan losses and adversely affect our operating results and financial condition.

Our consumer loans generally have a higher degree of risk of default than our other loans.

At December 31, 2009, consumer loans totaled $57.5 million, or 2.9% of our total loan and lease portfolio. Consumer loans typically have shorter terms and lower balances with higher yields as compared to one-to-four

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family residential loans, but generally carry higher risks of default. Consumer loan collections are dependent on the borrower's continuing financial stability, and thus are more likely to be affected by adverse personal circumstances. Furthermore, the application of various federal and state laws, including bankruptcy and insolvency laws, may limit the amount which can be recovered on these loans.

Our continued pace of growth may require us to raise additional capital in the future, but that capital may not be available when it is needed.

We are required by federal and state regulatory authorities to maintain adequate levels of capital to support our operations. In February 2009, we accepted a capital investment of $56.0 million under the U.S. Treasury's Capital Purchase Program, and in November 2009 we raised $57.9 million in a public offering of common stock to further strengthen our capital position. However, we may at some point need to raise additional capital to support our continued growth. Our ability to raise additional capital, if needed, will depend on conditions in the capital markets at that time, which are outside our control, and on our financial performance. Accordingly, we cannot make assurances of our ability to raise additional capital, if needed, on terms acceptable to us. If we cannot raise additional capital when needed, our ability to further expand our operations through internal growth or acquisitions could be materially impaired.

Interest rates and other conditions impact our results of operations.

Our profitability is significantly driven by the spread between the interest rates earned on investments and loans and the interest rates paid on deposits and other interest-bearing liabilities. Like most banking institutions, our net interest spread and margin will be affected by general economic conditions and other factors, including fiscal and monetary policies of the federal government, that influence market interest rates and our ability to respond to changes in such rates. At any given time, our assets and liabilities will be such that they are affected differently by a given change in interest rates. As a result, an increase or decrease in rates, the length of loan terms or the mix of adjustable and fixed rate loans in our portfolio could have a positive or negative effect on our net income, capital and liquidity. We measure interest rate risk under various rate scenarios and using specific criteria and assumptions. Although we believe our current level of interest rate sensitivity is reasonable and effectively managed, significant fluctuations in interest rates may have an adverse effect on our business, results of operations and financial condition.

Our allowance for loan losses may prove to be insufficient to absorb potential losses in our loan portfolio.

We determined our allowance for loan losses pursuant to our established guidelines and practices and maintained a level considered adequate by management to absorb loan losses that are inherent in the portfolio. The amount of future loan losses is susceptible to changes in economic, operating and other conditions (in our markets as well as the United States), including changes in interest rates, which may be beyond our control, and such losses may exceed current estimates. At December 31, 2009, our allowance for loan losses as a percentage of total loans was 1.59% and as a percentage of total nonperforming loans was 105%. Because of the nature of our loan portfolio and our concentration in commercial and industrial loans, which tend to be larger loans, the movement of a small number of loans to nonperforming status can have a significant impact on these ratios. Although management believes that the allowance for loan losses is adequate to absorb probable incurred losses on any existing loans, we cannot predict loan losses with certainty, and we cannot assure you that our allowance for loan losses will prove sufficient to cover actual loan losses in the future. Loan losses in excess of our reserves may adversely affect our business, results of operations and financial condition.

Liquidity risks could affect operations and jeopardize our business, results of operations and financial condition.

Liquidity is essential to our business. An inability to raise funds through deposits, borrowings, the sale of loans and other sources could have a substantial negative effect on our liquidity. Our primary sources of funds consist of cash from operations, investment maturities and sales and deposits. Additional liquidity is provided by brokered deposits, CDARS deposits, repurchase agreements and our participation in the Federal Reserve Bank's Term Auction Facility, as well as the ability to borrow from the Federal Reserve Bank and the Federal Home Loan Bank. However, the Federal Reserve Bank's Term Auction Facility will no longer be available after March 8, 2010. Our access to funding sources in amounts adequate to finance or capitalize our activities or on terms that are acceptable to us could be impaired by factors that affect us directly or the financial services industry or economy in general, such as further disruptions in the financial markets or negative views and expectations about the prospects for the financial services industry.

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Since late 2007, and particularly during the second half of 2008 and much of 2009, the financial services industry and the credit markets generally have been materially and adversely affected by significant declines in asset values and by a lack of liquidity. The liquidity issues have been particularly acute for regional and community banks, as many of the larger financial institutions have significantly curtailed their lending to regional and community banks to reduce their exposure to the risks of other banks. In addition, many of the larger correspondent lenders have reduced or even eliminated federal funds lines for their correspondent customers. Furthermore, regional and community banks generally have less access to the capital markets than do the national and super-regional banks because of their smaller size and limited analyst coverage. Any decline in available funding could adversely impact our ability to originate loans, invest in securities, meet our expenses, pay dividends to our shareholders, or fulfill obligations such as repaying our borrowings or meeting deposit withdrawal demands, any of which could have a material adverse impact on our liquidity, business, results of operations and financial condition.

In addition, approximately 20% of our deposits are concentrated in public funds from a small number of municipalities and government agencies. Public deposits can be cyclical in nature and are often reduced in June and December of each year. If these government entities withdraw their deposits at inopportune times, or if we lose one or more of these deposit customers, the Bank would need to find a replacement source of liquidity for the funds withdrawn. If the Bank is unable to find a replacement source of liquidity, the Bank’s liquidity could be adversely affected.

Declines in asset values may result in impairment charges and adversely affect the value of our investments, financial performance and capital.

We maintain an investment portfolio that includes, but is not limited to, mortgage-backed securities. The market value of investments in our portfolio has become increasingly volatile over the past year. The market value of investments may be affected by factors other than the underlying performance of the servicer of the securities or the mortgages underlying the securities, such as ratings downgrades, adverse changes in the business climate and a lack of liquidity in the secondary market for certain investment securities. On a monthly basis, we evaluate investments and other assets for impairment indicators. We may be required to record additional impairment charges if our investments suffer a decline in value that is considered other-than-temporary. If we determine that a significant impairment has occurred, we would be required to charge against earnings the credit-related portion of the other-than-temporary impairment, which could have a material adverse effect on our results of operations in the periods in which the write-offs occur.

We may experience difficulties in managing our growth, and our growth strategy involves risks that may negatively impact our net income.

Although we do not have any current plans to do so, we may expand into additional communities or attempt to strengthen our position in our current markets through opportunistic acquisitions of all or part of other financial institutions, including FDIC-assisted transactions, or by opening new branches. To the extent that we undertake acquisitions or new branch openings, we are likely to experience the effects of higher operating expenses relative to operating income from the new operations, which may have an adverse effect on our levels of reported net income, return on average equity and return on average assets. Other effects of engaging in such growth strategies may include potential diversion of our management’s time and attention and general disruption to our business.

To the extent that we grow through acquisitions and branch openings, we cannot assure you that we will be able to adequately and profitably manage this growth. Acquiring other banks and businesses will involve similar risks to those commonly associated with branching, but may also involve additional risks, including:

- potential exposure to unknown or contingent liabilities of banks and businesses we acquire;

- exposure to potential asset quality issues of the acquired bank or related business;
- difficulty and expense of integrating the operations and personnel of banks and businesses we acquire; and
- the possible loss of key employees and customers of the banks and businesses we acquire.

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Attractive acquisition opportunities may not be available to us in the future.

We expect that other banking and financial service companies, many of which have significantly greater resources than us, will compete with us in acquiring other financial institutions if we pursue such acquisitions. This competition could increase prices for potential acquisitions that we believe are attractive. Also, acquisitions are subject to various regulatory approvals. If we fail to receive the appropriate regulatory approvals, we will not be able to consummate an acquisition that we believe is in our best interests. Among other things, our regulators consider our capital, liquidity, profitability, regulatory compliance and levels of goodwill and intangibles when considering acquisition and expansion proposals. Any acquisition could be dilutive to our earnings and shareholders' equity per share of our common stock.

Higher FDIC deposit insurance premiums and assessments could adversely affect our financial condition.

FDIC insurance premiums increased substantially in 2009, and we expect to pay higher FDIC premiums in the future. Bank failures have significantly depleted the FDIC's Deposit Insurance Fund and reduced the Deposit Insurance Fund's ratio of reserves to insured deposits. The FDIC adopted a revised risk-based deposit insurance assessment schedule on February 27, 2009, which raised deposit insurance premiums. On May 22, 2009, the FDIC also implemented a special assessment equal to five basis points of each insured depository institution's assets minus Tier 1 capital as of June 30, 2009, but no more than 10 basis points times the institution's assessment base for the second quarter of 2009, to be collected on September 30, 2009. Additional special assessments may be imposed by the FDIC for future periods. On November 12, 2009, the FDIC adopted a uniform three basis-point increase in assessment rates, which is effective on January 1, 2011. Also, on November 12, 2009, the FDIC adopted a rule that required the Bank to prepay its quarterly risk-based assessments for the fourth quarter of 2009 and for all of 2010, 2011 and 2012, along with their risk-based assessment for the third quarter of 2009.

We participate in the FDIC's Temporary Liquidity Guarantee Program, or TLG, for noninterest-bearing transaction deposit accounts. Banks that participate in the TLG's noninterest-bearing transaction account guarantee will pay the FDIC an annual assessment of 10 basis points on the amounts in such accounts above the amounts covered by FDIC deposit insurance. To the extent that these TLG assessments are insufficient to cover any loss or expenses arising from the TLG program, the FDIC is authorized to impose an emergency special assessment on all FDIC-insured depository institutions. The FDIC has authority to impose charges for the TLG program upon depository institution holding companies, as well. The TLG was scheduled to end December 31, 2009, but the FDIC has extended it to June 30, 2010 at an increased charge of 15 to 25 basis points beginning January 1, 2010, depending on the depository institution's risk assessment category rating assigned with respect to regular FDIC assessments if the institution elects to remain in the TLG. These changes have caused the premiums and TLG assessments charged by the FDIC to increase. These actions have significantly increased our noninterest expense in 2009 and are expected to increase our costs for the foreseeable future.

We face intense competition in all phases of our business from other banks and financial institutions.

The banking and financial services business in our market is highly competitive. Our competitors include large regional banks, local community banks, savings and loan associations, securities and brokerage companies, mortgage companies, insurance companies, finance companies, money market mutual funds, credit unions, farm credit services and other nonbank financial service providers. Many of these competitors are not subject to the same regulatory restrictions as we are and are able to provide customers with a feasible alternative to traditional banking services.

Increased competition in our market may also result in a decrease in the amounts of our loans and deposits, reduced spreads between loan rates and deposit rates or loan terms that are more favorable to the borrower. Any of these results could have a material adverse effect on our ability to grow and remain profitable. If increased competition causes us to significantly discount the interest rates we offer on loans or increase the amount we pay on deposits, our net interest income could be adversely impacted. If increased competition causes us to relax our underwriting standards, we could be exposed to higher losses from lending activities. Additionally, many of our competitors are much larger in total assets and capitalization, have greater access to capital markets, possess larger lending limits and offer a broader range of financial services than we can offer.

Government regulation can result in limitations on our operations.

We operate in a highly regulated environment and are subject to supervision and regulation by a number of governmental regulatory agencies, including the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, and the Indiana Department of Financial Institutions. Regulations adopted by these agencies, which are generally intended to provide protection for depositors and customers rather than for the benefit of shareholders, govern a comprehensive range of matters relating to ownership and control of our shares, our acquisition of other companies and businesses, permissible activities for us to engage in, maintenance of adequate capital levels and other aspects of our operations. These bank regulators possess broad authority to prevent or remedy unsafe or unsound practices or violations of law. The laws and regulations applicable to the banking industry could change at any time and we cannot predict the effects of these changes on our business and profitability. Increased regulation could increase our cost of compliance and adversely affect profitability. For example, new legislation or regulation may limit the manner in which we may conduct our business, including our ability to offer new products, obtain financing, attract deposits, make loans and achieve satisfactory interest spreads.

We cannot predict the effect on our operations of recent legislative and regulatory initiatives that were enacted in response to the ongoing financial crisis.

United States federal, state and foreign governments have taken or are considering extraordinary actions in an attempt to deal with the worldwide financial crisis. To the extent adopted, many of these actions have been in effect for only a limited time, and have produced limited or no relief to the capital, credit and real estate markets. There is no assurance that these actions or other actions under consideration will ultimately be successful.

In the United States, the federal government has adopted the Emergency Economic Stabilization Act of 2008 and the American Recovery and Reinvestment Act of 2009. With authority granted under these laws, the U.S. Treasury has proposed a financial stability plan that is intended to:

- invest in financial institutions and purchase troubled assets and mortgages from financial institutions for the purpose of stabilizing and providing liquidity to the United States financial markets;

- temporarily increase the limit on FDIC deposit insurance coverage to $250,000 per depositor through December 31, 2009 (which was extended to December 31, 2013 under the Helping Families Save Their Homes Act of 2009); and

- provide for various forms of economic stimulus, including to assist homeowners restructure and lower mortgage payments on qualifying loans.

Numerous other actions have been taken by the United States Congress, the Federal Reserve, the U.S. Treasury, the FDIC, the SEC and others to address the liquidity and credit crisis that has followed the sub-prime mortgage crisis that commenced in 2007, including the financial stability plan adopted by the U.S. Treasury. In addition, President Obama recently announced a financial regulatory reform proposal, and the House and Senate are expected to consider competing proposals over the coming years.

There can be no assurance that the financial stability plan proposed by the U.S. Treasury, the other proposals under consideration or any other legislative or regulatory initiatives will be effective at dealing with the ongoing economic crisis and improving economic conditions globally, nationally or in our markets, or that the measures adopted will not have adverse consequences. The terms and costs of these activities, or the failure of these actions to help stabilize the financial markets, asset prices, and market liquidity, and a continuation or worsening of current financial market and economic conditions, could materially and adversely affect our business, results of operations, financial condition and the trading prices of our securities.

Negative developments in the financial industry and the credit markets may subject us to additional regulation.

As a result of ongoing challenges facing the United States economy, the potential exists for new laws and regulations regarding lending and funding practices and liquidity standards to be promulgated, and bank regulatory agencies are expected to be active in responding to concerns and trends identified in examinations, including the expected issuance of many formal enforcement orders. Negative developments in the financial industry and credit markets, and the impact of new legislation in response to those developments, may negatively impact our operations by restricting our business operations, including our ability to originate or sell loans, and may adversely impact our financial performance.

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Changes in future rules applicable to TARP recipients could adversely affect our business, results of operations and financial condition.

On February 27, 2009, we issued $56.0 million of our Fixed Rate Cumulative Perpetual Preferred Stock, Series A, or the Series A Preferred Stock, to the U.S. Treasury pursuant to the TARP Capital Purchase Program. The rules and policies applicable to recipients of capital under the TARP Capital Purchase Program continue to evolve and their scope, timing and effect cannot be predicted. Any redemption of the securities sold to the U.S. Treasury to avoid these restrictions would require prior Federal Reserve and U.S. Treasury approval. Based on guidelines recently issued by the Federal Reserve, institutions seeking to redeem TARP Capital Purchase Program preferred stock must demonstrate an ability to access the long-term debt markets without reliance on the FDIC's TLG, successfully demonstrate access to public equity markets and meet a number of additional requirements and considerations before such institutions can redeem any securities sold to the U.S. Treasury.

Our ability to attract and retain management and key personnel may affect future growth and earnings, and the recent economic stimulus legislation imposes new compensation restrictions that could adversely affect our ability to do so.

Much of our success and growth has been influenced strongly by our ability to attract and retain management experienced in banking and financial services and familiar with the communities in our market areas. Our ability to retain the executive officers, management teams, branch managers and loan officers of our bank subsidiary will continue to be important to the successful implementation of our strategy. It is also critical, as we grow, to be able to attract and retain qualified additional management and loan officers with the appropriate level of experience and knowledge about our market areas to implement our community-based operating strategy. The unexpected loss of services of any key management personnel, or the inability to recruit and retain qualified personnel in the future, could have an adverse effect on our business, results of operations and financial condition.

The American Recovery and Reinvestment Act of 2009 that was signed into law in February 2009 includes extensive new restrictions on our ability to pay retention awards, bonuses and other incentive compensation during the period in which we have any outstanding securities held by the U.S. Treasury that were issued under the TARP Capital Purchase Program. Many of the restrictions may not be limited to our senior executives and could cover other employees whose contributions to revenue and performance can be significant. The limitations may adversely affect our ability to recruit and retain these key employees in addition to our senior executive officers, especially if we are competing for talent against institutions that are not subject to the same restrictions. The Federal Reserve, and perhaps the FDIC, are contemplating proposed rules governing the compensation practices of financial institutions and these rules, if adopted, may make it more difficult to attract and retain the people we need to operate our businesses and limit our ability to promote our objectives through our compensation and incentive programs.

We have a continuing need for technological change and we may not have the resources to effectively implement new technology.

The financial services industry is constantly undergoing rapid technological changes with frequent introductions of new technology-driven products and services. In addition to better serving customers, the effective use of technology increases efficiency and enables financial institutions to reduce costs. Our future success will depend in part upon our ability to address the needs of our customers by using technology to provide products and services that will satisfy customer demands for convenience as well as to create additional efficiencies in our operations as we continue to grow and expand our market areas. Many of our larger competitors have substantially greater resources to invest in technological improvements. As a result, they may be able to offer additional or superior products to those that we will be able to offer, which would put us at a competitive disadvantage. Accordingly, we cannot provide assurances that we will be able to effectively implement new technology-driven products and services or be successful in marketing such products and services to our customers.

System failure or breaches of our network security could subject us to increased operating costs as well as litigation and other liabilities.

The computer systems and network infrastructure we use could be vulnerable to unforeseen problems. Our operations are dependent upon our ability to protect our computer equipment against damage from physical theft, fire, power loss, telecommunications failure or a similar catastrophic event, as well as from security breaches, denial of service attacks, viruses, worms and other disruptive problems caused by hackers. Any damage or failure that causes an interruption in our operations could have a material adverse effect on our financial condition and results of operations. Computer break-ins, phishing and other disruptions could also jeopardize the security of information stored in and transmitted through our computer systems and network infrastructure, which may result in significant liability to us and may cause existing and potential customers to refrain from doing business with us. Although we,

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with the help of third-party service providers, intend to continue to implement security technology and establish operational procedures to prevent such damage, there can be no assurance that these security measures will be successful. In addition, advances in computer capabilities, new discoveries in the field of cryptography or other developments could result in a compromise or breach of the algorithms we and our third-party service providers use to encrypt and protect customer transaction data. A failure of such security measures could have a material adverse effect on our financial condition and results of operations.

We are subject to certain operational risks, including, but not limited to, customer or employee fraud and data processing system failures and errors.

Employee errors and misconduct could subject us to financial losses or regulatory sanctions and seriously harm our reputation. Misconduct by our employees could include hiding unauthorized activities from us, improper or unauthorized activities on behalf of our customers or improper use of confidential information. It is not always possible to prevent employee errors and misconduct, and the precautions we take to prevent and detect this activity may not be effective in all cases. Employee errors could also subject us to financial claims for negligence.

We maintain a system of internal controls and insurance coverage to mitigate operational risks, including data processing system failures and errors and customer or employee fraud. Should our internal controls fail to prevent or detect an occurrence, or if any resulting loss is not insured or exceeds applicable insurance limits, it could have a material adverse effect on our business, results of operations and financial condition.

We may be subject to a higher consolidated effective tax rate if there is a change in tax laws or if LCB Funding, Inc. fails to qualify as a real estate investment trust.

The Bank holds certain investment securities in its wholly-owned subsidiary LCB Investments II, Inc., which is incorporated in Nevada. Pursuant to the State of Indiana’s current tax laws and regulations, we are not subject to Indiana income tax for income earned through that subsidiary. If there are changes in tax laws or interpretations thereof requiring us to pay state taxes for income generated by LCB Investments II, Inc., the resulting tax consequences could increase our effective tax rate or cause us to have a tax liability for prior years.

The Bank also holds certain commercial real estate loans, residential real estate loans and other loans in a real estate investment trust through LCB Investments II, Inc. Qualification as a real estate investment trust involves application of specific provisions of the Internal Revenue Code relating to various asset tests. If LCB Funding, Inc. fails to meet any of the required provisions for real estate investment trusts, or there are changes in tax laws or interpretations thereof, it could no longer qualify as a real estate investment trust and the resulting tax consequences would increase our effective tax rate or cause us to have a tax liability for prior years.

ITEM 1b. UNRESOLVED STAFF COMMENTS

We have no unresolved SEC staff comments.

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ITEM 2. PROPERTIES

The Company conducts its operations from the following branch locations:

Location			
Main/Headquarters	202 East Center St.	Warsaw	IN
Warsaw Drive-up	East Center St.	Warsaw	IN
Akron	102 East Rochester	Akron	IN
Argos	100 North Michigan	Argos	IN
Auburn	1220 East 7th St.	Auburn	IN
Bremen	1600 State Road 331	Bremen	IN
Columbia City	601 Countryside Dr.	Columbia City	IN
Concord	4202 Elkhart Rd.	Goshen	IN
Cromwell	111 North Jefferson St.	Cromwell	IN
Elkhart Beardsley	864 East Beardsley St.	Elkhart	IN
Elkhart East	22050 State Road 120	Elkhart	IN
Elkhart Hubbard Hill	58404 State Road 19	Elkhart	IN
Elkhart Northwest	1208 North Nappanee St.	Elkhart	IN
Fort Wayne North	302 East DuPont Rd.	Fort Wayne	IN
Fort Wayne Northeast	10411 Maysville Rd.	Fort Wayne	IN
Fort Wayne Southwest	10429 Illinois Rd.	Fort Wayne	IN
Fort Wayne Jefferson Blvd	6851 West Jefferson Blvd.	Fort Wayne	IN
Goshen Downtown	102 North Main St.	Goshen	IN
Goshen South	2513 South Main St.	Goshen	IN
Granger	12830 State Road 23	Granger	IN
Huntington	1501 North Jefferson St.	Huntington	IN
Kendallville East	631 Professional Way	Kendallville	IN
LaGrange	901 South Detroit	LaGrange	IN
Ligonier Downtown	222 South Cavin St.	Ligonier	IN
Ligonier South	1470 U.S. Highway 33 South	Ligonier	IN
Medaryville	Main St.	Medaryville	IN
Mentone	202 East Main St.	Mentone	IN
Middlebury	712 Wayne Ave.	Middlebury	IN
Milford	State Road 15 North	Milford	IN
Mishawaka	5015 North Main St.	Mishawaka	IN
Nappanee	202 West Market St.	Nappanee	IN
North Webster	644 North Main St.	North Webster	IN
Pierceton	202 South First St.	Pierceton	IN
Plymouth	862 East Jefferson St.	Plymouth	IN
Rochester	507 East 9th St.	Rochester	IN
Shipshewana	895 North Van Buren St.	Shipshewana	IN
Silver Lake	102 Main St.	Silver Lake	IN
South Bend Northwest	21113 Cleveland Rd.	South Bend	IN
Syracuse	502 South Huntington	Syracuse	IN
Warsaw East	3601 Commerce Dr.	Warsaw	IN
Warsaw North	420 Chevy Way	Warsaw	IN
Warsaw West	1221 West Lake St.	Warsaw	IN
Winona Lake	99 Chestnut St.	Winona Lake	IN

Winona Lake East	1324 Wooster Rd.	Winona Lake	IN

The Company leases from third parties the real estate and buildings for its Milford and Winona Lake East offices. In addition, the Company leases the real estate for its four freestanding ATMs. The Company also leases from a third party office space in Indianapolis, Indiana, for a loan production office. All the other branch facilities are owned by the Company. The Company also owns parking lots in downtown Warsaw for the use and convenience of Company employees and customers, as well as leasehold improvements, equipment, furniture and fixtures necessary to operate the banking facilities.

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In addition, the Company owns buildings at 110 South High St., Warsaw, Indiana, and 114-118 East Market St., Warsaw, Indiana, which it uses for various offices, a building at 113 East Market St., Warsaw, Indiana, which it uses for office and computer facilities, and a building at 109 South Buffalo St., Warsaw, Indiana, which it uses for training and development.

None of the Company's assets are the subject of any material encumbrances.

ITEM 3. LEGAL PROCEEDINGS

There are no material pending legal proceedings other than ordinary routine litigation incidental to the business to which the Company and the Bank are a party or of which any of their property is subject.

ITEM 4. RESERVED

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED SHAREHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

	4th Quarter	3rd Quarter	2nd Quarter	1st Quarter
2009				
Trading prices (per share)*				
Low	$16.35	$17.80	$17.10	$14.14
High	$22.24	$22.49	$21.04	$23.87
Dividends declared (per share)	$0.155	$0.155	$0.155	$0.155
2008				
Trading prices (per share)*				
Low	$14.93	$18.52	$19.00	$16.87
High	$24.10	$30.09	$25.00	$23.97
Dividends declared (per share)	$0.155	$0.155	$0.155	$0.140

* The trading ranges are the high and low prices as obtained from The Nasdaq Stock Market.

The common stock of the Company began being quoted on The Nasdaq Stock Market under the symbol LKFN in August, 1997. Currently, the Company's common stock is listed for trading on the Nasdaq Global Select market. On December 31, 2009, the Company had approximately 436 shareholders of record and estimates that it has approximately 2,300 shareholders in total.

The Company paid dividends as set forth in the table above. The Company’s ability to pay dividends to shareholders is largely dependent upon the dividends it receives from the Bank, and the Bank is subject to regulatory limitations on the amount of cash dividends it may pay. In addition, as a result of the Company's participation in the TARP Capital Purchase Program, the Company may not increase the quarterly dividends it pays on the Company's common stock above $0.155 per share for three years, without the consent of Treasury, unless Treasury no longer holds shares of the Series A Preferred Stock. See “Business – Supervision and Regulation – The Company – Dividend Payments” and “Business - Supervision and Regulation – The Bank – Dividend Payments” for a more detailed description of these limitations.

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The following table provides information about purchases by the Company and its affiliates during the quarter ended December 31, 2009 of equity securities that are registered by the Company pursuant to Section 12 of the Exchange Act:

ISSUER PURCHASES OF EQUITY SECURITIES

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number (or Appropriate Dollar Value) of Shares that May Yet Be Purchased Under the Plans or Programs
10/01/09-10/31/09	0	$0.00	0	$0.00
11/01/09-11/30/09	772	20.12	0	0.00
12/01/09-12/31/09	0	0.00	0	0.00
Total	772	$20.12	0	$0.00

The shares purchased during the periods were credited to the deferred share accounts of seven nonemployee directors under the Company's directors' deferred compensation plan.

STOCK PRICE PERFORMANCE GRAPH

The graph below compares the cumulative total return of the Company, the Nasdaq Market Index and a peer group index.

INDEX	2004	2005	2006	2007	2008	2009
Lakeland Financial Corporation	$100.00	$104.08	$134.46	$112.75	$132.28	$98.80
NASDAQ Market Index	100.00	101.37	111.03	121.92	72.49	104.31
Peer Group Index	100.00	100.58	114.89	83.98	64.15	45.63

* Assumes $100 invested on December 31, 2004 and dividends were reinvested.

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The peer group index is comprised of all financial institution holding companies in the United States with total assets as of December 31, 2009 between $1.0 billion and $3.0 billion dollars whose equity securities were traded on an exchange or national quotation service.

Lakeland Financial Peer Group
9/30/2009

Company	Institution Key	Ticker	State	Assets
Alliance Financial Corporation	100700	ALNC	NY	1,456,276
AmericanWest Bancorporation	100865	AWBC	WA	1,763,431
Ameris Bancorp	100594	ABCB	GA	2,207,475
Arrow Financial Corporation	100134	AROW	NY	1,836,283
Atlantic Southern Financial Group, Inc.	4093166	ASFN	GA	1,083,677
Bancorp Rhode Island, Inc.	4054977	BARI	RI	1,569,880
Bancorp, Inc.	4054569	TBBK	DE	2,041,034
BancTrust Financial Group, Inc.	100351	BTFG	AL	2,036,069
Bank of Florida Corporation	4047172	BOFL	FL	1,488,008
Bank of Granite Corporation	100304	GRAN	NC	1,009,669
Bank of Kentucky Financial Corporation	1024571	BKYF	KY	1,391,669
Bank of Marin Bancorp	4164467	BMRC	CA	1,126,529
Bank of the Ozarks, Inc.	1018441	OZRK	AR	2,889,686
Bar Harbor Bankshares	100824	BHB	ME	1,060,707
BNC Bancorp	4086131	BNCN	NC	1,704,645
Bryn Mawr Bank Corporation	100154	BMTC	PA	1,195,525
Cadence Financial Corporation	1018635	CADE	MS	1,767,699
Camden National Corporation	101149	CAC	ME	2,272,746
Capital Bank Corporation	4042314	CBKN	NC	1,734,950
Capital City Bank Group, Inc.	100774	CCBG	FL	2,491,937
Cardinal Financial Corporation	4019138	CFNL	VA	1,893,403
Cascade Bancorp	100589	CACB	OR	2,272,047
Cascade Financial Corporation	102173	CASB	WA	1,646,987
Cass Information Systems, Inc.	100886	CASS	MO	1,033,395
Center Bancorp, Inc.	100687	CNBC	NJ	1,349,516
Center Financial Corporation	4084856	CLFC	CA	2,201,842
CenterState Banks, Inc.	4053925	CSFL	FL	1,783,823
Centrue Financial Corporation	1021347	TRUE	MO	1,338,474
Century Bancorp, Inc.	100209	CNBKA	MA	2,051,247
Citizens & Northern Corporation	100693	CZNC	PA	1,283,378
City Bank	1009626	CTBK	WA	1,219,356
City Holding Company	100199	CHCO	WV	2,596,236
CNB Financial Corporation	100790	CCNE	PA	1,090,300
CoBiz Financial Inc.	1017371	COBZ	CO	2,537,665
Colony Bankcorp, Inc.	100882	CBAN	GA	1,290,891
Columbia Bancorp	1025077	CBBO	OR	1,057,717
Commonwealth Bankshares, Inc.	100912	CWBS	VA	1,145,184
Community Bankers Trust Corporation	4100717	BTC	VA	1,239,138

Crescent Banking Company	100005	CSNT	GA	1,030,472
Crescent Financial Corporation	4066238	CRFN	NC	1,063,703
Dearborn Bancorp, Inc.	1024255	DEAR	MI	1,042,337
Eagle Bancorp, Inc.	4002078	EGBN	MD	1,682,773
Eastern Virginia Bankshares, Inc.	1974273	EVBS	VA	1,105,727
Encore Bancshares, Inc.	4057668	EBTX	TX	1,600,720
Enterprise Bancorp, Inc.	1025202	EBTC	MA	1,287,427
Enterprise Financial Services Corp	1024631	EFSC	MO	2,518,625
EuroBancshares, Inc.	4086027	EUBK	PR	2,806,909
Farmers Capital Bank Corporation	100257	FFKT	KY	2,273,259

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Fidelity Southern Corporation	100845	LION	GA	1,912,394
Financial Institutions, Inc.	1016825	FISI	NY	2,138,205
First Bancorp, Inc.	1019988	FNLC	ME	1,331,842
First Business Financial Services, Inc.	1021886	FBIZ	WI	1,073,653
First California Financial Group, Inc.	100349	FCAL	CA	1,469,628
First Chester County Corporation	100793	FCEC	PA	1,306,681
First Citizens Banc Corp	100876	FCZA	OH	1,103,720
First Community Bancshares, Inc.	100792	FCBC	VA	2,298,341
First Financial Corporation	100502	THFF	IN	2,500,913
First Financial Service Corporation	101772	FFKY	KY	1,107,566
First M&F Corporation	1018386	FMFC	MS	1,676,469
First Mariner Bancorp	1024706	FMAR	MD	1,410,427
First of Long Island Corporation	100265	FLIC	NY	1,507,614
First Regional Bancorp	100282	FRGB	CA	2,175,019
First Security Group, Inc.	4050826	FSGI	TN	1,202,908
First State Bancorporation	100565	FSNM	NM	2,886,347
First United Corporation	100525	FUNC	MD	1,681,749
Firstbank Corporation	100768	FBMI	MI	1,429,810
FNB United Corp.	100805	FNBN	NC	2,193,906
German American Bancorp, Inc.	100551	GABC	IN	1,233,815
Great Florida Bank	4091674	GFLB	FL	1,716,557
Green Bankshares, Inc.	1019938	GRNB	TN	2,794,217
Guaranty Bancorp	4093621	GBNK	CO	2,057,378
Hampton Roads Bankshares, Inc.	4066242	HMPR	VA	2,938,994
Hawthorn Bancshares, Inc.	1023919	HWBK	MO	1,240,228
Heritage Commerce Corp	4019167	HTBK	CA	1,367,610
Heritage Financial Corporation	1024198	HFWA	WA	1,017,956
Home BancShares, Inc.	1022914	HOMB	AR	2,631,736
Horizon Bancorp	100750	HBNC	IN	1,321,224
Horizon Financial Corp.	1024822	HRZB	WA	1,300,100
Hudson Valley Holding Corp.	1016867	HUVL	NY	2,578,790
Independent Bank Corporation	100319	IBCP	MI	2,962,028
Indiana Community Bancorp	101857	INCB	IN	1,052,998
Intervest Bancshares Corporation	1023951	IBCA	NY	2,382,170
Lakeland Bancorp, Inc.	1022451	LBAI	NJ	2,769,463
Lakeland Financial Corporation	100608	LKFN	IN	2,469,882
LNB Bancorp, Inc.	100612	LNBB	OH	1,181,179
Macatawa Bank Corporation	4004314	MCBC	MI	1,981,772
MainSource Financial Group, Inc.	100513	MSFG	IN	2,934,326
MBT Financial Corp.	4056273	MBTF	MI	1,442,512
Mercantile Bancorp, Inc.	1018583	MBR	IL	1,685,805
Mercantile Bank Corporation	113567	MBWM	MI	2,017,350
Merchants Bancshares, Inc.	100353	MBVT	VT	1,405,994
Metro Bancorp, Inc.	4048256	METR	PA	2,086,495
MetroCorp Bancshares, Inc.	4039909	MCBI	TX	1,629,732
MidWestOne Financial Group, Inc.	1021746	MOFG	IA	1,529,676
NewBridge Bancorp	100346	NBBC	NC	2,009,544
Old Second Bancorp, Inc.	100625	OSBC	IL	2,699,094
Orrstown Financial Services, Inc.	100631	ORRF	PA	1,159,996
PAB Bankshares, Inc.	106981	PABK	GA	1,251,219

Pacific Continental Corporation	4049245	PCBK	OR	1,150,508
Pacific Mercantile Bancorp	4055039	PMBC	CA	1,110,533
Peapack-Gladstone Financial Corporation	1137117	PGC	NJ	1,487,679
Peoples Bancorp Inc.	100532	PEBO	OH	2,004,754
Peoples Bancorp of North Carolina, Inc.	4050385	PEBK	NC	1,041,231
Porter Bancorp, Inc.	1022071	PBIB	KY	1,728,762

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Preferred Bank	1023519	PFBC	CA	1,411,817
PremierWest Bancorp	4054224	PRWT	OR	1,715,550
Princeton National Bancorp, Inc.	100504	PNBC	IL	1,287,059
QCR Holdings, Inc.	1024092	QCRH	IL	1,749,304
Royal Bancshares of Pennsylvania, Inc.	100416	RBPAA	PA	1,361,810
S.Y. Bancorp, Inc.	100548	SYBT	KY	1,763,533
Savannah Bancorp, Inc.	100844	SAVB	GA	1,041,358
SCBT Financial Corporation	1019950	SCBT	SC	2,776,684
Seacoast Banking Corporation of Florida	100425	SBCF	FL	2,139,915
Shore Bancshares, Inc.	1027751	SHBI	MD	1,157,685
Sierra Bancorp	4064269	BSRR	CA	1,307,049
Simmons First National Corporation	100431	SFNC	AR	2,915,437
Smithtown Bancorp, Inc.	100654	SMTB	NY	2,670,257
Southern Community Financial Corporation	4072468	SCMF	NC	1,725,341
Southside Bancshares, Inc.	1021743	SBSI	TX	2,941,563
State Bancorp, Inc.	100446	STBC	NY	1,596,464
StellarOne Corporation	1032007	STEL	VA	2,982,264
Sterling Bancorp	100450	STL	NY	2,136,805
Suffolk Bancorp	100453	SUBK	NY	1,671,816
Summit Financial Group, Inc.	1021909	SMMF	WV	1,577,793
Tennessee Commerce Bancorp, Inc.	4056797	TNCC	TN	1,335,751
TIB Financial Corp.	108287	TIBB	FL	1,717,622
Tower Bancorp, Inc.	100663	TOBC	PA	1,378,936
TriCo Bancshares	100546	TCBK	CA	2,095,666
Union Bankshares Corporation	100575	UBSH	VA	2,583,284
Univest Corporation of Pennsylvania	100671	UVSP	PA	2,117,849
Virginia Commerce Bancorp, Inc.	4053565	VCBI	VA	2,734,112
VIST Financial Corp.	100598	VIST	PA	1,276,395
Wainwright Bank & Trust Company	100490	WAIN	MA	1,009,883
Washington Trust Bancorp, Inc.	100491	WASH	RI	2,888,065
West Bancorporation, Inc.	1021570	WTBA	IA	1,499,611
West Coast Bancorp	100183	WCBO	OR	2,653,357
Yadkin Valley Financial Corporation	4140013	YAVY	NC	2,051,672

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ITEM 6. SELECTED FINANCIAL DATA

	2009	2008	2007	2006	2005
	(in thousands except share and per share data)				
Interest income	$116,343	$118,484	$117,973	$105,551	$80,616
Interest expense	36,062	55,216	63,417	53,224	30,353
Net interest income	80,281	63,268	54,556	52,327	50,263
Provision for loan losses	21,202	10,207	4,298	2,644	2,480
Net interest income after provision for loan losses	59,079	53,061	50,258	49,683	47,783
Other noninterest income	20,547	22,236	19,844	18,668	16,771
Gain on sale of credit card portfolio	0	0	0	0	863
Gain on redemption of Visa shares	0	642	0	0	0
Mortgage banking income	1,695	411	309	194	521
Net securities gains (losses)	2	39	89	(68)	(69)
Noninterest expense	(53,475)	(47,481)	(42,923)	(40,242)	(38,432)
Income before income tax expense	27,848	28,908	27,577	28,235	27,437
Income tax expense	8,869	9,207	8,366	9,514	9,479
Net income	18,979	19,701	19,211	18,721	17,958
Dividends and accretion of discount on preferred stock	2,694	0	0	0	0
Net income available to common shareholders	$16,285	$19,701	$19,211	$18,721	$17,958
Basic weighted average common shares outstanding*	12,851,845	12,271,927	12,188,594	12,069,300	11,927,756
Basic earnings per common share*	$1.27	$1.61	$1.58	$1.55	$1.51
Diluted weighted average common shares outstanding*	12,952,444				