FIRST MID ILLINOIS BANCSHARES INC
Form 10-K
March 03, 2010

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

FORM 10-K

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2009

or

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from _____________ to ______________

Commission file number: 0-13368

FIRST MID-ILLINOIS BANCSHARES, INC.
(Exact name of Registrant as specified in its charter)

Delaware	37-1103704
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1515 Charleston Avenue, Mattoon, Illinois	61938
(Address of Principal Executive Offices)	(Zip Code)

(217) 234-7454
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:
NONE

Securities registered pursuant to Section 12(g) of the Act:
Common stock, par value $4.00 per share,
and related Common Stock Purchase Rights
(Title of class)

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. [ ] Yes [X] No

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. [ ] Yes [X] No

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes [X] No [ ]

Indicate by check mark 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 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, non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer [ ]	Accelerated filer [X]
Non-accelerated filer [ ] (Do not check if a smaller reporting company)	Smaller reporting company [ ]

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

The aggregate market value of the outstanding common stock, other than shares held by persons who may be deemed affiliates of the Registrant, as of the last business day of the Registrant's most recently completed second fiscal quarter was approximately $73,743,000. Determination of stock ownership by non-affiliates was made solely for the purpose of responding to this requirement and the Registrant is not bound by this determination for any other purpose.

As of March 3, 2010, 6,102,360 shares of the Registrant's common stock, $4.00 par value, were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Document	Into Form 10-K Part:
Portions of the Proxy Statement for 2010 Annual Meeting of Shareholders to be held on April 28, 2010	III

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PART I

ITEM 1.BUSINESS

Company and Subsidiaries

First Mid-Illinois Bancshares, Inc. (the "Company") is a financial holding company. The Company is engaged in the business of banking through its wholly owned subsidiary, First Mid-Illinois Bank & Trust, N.A. ("First Mid Bank"). The Company provides data processing services to affiliates through another wholly owned subsidiary, Mid-Illinois Data Services, Inc. ("MIDS"). The Company offers insurance products and services to customers through its wholly owned subsidiary, The Checkley Agency, Inc. ("Checkley"). The Company also wholly owns two statutory business trusts, First Mid-Illinois Statutory Trust I ("Trust I"), and First Mid-Illinois Statutory Trust II ("Trust II"), both unconsolidated subsidiaries of the Company.

The Company, a Delaware corporation, was incorporated on September 8, 1981, and pursuant to the approval of the Board of Governors of the Federal Reserve System (the "Federal Reserve Board") became the holding company owning all of the outstanding stock of First National Bank, Mattoon ("First National") on June 1, 1982. First National changed its name to First Mid-Illinois Bank & Trust, N.A. in 1992. The Company acquired all of the outstanding stock of a number of community banks or thrift institutions on the following dates, and subsequently combined their operations with those of the Company:

- Mattoon Bank, Mattoon on April 2, 1984
- State Bank of Sullivan on April 1, 1985
- Cumberland County National Bank in Neoga on December 31, 1985
- First National Bank and Trust Company of Douglas County on December 31, 1986
- Charleston Community Bank on December 30, 1987
- Heartland Federal Savings and Loan Association on July 1, 1992
- Downstate Bancshares, Inc. on October 4, 1994
- American Bank of Illinois on April 20, 2001

In 1997, First Mid Bank acquired the Charleston, Illinois branch location and the customer base of First of America Bank and in 1999 acquired the Monticello, Taylorville and DeLand branch offices and deposit base of Bank One Illinois, N.A.

First Mid Bank also opened a de novo branch in Decatur, Illinois and a banking center in the Student Union of Eastern Illinois University in Charleston, Illinois (2000); de novo branches in Champaign, Illinois and Maryville, Illinois (2002), and a de novo branch in Highland, Illinois (2005).

In 2002, the Company acquired all of the outstanding stock of Checkley, an insurance agency located in Mattoon.

On May 1, 2006, the Company acquired Mansfield Bancorp, Inc. ("Mansfield"), and its wholly owned subsidiary, Peoples State Bank of Mansfield ("Peoples") with locations in Mansfield, Mahomet and Weldon, Illinois. On September 8, 2006, Peoples merged with and into First Mid Bank with First Mid Bank being the surviving entity.

In 2009, the Company opened de novo branches in Decatur and Champaign.

Employees

The Company, MIDS, Checkley and First Mid Bank, collectively, employed 347 people on a full-time equivalent basis as of December 31, 2009. The Company places a high priority on staff development, which involves extensive training, including customer service training. New employees are selected on the basis of both technical skills and customer service capabilities. None of the employees are covered by a collective bargaining agreement with the Company. The Company offers a variety of employee benefits.

Business Lines

The Company has chosen to operate in three primary lines of business—community banking and wealth management through First Mid Bank and insurance brokerage through Checkley. Of these, the community banking line contributes approximately 90% of the Company's total revenues and profits. Within the community banking line, the Company serves commercial, retail and agricultural customers with a broad array of deposit and loan related products. The wealth management line provides estate planning, investment and farm management services for individuals and employee benefit services for business enterprises. The insurance brokerage line provides commercial lines insurance to businesses as well as homeowner, automobile and other types of personal lines insurance to individuals.

All three lines emphasize a "hands on" approach to service so that products and services can be tailored to fit the specific needs of existing and potential customers. Management believes that by emphasizing this personalized approach, the Company can, to a degree, diminish the trend towards homogeneous financial services, thereby differentiating the Company from competitors and allowing for slightly higher operating margins in each of the three lines.

Business Strategies

Strategy for Operations and Risk Management
Operationally, the Company centralizes as many administrative and clerical tasks as possible within its home office location in Mattoon, Illinois. This allows branches to maintain customer focus, helps assure compliance with banking regulations, keeps fixed administrative costs at as low a level as is practicable, and better manages the various forms of risk inherent in this business. This approach also allows for the best possible use of technology in day-to-day banking activities thereby reducing the potential for human error. While the Company does not employ every new technology that is introduced, it does attempt to be near the leading edge with respect to operational technology.

The Company has a comprehensive set of operational policies and procedures that have been developed over time to address risk. These policies are intended to be as close as possible to "best practices" of the financial services industry and are subjected to continual review by management and the Board of Directors. The Company's internal audit function incorporates procedures to determine compliance with these policies.

In the business of banking, credit risk is the single most important risk as losses from uncollectible loans can significantly diminish capital, earnings and shareholder value. In order to address this risk, the lending function of First Mid Bank receives significant attention from executive management and the Board of Directors. An important element of credit risk management is the quality, experience and training of the loan officers of First Mid Bank. The Company has invested, and will continue to invest, significant resources to ensure the quality, experience and training of First Mid Bank's loan officers in order to keep credit losses at a minimum. In addition to the human element of credit risk management, the Company's loan policies address the additional aspects of credit risk. Most lending personnel have signature authority that allows them to lend up to a certain amount based on their own judgment as to the creditworthiness of a borrower. The amount of the signature authority is based on the lending officers' experience and training. The Senior Loan Committee, consisting of the most experienced lenders within the organization, must approve all underwriting decisions in excess of $1.5 million. The Board of Directors must approve all underwriting decisions in excess of $2 million.

While the underlying nature of lending will result in some amount of loan losses, First Mid Bank's loan loss experience has been good with average net charge offs amounting to $1.3 million (.19% of average loans) over the past five years. Nonperforming loans were $12.7 million (1.82% of total loans) at December 31, 2009. These percentages have historically compared well with peer financial institutions and continue to do so today.

Interest rate and liquidity risk are two other forms of risk embedded in the business of financial intermediation. The Company's Asset Liability Management Committee, consisting of experienced individuals who monitor all aspects of interest rates and maturities of interest earning assets and interest paying liabilities, manages these risks. The underlying objectives of interest rate and liquidity risk management are to shelter the Company's net interest margin from changes in interest rates while maintaining adequate liquidity reserves to meet unanticipated funding demands. The Company uses financial modeling technology as a tool, employing a variety of "what if" scenarios to properly plan its activities. Despite the tools and methods used to monitor this risk, a sustained unfavorable interest rate environment will lead to some amount of compression in the net interest margin. During 2009, the Company's net interest margin decreased to 3.40% from 3.73% in 2008. This was the result of a greater decrease in interest-earning asset rates compared to the decrease in borrowing and deposit rates.

Strategy for Growth
The Company believes that growth of its revenue stream and of its customer base is vital to the goal of increasing the value of its shareholders' investment. Management attempts to grow in two primary ways:

• by organic growth through adding new customers and selling more products and services to existing customers; and

• by acquisitions.

Virtually all of the Company's customer-contact personnel, in each of its business lines, are engaged in organic growth efforts to one degree or another. These personnel are trained to engage in needs-based selling whereby they make an attempt to match its products and services with the particular financial needs of individual customers and prospective customers. Most senior officers of the organization are required to attend monthly sales meetings where they report on their business development efforts and results. Executive management uses these meetings as an educational and risk management opportunity as well. Cross-selling opportunities are encouraged between the business lines.

Within the community banking line, the Company has focused on growing business operating and real estate loans. Total commercial real estate loans have increased modestly from $187 million at December 31, 2005 to $226 million at December 31, 2009. Approximately 66% of the Company's total revenues are derived from lending activities. The Company has also focused on growing the commercial and retail deposit base through growth in checking, money markets and customer repurchase agreement balances. The wealth management line has focused its growth efforts on estate planning, investment and farm management services for individuals and employee benefit services for businesses. The insurance brokerage line has focused on increasing property and casualty insurance for businesses and personal lines insurance to individuals.

Growth through a series of small acquisitions has been an integral part of the Company's strategy for an extended period of time. When reviewing acquisition possibilities, the Company focuses on those organizations where there is a cultural fit with its existing operations and where there is a strong likelihood of adding to shareholder value. Most past acquisitions have been cash-based transactions. While the Company expects to continue this trend in the future, it would consider a stock-based acquisition if the strategic and financial metrics were compelling. The emphasis on smaller acquisitions is due to the inherent risks accompanying acquisitions and the preference for cash financing rather than use of the Company's common stock.

This overall growth strategy has been to grow the customer base without significantly increasing the shareholder base. This requires a certain amount of financial leverage and the Company monitors its capital base carefully to satisfy all regulatory requirements while maintaining flexibility. The Company has maintained a Dividend Reinvestment Plan as well as various forms of equity compensation for directors and key managers. It has also maintained an ongoing share buy back program both as a service to shareholders and a means of maintaining optimal levels of capital. In 2009, the Company issued and sold Series B Preferred Stock to certain investors. The Company also uses various forms of long-term debt to augment its capital when appropriate.

Markets and Competition

The Company has active competition in all areas in which First Mid Bank presently does business. First Mid Bank competes for commercial and individual deposits, loans, and trust business with many east central Illinois banks, savings and loan associations, and credit unions. The principal methods of competition in the banking and financial services industry are quality of services to customers, ease of access to facilities, and pricing of services, including interest rates paid on deposits, interest rates charged on loans, and fees charged for fiduciary and other banking services.

First Mid Bank operates facilities in the Illinois counties of Bond, Champaign, Christian, Coles, Cumberland, Dewitt, Douglas, Effingham, Macon, Madison, Moultrie, and Piatt. Each facility primarily serves the community in which it is located. First Mid Bank serves nineteen different communities with twenty-six separate locations in the towns of Altamont, Arcola, Champaign, Charleston, Decatur, Effingham, Highland, Mansfield, Mahomet, Maryville, Mattoon, Monticello, Neoga, Pocahontas, Sullivan, Taylorville, Tuscola, Urbana, and Weldon Illinois. Within the areas of service, there are numerous competing financial institutions and financial services companies.

Website

The Company maintains a website at www.firstmid.com. All periodic and current reports of the Company and amendments to these reports filed with the Securities and Exchange Commission (“SEC”) can be accessed, free of charge, through this website as soon as reasonably practicable after these materials are filed with the SEC.

SUPERVISION AND REGULATION

General

Financial institutions, financial services companies, and their holding companies are extensively regulated under federal and state law. As a result, the growth and earnings performance of the Company can be affected not only by management decisions and general economic conditions, but also by the requirements of applicable state and federal statutes and regulations and the policies of various governmental regulatory authorities including, but not limited to, the Office of the Comptroller of the Currency (the “OCC”), the Federal Reserve Board, the Federal Deposit Insurance Corporation (the “FDIC”), the Internal Revenue Service and state taxing authorities. Any change in applicable laws, regulations or regulatory policies may have material effects on the business, operations and prospects of the Company and First Mid Bank. The Company is unable to predict the nature or extent of the effects that fiscal or monetary policies, economic controls or new federal or state legislation may have on its business and earnings in the future.

Federal and state laws and regulations generally applicable to financial institutions and financial services companies, such as the Company and its subsidiaries, regulate, among other things, the scope of business, investments, reserves against deposits, capital levels relative to operations, the nature and amount of collateral for loans, the establishment of branches, mergers, consolidations and dividends. The system of supervision and regulation applicable to the Company and its subsidiaries establishes a comprehensive framework for their respective operations and is intended primarily for the protection of the FDIC’s deposit insurance fund and the depositors, rather than the stockholders, of financial institutions.
The following references to material statutes and regulations affecting the Company and its subsidiaries are brief summaries thereof and do not purport to be complete, and are qualified in their entirety by reference to such statutes and regulations. Any change in applicable law or regulations may have a material effect on the business of the Company and its subsidiaries.

Financial Modernization Legislation

The 1999 Gramm-Leach-Bliley Act (the “GLB Act”) significantly changed financial services regulation by expanding permissible non-banking activities of bank holding companies and removing certain barriers to affiliations among banks, insurance companies, securities firms and other financial services entities. These activities and affiliations can be structured through a holding company structure or, in the case of many of the activities, through a financial subsidiary of a bank. The GLB Act also established a system of federal and state regulation based on functional regulation, meaning that primary regulatory oversight for a particular activity generally resides with the federal or state regulator having the greatest expertise in the area. Banking is supervised by banking regulators, insurance by state insurance regulators and securities activities by the SEC and state securities regulators. The GLB Act also requires the disclosure of agreements reached with community groups that relate to the Community Reinvestment Act, and contains various other provisions designed to improve the delivery of financial services to consumers while maintaining an appropriate level of safety in the financial services industry.

The GLB Act repeals the anti-affiliation provisions of the Glass-Steagall Act and revises the Bank Holding Company Act of 1956 (the “BHCA”) to permit qualifying holding companies, called “financial holding companies,” to engage in, or to affiliate with companies engaged in, a full range of financial activities, including banking, insurance activities (including insurance portfolio investing), securities activities, merchant banking and additional activities that are “financial in nature,” incidental to financial activities or, in certain circumstances, complementary to financial activities. A bank holding company’s subsidiary banks must be “well-capitalized” and “well-managed” and have at least a “satisfactory” Community Reinvestment Act rating for the bank holding company to elect and maintain its status as a financial holding company.

A significant component of the GLB Act’s focus on functional regulation relates to the application of federal securities laws and SEC oversight of some bank securities activities previously exempt from broker-dealer registration. Among other things, the GLB Act amends the definitions of “broker” and “dealer” under the Securities Exchange Act of 1934 to remove the blanket exemption for banks. Under the GLB Act, banks may conduct securities activities without broker-dealer registration only if the activities fall within a set of activity-based exemptions designed to allow banks to conduct only those activities traditionally considered to be primarily banking or trust activities. Securities activities outside these exemptions, as a practical matter, need to be conducted by registered broker-dealer affiliate. By several orders, the SEC extended the blanket exemption for banks from the definition of “broker” and “dealer” while it considered implementing rules. In 2003, the SEC adopted amendments to its rules relating to the “dealer” exemption for banks. In September 2007, the SEC and the Federal Reserve Board adopted a regulation to implement the broker activities exemption of the GLB Act that became effective for First Mid Bank beginning January 1, 2009. The GLB Act also amends the Investment Advisers Act of 1940 to require the registration of banks that act as investment advisers for mutual funds. The Company believes that it has taken the necessary actions to comply with these requirements of the GLB Act and the regulations adopted under them.

Anti-Terrorism Legislation

The USA PATRIOT Act of 2001 included the International Money Laundering Abatement and Anti-Terrorist Financing Act of 2001 (the “IMLAFA”). The IMLAFA contains anti-money laundering measures affecting insured depository institutions, broker-dealers, and certain other financial institutions. The IMLAFA requires U.S. financial institutions to adopt policies and procedures to combat money laundering and grants the Secretary of the Treasury broad authority to establish regulations and to impose requirements and restrictions on financial institutions’ operations. The Company has established policies and procedures for compliance with the IMLAFA and the related regulations. The Company has designated an officer solely responsible for ensuring compliance with existing regulations and monitoring changes to the regulations as they occur.

Emergency Economic Stabilization Act of 2008

In response to recent unprecedented financial market turmoil, the Emergency Economic Stabilization Act of 2008 ("EESA") was enacted on October 3, 2008. EESA authorizes the U.S. Treasury Department to provide up to $700 billion in funding for the financial services industry. Pursuant to the EESA, the Treasury was initially authorized to use $350 billion for the Troubled Asset Relief Program (TARP). Of this amount, Treasury allocated $250 billion to the TARP Capital Purchase Program. On January 15, 2009, the second $350 billion of TARP monies was released to the Treasury. The Secretary's authority under TARP expires October 3, 2010. The Company decided to not participate in the TARP Capital Purchase Program.

Before and after EESA, there have been numerous actions by Congress, the Federal Reserve Board, the Treasury, the FDIC, the SEC and others to further the economic and banking industry stabilization efforts, including the American Recovery and Reinvestment Ac enacted February 17, 2009.

On October 14, 2008, the FDIC announced the Temporary Liquidity Guarantee Program (TLGP). The final rule was adopted on November 21, 2008. The FDIC stated that the purpose of these actions is to strengthen confidence and encourage liquidity in the banking system by guaranteeing newly issued senior unsecured debt of 31 days or greater, of banks, thrifts, and certain holding companies, and by providing full FDIC insurance coverage for all non-interest bearing transaction accounts, regardless of dollar amount. Inclusion in the program was voluntary. Institutions participating in the senior unsecured debt portion of the program are assessed fees based on a sliding scale, depending on length of maturity. Shorter-term debt has a lower fee structure and longer-term debt has a higher fee. The range is from 50 basis points on debt of 180 days or less, to a maximum of 100 basis points for debt with maturities of one year or longer, on an annualized basis. A 10-basis point surcharge is added to a participating institution's current insurance assessment in exchange for final coverage for all transaction accounts.

First Mid Bank elected to participate in both parts of the TLGP, the Transaction Account Guarantee Program and the Debt Guarantee Program. The FDIC’s Transaction Account Guarantee Program, provides, without charge to depositors, a full guarantee on all non-interest bearing transaction accounts held by any depositor, regardless of dollar amount, through June 30, 2010. Participation in the Transaction Account Guarantee Program cost the Company 10 basis points annually on the amount of the deposits. The FDIC’s Debt Guarantee Program, which expired in October 2009, provided for the guarantee of eligible newly issued senior unsecured debt of participating entities, but the Company and the Bank did not issue any debt under this program.

The Company

General. As a registered bank holding company under the BHCA that has elected to become a financial holding company under the GLB Act, the Company is subject to regulation by the Federal Reserve Board. In accordance with Federal Reserve Board policy, the Company is expected to act as a source of financial strength to First Mid Bank and to commit resources to support First Mid Bank in circumstances where the Company might not do so absent such policy. The Company is subject to inspection, examination, and supervision by the Federal Reserve Board.

Activities. As a financial holding company, the Company may affiliate with securities firms and insurance companies and engage in other activities that are financial in nature or incidental or complementary to activities that are financial in nature. A bank holding company that is not also a financial holding company is limited to engaging in banking and such other activities as determined by the Federal Reserve Board to be so closely related to banking or managing or controlling banks as to be a proper incident thereto.

No Federal Reserve Board approval is required for the Company to acquire a company (other than a bank holding company, bank, or savings association) engaged in activities that are financial in nature or incidental to activities that are financial in nature, as determined by the Federal Reserve Board. However, the Company generally must give the Federal Reserve Board after-the-fact notice of these activities. Prior Federal Reserve Board approval is required before the Company may acquire beneficial ownership or control of more than 5% of the voting shares or substantially all of the assets of a bank holding company, bank, or savings association.

If any subsidiary bank of the Company ceases to be “well-capitalized” or “well-managed” under applicable regulatory standards, the Federal Reserve Board may, among other actions, order the Company to divest its depository institution. Alternatively, the Company may elect to conform its activities to those permissible for a bank holding company that is not also a financial holding company.

If any subsidiary bank of the Company receives a rating under the Community Reinvestment Act of less than “satisfactory”, the Company will be prohibited, until the rating is raised to “satisfactory” or better, from engaging in new activities or acquiring companies other than bank holding companies, banks, or savings associations.

Capital Requirements. Bank holding companies are required to maintain minimum levels of capital in accordance with Federal Reserve Board capital adequacy guidelines. The Federal Reserve Board's capital guidelines establish the following minimum regulatory capital requirements for bank holding companies: a risk-based requirement expressed as a percentage of total risk-weighted assets, and 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%, at least one-half of which must be Tier 1 capital. The leverage requirement consists of a minimum ratio of Tier 1 capital to total assets of 3% for the most highly rated companies, with minimum requirements of at least 4% for all others. For purposes of these capital standards, Tier 1 capital consists primarily of permanent stockholders' equity, which includes the Series B 9% Non-Cumulative Perpetual Convertible Preferred Stock issued by the Company in 2009, less intangible assets (other than certain mortgage servicing rights and purchased credit card relationships), and total capital means Tier 1 capital plus certain other debt and equity instruments which do not qualify as Tier 1 capital, limited amounts of unrealized gains on equity securities and a portion of the Company's allowance for loan and lease losses.

The risk-based and leverage standards described above are minimum requirements, and higher capital levels will be required if warranted by the particular circumstances or risk profiles of individual banking organizations. For example, the Federal Reserve Board'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.

In December 2007, the U.S. bank regulatory agencies adopted final rules that require large, internationally active financial services organizations to use the most sophisticated and complex methodology for calculating capital requirements reflected in the New Basel Capital Accord, developed by the Basel Committee on Banking Supervision. These rules became operational in April 2008, but are mandatory only for "core banks," i.e., banks with consolidated total assets of $250 billion or more. In July 2008, the U.S. bank regulatory agencies also published a notice of proposed rule-making that would provide all non-core banking organizations with the option to adopt a standardized approach under these rules, which reflects a simpler methodology than the advanced approaches required of core banks.

As of December 31, 2009, the Company had regulatory capital, calculated on a consolidated basis, in excess of the Federal Reserve Board's minimum requirements, and its capital ratios exceeded those required for categorization as well-capitalized under the capital adequacy guidelines established by bank regulatory agencies with a total risk-based capital ratio of 15.76%, a Tier 1 risk-based ratio of 14.57% and a leverage ratio of 10.63%.

Control Acquisitions. The Change in Bank Control Act prohibits a person or group of person from acquiring "control" of a bank holding company unless the Federal Reserve Board has been notified and has not objected to the transaction. Under a rebuttable presumption established by the Federal Reserve Board, the acquisition of 10% or more of a class of voting stock of a bank holding company with a class of securities registered under Section 12 of the Exchange Act, such as the Company, would, under the circumstances set forth in the presumption, constitute acquisition of control of the Company.

In addition, any company is required to obtain the approval of the Federal Reserve Board under the BHCA before acquiring 25% (5% in the case of an acquirer that is a bank holding company) or more of the outstanding common of the Company, or otherwise obtaining control of a "controlling influence" over the Company or First Mid Bank.

Interstate Banking and Branching. The Riegle-Neal Act enacted in 1994 permits an adequately capitalized and adequately managed bank holding company, with Federal Reserve Board approval, to acquire banking institutions located in states other than the bank holding company's home state without regard to whether the transaction is prohibited under state law. In addition, national banks and state banks with different home states are permitted to merge across state lines, with the approval of the appropriate federal banking agency, unless the home state of a participating banking institution has passed legislation prior to that date that expressly prohibits interstate mergers. De novo interstate branching is permitted if the laws of the host state so authorize. Moreover, national banks, such as First Mid Bank, may provide trust services in any state to the same extent as a trust company chartered by that state.

Privacy and Security. The GLB Act establishes a minimum federal standard of financial privacy by, among other provisions, requiring banks to adopt and disclose privacy policies with respect to consumer information and setting forth certain rules with respect to the disclosure to third parties of consumer information. The Company has adopted and disseminated its privacy policies pursuant to the GLB Act. Regulations adopted under the GLB Act set standards for protecting the security, confidentiality and integrity of customer information, and require notice to regulators, and in some cases, to customers, in the event of security breaches. A number of states have adopted their own statutes requiring notification of security breaches. In addition, the GLB Act requires the disclosure of agreements reached with community groups that relate to the CRA, and contains various other provisions designed to improve the delivery of financial services to consumers while maintaining an appropriate level of safety in the financial services industry.

First Mid Bank

General. First Mid Bank is a national bank, chartered under the National Bank Act. The FDIC insures the deposit accounts of First Mid Bank. As a national bank, First Mid Bank is a member of the Federal Reserve System and is subject to the examination, supervision, reporting and enforcement requirements of the OCC, as the primary federal regulator of national banks, and the FDIC, as administrator of the deposit insurance fund.

Deposit Insurance. As an FDIC-insured institution, First Mid Bank is required to pay deposit insurance premium assessments to the FDIC.
On October 3, 2008, the FDIC temporarily increased the standard maximum deposit insurance amount (SMDIA) from $100,000 to $250,000 per depositor. On May 20, 2009, the Helping Families Save Their Homes Act extended the temporary increase in the SMDIA through December 31, 2013. This extension of the temporary $250,000 coverage limit became effective immediately upon the President's signature. The legislation provides that the SMDIA will return to $100,000 on January 1, 2014. The additional cost of the increase to the SMDIA, assessed on a quarterly basis, is a 10 basis point annualized surcharge (2.5 basis points quarterly) on balances in non-interest bearing transaction accounts that exceed $250,000. The Company has expensed $49,000 for this program in 2009.

On February 27, 2009, the FDIC adopted a final rule modifying the risk-based assessment system and setting initial base assessment rates beginning April 1, 2009, at 12 to 45 basis points and, due to extraordinary circumstances, extended the period of the restoration plan to increase the deposit insurance fund to seven years. Also on February 27, 2009, the FDIC issued final rules on changes to the risk-based assessment system. The final rules both increase base assessment rates and incorporate additional assessments for excess reliance on brokered deposits and FHLB advances. The new rates would increase annual assessment rates from 5 to 7 basis points to 7 to 24 basis points. This new assessment took effect April 1, 2009. The Company has expensed $1,260,000 for this assessment in 2009.

Also on February 27, 2009, the FDIC adopted an interim rule to impose a 20 basis point emergency special assessment payable September 30, 2009 based on the second quarter 2009 assessment base, to help shore up the Deposit Insurance Fund (“DIF”). This assessment equates to a one-time cost of $200,000 per $100 million in assessment base. The interim rule also allows the Board to impose possible additional special assessments of up to 10 basis points thereafter to maintain public confidence in the DIF. Subsequently, the FDIC’s Treasury borrowing authority increased from $30 billion to $100 billion, allowing the agency to cut the planned special assessment from 20 to 10 basis points. On May 22, 2009, the FDIC adopted a final rule which established a special assessment of five basis points on each FDIC-insured depository institutions assets, minus it Tier 1 capital, as of September 30, 2009. The assessment was capped at 10 basis points of an institution’s domestic deposits so that no institution would pay an amount higher than they would have under the interim rule. This special assessment was collected September 30, 2009. The Company expensed $522,000 as of June 30, 2009 for this special assessment.

In addition to its insurance assessment, each insured bank was subject, in 2009, to quarterly debt service assessments in connection with bonds issued by a government corporation that financed the federal savings and loan bailout. The Company expensed $112,000 during 2009 for this assessment.

On September 29, 2009, the FDIC Board proposed a Deposit Insurance Fund restoration plan that required banks 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. Under the plan—which applies to all banks except those with liquidity problems—banks were assessed through 2010 according to the risk-based premium schedule adopted earlier this year. Beginning January 1, 2011, the base rate increase by 3 basis points. The Company recorded a prepaid expense asset of $4,855,000 as of December 31, 2009 as a result of this plan. This asset will be amortized to non-interest expense over the next three years.

OCC Assessments. All national banks are required to pay supervisory fees to the OCC to fund the operations of the OCC. The amount of such supervisory fees is based upon each institution’s total assets, including consolidated subsidiaries, as reported to the OCC. During the year ended December 31, 2009, First Mid Bank paid supervisory fees to the OCC totaling $240,000.

Capital Requirements. The OCC has established the following minimum capital standards for national banks, such as First Mid Bank: a leverage requirement consisting of a minimum ratio of Tier 1 capital to total assets of 3% for the most highly-rated banks with minimum requirements of at least 4% for all others, and a risk-based capital requirement consisting of a minimum ratio of total capital to total risk-weighted assets of 8%, at least one-half of which must be Tier 1 capital. For purposes of these capital standards, Tier 1 capital and total capital consists of substantially the same components as Tier 1 capital and total capital under the Federal Reserve Board’s capital guidelines for bank holding companies (See “The Company—Capital Requirements”).

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, the regulations of the OCC 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.

During the year ended December 31, 2009, First Mid Bank was not required by the OCC to increase its capital to an amount in excess of the minimum regulatory requirements, and its capital ratios exceeded those required for categorization as well-capitalized under the capital adequacy guidelines established by bank regulatory agencies with a total risk-based capital ratio of 14.50%, a Tier 1 risk-based ratio of 13.31% and a leverage ratio of 9.67%.

Prompt Corrective Action. Federal law 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 "well-capitalized," "adequately-capitalized," "undercapitalized," "significantly undercapitalized" or "critically undercapitalized." Depending upon the capital category to which an institution is assigned, the regulators' corrective powers include: requiring the submission of a capital restoration plan; placing limits on asset growth and restrictions on activities; requiring the institution to issue additional capital stock (including additional voting stock) or to be acquired; restricting transactions with affiliates; restricting the interest rate the institution may pay on deposits; ordering a new election of directors of the institution; requiring that senior executive officers or directors be dismissed; prohibiting the institution from accepting deposits from correspondent banks; requiring the institution to divest certain subsidiaries; prohibiting the payment of principal or interest on subordinated debt; and in the most severe cases, appointing a conservator or receiver for the institution.

Dividends. The National Bank Act imposes limitations on the amount of dividends that may be paid by a national bank, such as First Mid Bank. Generally, a national bank may pay dividends out of its undivided profits, in such amounts and at such times as the bank's board of directors deems prudent. Without prior OCC approval, however, a national bank may not pay dividends in any calendar year which, in the aggregate, exceed the bank's year-to-date net income plus the bank's adjusted retained net income for the two preceding years.

The payment of dividends by any financial institution or its holding company 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, First Mid Bank exceeded its minimum capital requirements under applicable guidelines as of December 31, 2009. As of December 31, 2009, approximately $18.6 million was available to be paid as dividends to the Company by First Mid Bank. Notwithstanding the availability of funds for dividends, however, the OCC may prohibit the payment of any dividends by First Mid Bank if the OCC determines that such payment would constitute an unsafe or unsound practice.

Affiliate and Insider Transactions. First Mid Bank is subject to certain restrictions under federal law, including Regulation W of the Federal Reserve Board, on extensions of credit to the Company and its subsidiaries, on investments in the stock or other securities of the Company and its subsidiaries and the acceptance of the stock or other securities of the Company or its subsidiaries as collateral for loans. Certain limitations and reporting requirements are also placed on extensions of credit by First Mid Bank to its directors and officers, to directors and officers of the Company and its subsidiaries, to principal stockholders of the Company, and to “related interests” of such directors, officers and principal stockholders.

First Mid Bank is subject to restrictions under federal law that limits certain transactions with the Company, including loans, other extensions of credit, investments or asset purchases. Such transactions by a banking subsidiary with any one affiliate are limited in amount to 10 percent of the bank’s capital and surplus and, with all affiliates together, to an aggregate of 20 percent of the bank’s capital and surplus. Furthermore, such loans and extensions of credit, as well as certain other transactions, are required to be secured in specified amounts. These and certain other transactions, including any payment of money to the Company, must be on terms and conditions that are or in good faith would be offered to nonaffiliated companies.

In addition, federal law and regulations may affect the terms upon which any person becoming a director or officer of the Company or one of its subsidiaries or a principal stockholder of the Company may obtain credit from banks with which First Mid 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. In general, the 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. The preamble to the guidelines states that the agencies expect to require a compliance plan from an institution whose failure to meet one or more of the guidelines are of such severity that it could threaten the safety and soundness of the institution. Failure to submit an acceptable plan, or failure to comply with a plan that has been accepted by the appropriate federal regulator, would constitute grounds for further enforcement action.

Community Reinvestment Act. First Mid Bank is subject to the Community Reinvestment Act (CRA). The CRA and the regulations issued thereunder are intended to encourage banks to help meet the credit needs of their service areas, including low and moderate income neighborhoods, consistent with the safe and sound operations of the banks. These regulations also provide for regulatory assessment of a bank’s record in meeting the needs of its service area when considering applications to establish branches, merger applications and applications to acquire the assets and assume the liabilities of another bank. The Financial Institutions Reform, Recovery and Enforcement Act of 1989 requires federal banking agencies to make public a rating of a bank’s performance under the CRA. In the case of a bank holding company, the CRA performance record of its bank subsidiaries is reviewed by federal banking agencies in connection with the filing of an application to acquire ownership or control of shares or assets of a bank or thrift or to merge with any other bank holding company. An unsatisfactory record can substantially delay or block the transaction. First Mid Bank received a satisfactory CRA rating from its regulator in its most recent CRA examination.

Consumer Laws and Regulations. In addition to the laws and regulations discussed above, First Mid Bank is also subject to certain consumer laws and regulations that are designed to protect consumers in transactions with banks. While the list set forth herein is not exhaustive, these laws and regulations include the Truth in Lending Act, the Truth in Savings Act, the Equal Credit Opportunity Act, the Fair Housing Act, the Fair Credit Reporting Act, the Fair and Accurate Credit Transactions Act and the Real Estate Settlement Procedures Act, among others. These laws and regulations mandate certain disclosure requirements and regulate the manner in which financial institutions must deal with customers when taking deposits, making loans to or marketing to or engaging in other types of transactions with such customers. Failure to comply with these laws and regulations could lead to substantial penalties, operating restrictions and reputational damage to the financial institution.

Supplemental Item – Executive Officers of the Registrant

The executive officers of the Company are elected annually by the Company's board of directors and are identified below.

Name (Age)	Position With Company
William S. Rowland (63)	Chairman of the Board of Directors, President and Chief Executive Officer
Michael L. Taylor (41)	Executive Vice President and Chief Financial Officer
John W. Hedges (62)	Executive Vice President
Laurel G. Allenbaugh (49)	Executive Vice President
Kelly A. Downs (42)	Senior Vice President
Christopher L. Slabach (47)	Senior Vice President
Eric S. McRae (44)	Vice President
Charles A. LeFebvre (40)	Vice President

William S. Rowland, age 63, has been Chairman of the Board of Directors, President and Chief Executive Officer of the Company since May 1999. He served as Executive Vice President of the Company from 1997 to 1999 and as Treasurer and Chief Financial Officer from 1989 to 1999. He also serves as Chairman of the Board of Directors and Chief Executive Officer of First Mid Bank.

Michael L. Taylor, age 41, has been the Executive Vice President and Chief Financial Officer of the Company since May 2007. He served as Vice President and Chief Financial Officer from May 2000 to May 2007. He was with AMCORE Bank in Rockford, Illinois from 1996 to 2000.

John W. Hedges, age 62, has been Executive Vice President of the Company and the President of First Mid Bank since September 1999. He was with National City Bank in Decatur, Illinois from 1976 to 1999.

Laurel G. Allenbaugh, age 49, has been Executive Vice President of Operations since April 2008. She served as Vice President of Operations from February 2000 to April 2008. She served as Controller of the Company and First Mid Bank from 1990 to February 2000 and has been President of MIDS since 1998.

Kelly A. Downs, age 42, has been Senior Vice President of Human Resources since April 2008, has served as Vice President of Human Resources from 2001 to April 2008, and has been with the Company since 1991.

Christopher L. Slabach, age 47, has been Senior Vice President of the Company since 2007 and Senior Vice President, Risk Management of First Mid Bank since 2008. He served as Vice President, Audit from 1998-2007.

Eric S. McRae, age 44, has been Vice President of the Company and Executive Vice President, Chief Credit Officer of First Mid Bank since December 2008. He served as President of the Decatur region from 2001 to December 2008.

Charles A. LeFebvre, age 40, has been Vice President of the Company and Executive Vice President of the Trust and Wealth Management Division of First Mid Bank since 2007. He was an attorney with the law firm of Thomas, Mamer & Haughey from 2001 to 2007.

ITEM 1A. RISK FACTORS

Various risks and uncertainties, some of which are difficult to predict and beyond the Company's control, could negatively impact the Company. As a financial institution, the Company is exposed to interest rate risk, liquidity risk, credit risk, operational risk, risks from economic or market conditions, and general business risks among others. Adverse experience with these or other risks could have a material impact on the Company's financial condition and results of operations, as well as the value of its common stock.

Difficult economic conditions and market disruption have adversely impacted the banking industry and financial markets generally and may significantly affect the business, financial condition, or results of operations of the Company. The Company's success depends, to a certain extent, upon economic and political conditions, local and national, as well as governmental monetary policies. Conditions such as inflation, recession, unemployment, changes in interest rates, money supply and other factors beyond the Company's control may adversely affect its asset quality, deposit levels and loan demand and, therefore, its earnings.

Dramatic declines in the housing market beginning in the latter half of 2007, with falling home prices and increasing foreclosures, unemployment and underemployment, have negatively impacted the credit performance of mortgage loans and resulted in significant write-downs of asset values by some financial institutions. The resulting write-downs to assets of financial institutions have caused many financial institutions to merge with other institutions and, in some cases, to seek government assistance or bankruptcy protection.

The capital and credit markets, including the fixed income markets, have been experiencing volatility and disruption for over a year. In some cases, the markets have produced downward pressure on stock prices and credit capacity for certain issuers without regard to those issuers' financial strength.

Many lenders and institutional investors have reduced and, in some cases, ceased to provide funding to borrowers, including to other financial institutions because of concern about the stability of the financial markets and the strength of counterparties. It is difficult to predict how long these economic conditions will exist, and which of our markets, products or other businesses will ultimately be affected. Accordingly, the resulting lack of available credit, lack of confidence in the financial sector, decreased consumer confidence, increased volatility in the financial markets and reduced business activity could materially and adversely affect the Company's business, financial condition and results of operations.

As a result of the challenges presented by economic conditions, the Company has faced the following risks in connection with these events:

- Inability of borrowers to make timely repayments of their loans, or decreases in value of real estate collateral securing the payment of such loans resulting in significant credit losses, which results in increased delinquencies, foreclosures and customer bankruptcies, any of which could have a material adverse effect on the Company's operating results.

- Increased regulation of the banking industry, including heightened legal standards and regulatory requirements. Compliance with such regulation increases costs and may limit the Company's ability to pursue business opportunities.

- Further disruptions in the capital markets or other events, including actions by rating agencies and deteriorating investor expectations, may result in an inability to borrow on favorable terms or at all from other financial institutions.

The Company’s profitability depends significantly on economic conditions in the geographic region in which it operates. A large percentage of the Company’s loans are to individuals and businesses in Illinois, consequently, any decline in the economy of this market area could have a materially adverse effect on the Company’s financial condition and results of operations.

The strength and stability of other financial institutions may adversely affect the Company’s business. The actions and commercial soundness of other financial institutions could affect the Company’s ability to engage in routine funding transactions. Financial services to institutions are interrelated as a result of clearing, counterparty or other relationships. The Company has exposure to different industries and counterparties, and executes transactions with various counterparties in the financial industry. Recent defaults by financial services institutions, and even rumors or questions about one or more financial services institution or the financial services industry in general, have led to market-wide liquidity problems and could lead to losses or defaults by the Company or by other institutions. Many of these transactions expose the Company to credit risk in the event of default of its counterparty or client. Any such losses could materially and adversely affect the Company’s results of operations.

Changes in interest rates may negatively affect our earnings. Changes in market interest rates and prices may adversely affect the Company’s financial condition or results of operations. The Company’s net interest income, its largest source of revenue, is highly dependent on achieving a positive spread between the interest earned on loans and investments and the interest paid on deposits and borrowings. Changes in interest rates could negatively impact the Company’s ability to attract deposits, make loans, and achieve a positive spread resulting in compression of the net interest margin.

The Company may not have sufficient cash or access to cash to satisfy current and future financial obligations, including demands for loans and deposit withdrawals, funding operating costs, payment of preferred stock dividends and for other corporate purposes. This type of liquidity risk arises whenever the maturities of financial instruments included in assets and liabilities differ. The Company’s liquidity can be affected by a variety of factors, including general economic conditions, market disruption, operational problems affecting third parties or the Company, unfavorable pricing, competition, the Company’s credit rating and regulatory restrictions. (See “Liquidity” herein for management’s actions to mitigate this risk.)

If the Company were unable to borrow funds through access to capital markets, it may not be able to meet the cash flow requirements of its depositors, creditors, and borrowers, or the operating cash needed to fund corporate expansion and other corporate activities. Liquidity policies and limits are established by the board of directors, with operating limits set based upon the ratio of loans to deposits and percentage of assets funded with non-core or wholesale funding. The Company regularly monitors the overall liquidity position of First Mid Bank and the parent company to ensure that various alternative strategies exist to cover unanticipated events that could affect liquidity. The Company also establishes policies and monitors guidelines to diversify First Mid Bank's wholesale funding sources to avoid concentrations in any one market source. Wholesale funding sources include Federal funds purchased, securities sold under repurchase agreements, non-core deposits, and debt. First Mid Bank is also a member of the Federal Home Loan Bank of Chicago (FHLB), which provides funding through advances to members that are collateralized with mortgage-related assets.

First Mid Bank maintains a portfolio of securities that can be used as a secondary source of liquidity. There are other sources of liquidity available to the Company should they be needed. These sources include the sale or securitization of loans, the ability to acquire additional national market, non-core deposits, issuance of additional collateralized borrowings such as FHLB advances, the issuance of debt securities, and the issuance of preferred or common securities in public or private transactions. The Bank also can borrow from the Federal Reserve's discount window.

Starting in the middle of 2007, there has been significant turmoil and volatility in worldwide financial markets which, although there has been some improvement, is still ongoing. These conditions have resulted in a disruption in the liquidity of financial markets, and could directly impact the Company to the extent it needs to access capital markets to raise funds to support its business and overall liquidity position. This situation could affect the cost of such funds or the Company's ability to raise such funds. If the Company were unable to access any of these funding sources when needed, it might be unable to meet customers' needs, which could adversely impact its financial condition, results of operations, cash flows, and level of regulatory-qualifying capital. The Company may, from time to time, consider opportunistically retiring its outstanding securities, including its trust preferred securities and common shares in privately negotiated or open market transactions for cash. For further discussion, see the "Liquidity" section.

Loan customers or other counter-parties may not be able to perform their contractual obligations resulting in a negative impact on the Company's earnings. Overall economic conditions affecting businesses and consumers, including the current difficult economic conditions and market disruptions, could impact the Company's credit losses. In addition, real estate valuations could also impact the Company's credit losses as the Company maintains $517 million in loans secured by commercial, agricultural, and residential real estate. A significant decline in real estate values could have a negative effect on the Company's financial condition and results of operations. In addition, the Company's total loan balances by industry exceeded 25% of total risk-based capital for each of four industries as of December 31, 2009. A listing of these industries is contained in under "Item 6. Management's Discussion and Analysis of Financial Condition and Results of Operations -- Loans" herein. A significant change in one of these industries such as a significant decline in agricultural crop prices, could adversely impact the Company's credit losses.

Continued deterioration in the real estate market could lead to additional losses, which could have a material adverse effect on the business, financial condition and results of operations or the Company. Commercial and commercial real estate loans generally involve higher credit risks than residential real estate and consumer loans. Because payments on loans secured by commercial real estate or equipment are often dependent upon the successful operation and management of the underlying assets, repayment of such loans may be influenced to a great extent by conditions in the market or the economy. Continued increases in commercial and consumer delinquency levels or continued declines in real estate market values would require increased net charge-offs and increases in the allowance for loan and lease losses, which could have a material adverse effect on our business, financial condition and results of operations and prospects.

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

Declines in the value of securities held in the investment portfolio may negatively affect the Company's earnings. The value of an investment in the portfolio could decrease due to changes in market factors. The market value of certain investment securities is volatile and future declines or other-than-temporary impairments could materially adversely affect the Company's future earnings and regulatory capital. Continued volatility in the market value of certain of the investment securities, whether caused by changes in market perceptions of credit risk, as reflected in the expected market yield of the security, or actual defaults in the portfolio could result in significant fluctuations in the value of the securities. This could have a material adverse impact on the Company's accumulated other comprehensive loss and shareholders' equity depending upon the direction of the fluctuations.

Furthermore, future downgrades or defaults in these securities could result in future classifications as other-than-temporarily impaired. The Company has invested in trust preferred securities issued by financial institutions and insurance companies, corporate securities of financial institutions, and stock in the Federal Home Loan Bank of Chicago and Federal Reserve Bank of Chicago. Deterioration of the financial stability of the underlying financial institutions for these investments could result in other-than-temporary impairment charges to the Company and could have a material impact on future earnings. For further discussion of the Company's investments, see Note 4 – "Investment Securities."

If the Company’s stock price declines from levels at December 31, 2009, management will evaluate the goodwill balances for impairment, and if the values of the businesses have declined, the Company could recognize an impairment charge for its goodwill. Management performed an annual goodwill impairment assessment as of September 30, 2009. Based on these analyses, management concluded that the fair value of the Company’s reporting units exceeded the fair value of its assets and liabilities and, therefore, goodwill was not considered impaired. It is possible that management’s assumptions and conclusions regarding the valuation of the Company’s lines of business could change adversely, which could result in the recognition of impairment for goodwill, which could have a material effect on the Company’s financial position and future results of operations.

The Series B preferred stock impacts net income available to common stockholders and earnings per share. As long as shares of the Series B preferred stock are outstanding, no dividends may be paid on the Company’s common stock unless all dividends on the Series B preferred stock have been paid in full. The dividends declared on the Series B preferred stock reduce the net income available to common stockholders and earnings per share.

Holders of the Series B preferred stock have rights that are senior to those of common stockholders. The Series B preferred stock is senior to the shares of common stock and holders of the Series B preferred stock have certain rights and preferences that are senior to holders of common stock. The Series B preferred stock will rank senior to the common stock and all other equity securities designated as ranking junior to the Series B preferred stock. So long as any shares of the Series B preferred stock remain outstanding, unless all accrued and unpaid dividends for all prior dividend periods have been paid or are contemporaneously declared and paid in full, no dividend shall be paid or declared on common stock or other junior stock, other than a dividend payable solely in common stock. The Company also may not purchase, redeem or otherwise acquire for consideration any shares of its common stock or other junior stock unless it has paid in full all accrued dividends on the Series B preferred stock for all prior dividend periods. The Series B preferred stock is entitled to a liquidation preference over shares of common stock in the event of the Company’s liquidation, dissolution or winding up.

The Company may issue additional common stock or other equity securities in the future which could dilute the ownership interest of existing stockholders. In order to maintain capital at desired or regulatory-required levels or to replace existing capital, the Company may be required to issue additional shares of common stock, or securities convertible into, exchangeable for or representing rights to acquire shares of common stock. The Company may sell these shares at prices below the current market price of shares, and the sale of these shares may significantly dilute stockholder ownership. The Company could also issue additional shares in connection with acquisitions of other financial institutions.

Human error, inadequate or failed internal processes and systems, and external events may have adverse effects on the Company. Operational risk includes compliance or legal risk, which is the risk of loss from violations of, or noncompliance with, laws, rules, regulations, prescribed practices, or ethical standards. Operational risk also encompasses transaction risk, which includes losses from fraud, error, the inability to deliver products or services, and loss or theft of information. Losses resulting from operational risk could take the form of explicit charges, increased operational costs, harm to the Company’s reputation or forgone opportunities. Any of these could potentially have a material adverse effect on the Company’s financial condition and results of operations.

The Company is exposed to various business risks that could have a negative effect on the financial performance of the Company. These risks include: changes in customer behavior, changes in competition, new litigation or changes to existing litigation, claims and assessments, environmental liabilities, real or threatened acts of war or terrorist activity, adverse weather, changes in accounting standards, legislative or regulatory changes, taxing authority interpretations, and an inability on the Company’s part to retain and attract skilled employees.

In addition to these risks identified by the Company, investments in the Company’s common stock involve risk. The market price of the Company’s common stock may fluctuate significantly in response to a number of factors including:

volatility of stock market prices and volumes, rumors or erroneous information, changes in market valuations of similar companies, changes in securities analysts’ estimates of financial performance, and variations in quarterly or annual operating results.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

The Company or First Mid Bank own all of the following properties except those specifically identified as being leased.

First Mid Bank

Mattoon. First Mid Bank's main office is located at 1515 Charleston Avenue, Mattoon, Illinois. The office building consists of a one-story structure with occupied basement, which was opened in 1965 with approximately 36,000 square feet of office space, four walk-up teller stations, and four sit-down teller stations. Adjacent to this building is a parking lot with parking for approximately seventy cars. A drive-up facility with nine drive-up lanes and a drive-up automated teller machine ("ATM") is located across the street from First Mid Bank's main office.

First Mid Bank has a facility at 333 Broadway Avenue East, Mattoon, Illinois. The one-story office building contains approximately 7,600 square feet of office space. The main floor provides space for five teller windows, two private offices, a safe deposit vault and four drive-up lanes. There is adequate parking located adjacent to the building. A drive-up ATM is located adjacent to the building.

First Mid Bank leases a facility at 1504-A Lakeland Boulevard, Mattoon, Illinois that provides space for three tellers, two drive-up lanes and a drive-up ATM.

First Mid Bank owns a facility located at 1520 Charleston Avenue, Mattoon, Illinois, which is used as the corporate headquarters of the Company and is used by MIDS for its data processing and back room operations for the Company and First Mid Bank. The office building consists of a two-story structure with an occupied basement that has approximately 20,000 square feet of office space.

The Company owns a facility at 1500 Wabash Avenue, Mattoon, Illinois, which is used by the loan and deposit services departments of First Mid Bank. The office building consists of a two-story structure with a basement that has approximately 11,200 square feet of office space.

First Mid Bank leases a facility located at 14th and Charleston, Mattoon, Illinois which is used by the trust and investment services departments of First Mid Bank. The office space, comprised of approximately 2,100 square feet, contains five offices, one conference rooms, a file room and a waiting/reception area. Adequate parking is available to serve customers.

There are four additional ATMs located in Mattoon. They are located in the Administration building of Lake Land College, in the main lobby of Sarah Bush Lincoln Health Center, at R.R. Donnelley & Sons Co. on North Route 45 and County Market at 2000 Western Avenue.

Sullivan. First Mid Bank operates one location in Sullivan, Illinois. The main office is located at 200 South Hamilton Street, Sullivan, Illinois. Its office building is a one-story structure containing approximately 11,400 square feet of office space with five teller windows, six private offices and four drive-up lanes. Adequate customer parking is available on two sides of the main office building. There is also a walk-up ATM located in the Sullivan Citgo Station at 105 West Jackson.

Neoga. First Mid Bank's office in Neoga, Illinois, is located at 102 East Sixth Street, Neoga, Illinois. The building consists of a one-story structure containing approximately 4,000 square feet of office space. The main office building provides space for four tellers in the lobby of the building, two drive-up tellers, four private offices, two night depositories, and an ATM. Adequate customer parking is available on three sides of the main office building.

Tuscola. First Mid Bank operates an office in Tuscola, Illinois, which is located at 410 South Main Street. The all brick building consists of a one-story structure with approximately 4,000 square feet of office space. This main office building provides for four lobby tellers, two drive-up tellers, four private offices, a conference room, four drive-through lanes, including one with a drive-up ATM and one with a drive-up night depository. Adequate customer parking is available outside the main entrance.

Charleston. The main office, acquired in March 1997, is located at 500 West Lincoln Avenue, Charleston, Illinois. This one-story facility contains approximately 8,400 square feet with five teller stations, eight private offices and four drive-up lanes.

A second facility is located at 701 Sixth Street, Charleston, Illinois. It is a one-story facility with an attached two-bay drive-up structure and consists of approximately 5,500 square feet of office space. Adequate parking is available to serve its customers. The office space is comprised of three teller stations, three private offices, storage area, and a night depository. Approximately 2,200 square feet of this building is rented out to non-affiliated companies.

The third facility consists of approximately 400 square feet of leased space at the Martin Luther King Student Union on the Eastern Illinois University campus. The facility has two walk-up teller stations and two sit-down teller/CSR stations.

Seven ATMs are located in Charleston. One drive-up ATM is located in the parking lot of the facility at 500 West Lincoln Avenue, one in the parking lot of Save-A-Lot at 1400 East Lincoln Avenue, and one drive-up ATM is located in the parking lot of the Sixth Street facility. The fourth is an off-site walk-up ATM located in the Student Union at Eastern Illinois University and the fifth is a walk-up ATM located in Lantz Arena at Eastern Illinois University. The sixth ATM is a drive-up unit located on the Eastern Illinois University campus in a parking lot at the corner of Ninth Street and Roosevelt and the seventh is a drive-up unit located on the Eastern Illinois University campus in a parking lot at the corner of Fourth Street and Roosevelt.

Champaign. First Mid Bank leases a facility at 2229 South Neil Street, Champaign, Illinois. The office space, comprised of approximately 3,496 square feet, contains six lobby teller windows, two drive-up lanes, one drive-up ATM, a night depository, four private offices, and a conference room. Adequate customer parking is available to serve customers.

First Mid Bank also leases a facility at 913A West Marketview, Champaign, Illinois, located in the Rural King Store. The office space is approximately 1,276 square feet, contains three teller stations, two private offices, a walk-up ATM, a night depository and a conference room.

Urbana. First Mid Bank owns a facility located at 601 South Vine Street, Urbana, Illinois. Its office building consists of a one-story structure and contains approximately 3,600 square feet. The office building provides space for three tellers, two private offices and two drive-up lanes. An ATM machine is located in front of the building. An adequate customer parking lot is located on the south side of the building.

Effingham. First Mid Bank operates a facility at 902 North Keller Drive, Effingham, Illinois. The building is a two-story structure with approximately 4,000 square feet of office space. This office space consists of four teller stations, three drive-up teller lanes, five private offices and a night depository. Adequate parking is available to customers in front of the facility.

First Mid Bank also owns property at 900 North Keller Drive, Effingham, Illinois that provides additional customer parking along with a drive-up ATM.

Altamont. First Mid Bank has a banking facility located at 101 West Washington Street, Altamont, Illinois. This building is a one-story structure that has approximately 4,300 square feet of office space. The office space consists of nine teller windows, three drive-up teller lanes (one of which facilitates an ATM), seven private offices, one conference room and a night depository. Adequate parking is available on three sides of the building.

Arcola. First Mid Bank owns a facility at 249 West Springfield Road, Arcola, Illinois. This building is a one-story structure with approximately 2,800 square feet of office space. This office space consists of three lobby teller stations, three drive-up teller lanes, three private offices, a conference room, safe deposit vault and a night depository. A drive-up ATM lane is available adjacent to the teller lanes. Adequate parking is available to customers in front of the facility. There are also two additional ATMs located at the Arcola Citgo Station on Route 133 at Interstate Five and the Arthur Citgo Station at 209 North Vine.

Monticello. First Mid Bank has two offices in Monticello. The main facility is located on the northeast corner of the historic town square at 100 West Washington Street. This building is a two-story structure that has 8,000 square feet of office space consisting of five teller stations, seven private offices, and a night depository. The second floor is furnished and the basement is used for storage. Adequate parking is available to customers in back of the facility.

A second facility is located at 219 West Center Street, Monticello, Illinois. It is a one-story facility with two lobby teller stations and an attached two-bay drive-up structure with a drive-up ATM and a night depository. Adequate parking is available to serve its customers.

Taylorville. First Mid Bank has a banking facility located at 200 North Main Street, Taylorville, Illinois. This one-story building has approximately 3,700 square feet with five teller stations, three private offices, one drive-up lane, and a finished basement. A drive-up ATM is located in the parking lot and adequate customer parking is available adjacent to the building.

Decatur. First Mid Bank leases a facility at 111 E. Main Street, Decatur, Illinois. The office space comprised of 4,340 square feet contains three lobby teller windows, two drive-up lanes, a night depository, three private offices, safe deposit and loan vaults, and a conference room. Customer parking is available adjacent to the building.

First Mid Bank also leases a facility at 3101 North Water Street, Decatur, Illinois. This one-story facility has approximately 768 square feet of office space. This office space consists of two lobby teller windows, four drive-up teller lanes and a drive-up ATM.

Highland. First Mid Bank owns a facility located at 12616 State Route 143, Highland, Illinois. The building is a two-story structure with approximately 6,720 square feet of office space, a portion of which is leased to an unaffiliated business. This office space consists of a customer service area and teller windows, three drive-up teller lanes, an ATM and four private offices. Adequate parking is available to serve customers.

First Mid Bank leases a facility located at 1301 Broadway, Highland, Illinois. The office space, comprised of 1300 square feet, contains three lobby teller windows, two drive-up lanes and one drive-up ATM, a night depository, two private offices, safe deposit and loan vaults and a conference room. Adequate parking is available to serve customers.

St. Jacob. First Mid Bank rents property at 705 N. Douglas Street, St. Jacob, Illinois where a drive-up ATM is located.

Pocahontas. First Mid Bank owns a facility located at 103 Park Street, Pocahontas, Illinois. The building is a one-story brick structure with approximately 3,360 square feet of office space. This office space consists of a customer processing room, three private offices and three bank vaults. Adequate parking is available to serve customers.

First Mid Bank also has an ATM at 4 O'Fallon Street in Powhaten Restaurant.

Maryville. First Mid leases a facility located at 2930 North Center Street, Maryville, Illinois. The office space, comprised of approximately 6,684 square feet, contains four lobby teller windows, including one sit-down teller, two drive-up lanes, one drive-up ATM, a night depository, three private offices, a vault, and a conference room. Adequate customer parking is available to serve customers.

Mansfield. First Mid Bank owns a facility at 1 Jefferson, Mansfield, Illinois. The building is a one-story structure with approximately 3,695 square feet of office space which contains a lobby with teller windows, one drive-up lane, three private offices, a vault, a conference room and a basement used for storage. Customer parking is available adjacent to the building.

Mahomet. First Mid Bank owns a facility located at 504 E. Oak Street, Mahomet, Illinois. The building is a one-story structure with approximately 3,045 square feet of office space which contains a lobby with teller windows, a drive-up lane, an ATM, two private offices, a vault, a conference room and a basement used for storage. Adequate customer parking is available to serve customers.

Weldon. First Mid Bank owns a facility located at Oak and Maple, Weldon, Illinois. The building is a two-story structure with approximately 5,964 square feet of office space which contains a lobby with teller windows, a drive-up lane, four private offices, two vaults, a conference room and a basement used for storage. Offices on the second floor have been leased to a separate entity. Adequate customer parking is available to serve customers.

Checkley

Mattoon. Checkley leases a facility located at 100 Lerna South, Mattoon, Illinois. The office space, comprised of approximately 8,829 square feet, contains ten offices, two conference rooms, a file room and an open work area that can accommodate nine workstations. Adequate parking is available to serve customers.

ITEM 3. LEGAL PROCEEDINGS

Since First Mid Bank acts as a depository of funds, it is named from time to time as a defendant in lawsuits (such as garnishment proceedings) involving claims to the ownership of funds in particular accounts. Management believes that all such litigation as well as other pending legal proceedings, in which the Company is involved, constitute ordinary routine litigation incidental to the business of the Company and that such litigation will not materially adversely affect the Company’s consolidated financial condition or results of operations.

ITEM 4. [RESERVED]

PART II

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

The Company's common stock was held by approximately 609 shareholders of record as of December 31, 2009 and is included for quotation on the over-the-counter electronic bulletin board.

The following table shows the high and low bid prices per share of the Company's common stock for the indicated periods. These quotations represent inter-dealer prices without retail mark-ups, mark-downs or commissions and may not necessarily represent actual transactions.

Quarter	High	Low
2009		
4th	$19.90	$16.55
3rd	$19.90	$17.10
2nd	$20.00	$16.00
1st	$22.20	$18.00
2008		
4th	$26.00	$13.00
3rd	$28.50	$24.45
2nd	$27.75	$24.90
1st	$26.15	$23.40

The following table sets forth the cash dividends per share on the Company's common stock for the last two years.

Date Declared	Date Paid	Dividend Per Share
12-15-2009	1-07-2010	$.190
4-29-2009	6-08-2009	$.190
12-16-2008	1-05-2009	$.190
4-30-2008	6-16-2008	$.190

On June 29, 2007, the Company effected a three-for-two stock split in the form of a 50% stock dividend. Par value remained at $4 per share. All share and per share amounts have been restated for years prior to 2007 to give retroactive recognition to the stock split.

The Company's shareholders are entitled to receive such dividends as are declared by the Board of Directors, which considers payment of dividends semi-annually. The ability of the Company to pay dividends, as well as fund its operations, is dependent upon receipt of dividends from First Mid Bank. Regulatory authorities limit the amount of dividends that can be paid by First Mid Bank without prior approval from such authorities. For further discussion of First Mid Bank's dividend restrictions, see Item1 – "Business" – "First Mid Bank" – "Dividends" and Note 17 – "Dividend

Restrictions" herein. The Board of Directors of the Company declared cash dividends semi-annually during the two years ended December 31, 2009.

The following table summarizes share repurchase activity for the fourth quarter of 2009:

ISSUER PURCHASES OF EQUITY SECURITIES				
Period	(a) Total Number of Shares Purchased	(b) Average Price Paid per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	(d) Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs at End of Period
October 1, 2009 – October 31, 2009	0	$0.00	0	$4,860,000
November 1, 2009 – November 30, 2009	41,756	$18.61	41,756	$4,083,000
December 1, 2009 – December 31, 2009	35,215	$18.91	35,215	$3,417,000
Total	76,971	$18.75	76,971	$3,417,000

Since August 5, 1998, the Board of Directors has approved repurchase programs pursuant to which the Company may repurchase a total of approximately $56.7 million of the Company’s common stock. The repurchase programs approved by the Board of Directors are as follows:

- On August 5, 1998, repurchases of up to 3%, or $2 million, of the Company’s common stock.
- In March 2000, repurchases up to an additional 5%, or $4.2 million of the Company’s common stock.
- In September 2001, repurchases of $3 million of additional shares of the Company’s common stock.
- In August 2002, repurchases of $5 million of additional shares of the Company’s common stock.
- In September 2003, repurchases of $10 million of additional shares of the Company’s common stock.
- On April 27, 2004, repurchases of $5 million of additional shares of the Company’s common stock.
- On August 23, 2005, repurchases of $5 million of additional shares of the Company’s common stock.
- On August 22, 2006, repurchases of $5 million of additional shares of the Company’s common stock.
- On February 27, 2007, repurchases of $5 million of additional shares of the Company’s common stock.
- On November 13, 2007, repurchases of $5 million of additional shares of the Company’s common stock.
- On December 16, 2008, repurchases of $2.5 million of additional shares of the Company’s common stock.
- On May 26, 2009, repurchases of $5 million of additional shares of the Company’s common stock.

ITEM 6. SELECTED FINANCIAL DATA

The following sets forth a five-year comparison of selected financial data (dollars in thousands, except per share data).

	2009	2008	2007	2006	2005
Summary of Operations					
Interest income	$51,409	$57,066	$59,931	$55,556	$44,580
Interest expense	15,837	21,344	28,429	24,712	15,687
Net interest income	35,572	35,722	31,502	30,844	28,893
Provision for loan losses	3,594	3,559	862	760	1,091
Other income	13,455	15,264	14,661	13,380	12,518
Other expense	33,212	31,460	30,055	28,423	25,385
Income before income taxes	12,221	15,967	15,246	15,041	14,935
Income tax expense	4,007	5,443	5,087	5,032	5,128
Net income	8,214	10,524	10,159	10,009	9,807
Dividends on preferred shares	1,821	-	-	-	-
Net income available to common stockholders	$6,393	$10,524	$10,159	$10,009	$9,807
Per Common Share Data (1)					
Basic earnings per share	$1.04	$1.69	$1.60	$1.54	$1.48
Diluted earnings per share	1.04	1.67	1.57	1.51	1.44
Dividends per share	.38	.38	.38	.35	.33
Book value per share	14.23	13.50	12.82	11.78	10.98
Capital Ratios					
Total capital to risk-weighted assets	15.76 %	11.99 %	11.13 %	10.91 %	11.87 %
Tier 1 capital to risk-weighted assets	14.57 %	11.02 %	10.32 %	10.10 %	11.14 %
Tier 1 capital to average assets	10.63 %	8.41 %	7.89 %	7.56 %	8.55 %
Financial Ratios					
Net interest margin	3.40 %	3.73 %	3.43 %	3.51 %	3.70 %
Return on average assets	.74 %	1.03 %	1.03 %	1.07 %	1.18 %
Return on average common equity	9.56 %	12.87 %	13.06 %	13.31 %	13.64 %
Dividend on common shares payout ratio	36.54 %	22.49 %	23.75 %	22.51 %	22.55 %
Average equity to average assets	9.59 %	8.00 %	7.90 %	8.01 %	8.64 %
Allowance for loan losses as a percent of total loans	1.35 %	1.02 %	0.82 %	0.81 %	0.73 %
Year End Balances					
Total assets	$1,095,155	$1,049,700	$1,016,338	$980,559	$850,573
Net loans	691,288	734,351	742,043	717,692	631,707
Total deposits	840,410	806,354	770,583	770,595	649,069
Total equity	111,221	82,778	80,452	75,786	72,326
Average Balances					
Total assets	$1,108,669	$1,022,734	$985,230	$938,784	$832,752
Net loans	692,961	733,681	722,672	686,069	606,064
Total deposits	744,043	795,786	771,561	737,344	650,116
Total equity	106,295	81,793	77,787	75,174	71,911

(1) All share and per share data have been restated to reflect the 3-for-2 stock split effective June 29, 2007.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis is intended to provide a better understanding of the consolidated financial condition and results of operations of the Company and its subsidiaries for the years ended December 31, 2009, 2008 and 2007. This discussion and analysis should be read in conjunction with the consolidated financial statements, related notes and selected financial data appearing elsewhere in this report.

Forward-Looking Statements

This report contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, such as discussions of the Company's pricing and fee trends, credit quality and outlook, liquidity, new business results, expansion plans, anticipated expenses and planned schedules. The Company intends such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995, and is including this statement for purposes of these safe harbor provisions. Forward-looking statements, which are based on certain assumptions and describe future plans, strategies and expectations of the Company, are identified by use of the words "believe," "expect," "intend," "anticipate," "estimate," "project," or similar expressions. Actual results cou differ materially from the results indicated by these statements because the realization of those results is subject to many uncertainties including: changes in interest rates, general economic conditions and those in the Company's market area, legislative/regulatory changes, monetary and fiscal policies of the U.S. Government, including policies of the U.S. Treasury and the Federal Reserve Board, the quality or composition of the loan or investment portfolios and the valuation of the investment portfolio, demand for loan products, deposit flows, competition, demand for financial services in the Company's market area and accounting principles, policies and guidelines. These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements. Further information concerning the Company and its business, including additional factors that could materially affect the Company's financial results, is included in Item 1A of this Annual Report on Form 10-K captioned "Risk Factors" and elsewhere in the filing and the Company's other filings with the SEC. Furthermore, forward-looking statements speak only as of the date they are made. Except as required under the federal securities laws or the rules and regulations of the SEC, we do not undertake any obligation to update or review any forward-looking information, whether as a result of new information, future events or otherwise.

For the Years Ended December 31, 2009, 2008 and 2007

Overview

This overview of management's discussion and analysis highlights selected information in this document and may not contain all of the information that is important to you. For a more complete understanding of trends, events, commitments, uncertainties, liquidity, capital resources, and critical accounting estimates, you should carefully read this entire document. These have an impact on the Company's financial condition and results of operations.

Net income was $8.21 million, $10.52 million, and $10.16 million and diluted earnings per share were $1.04, $1.67, and $1.57 for the years ended December 31, 2009, 2008, and 2007, respectively. The decrease in net income in 2009 was primarily the result of an increase in FDIC insurance assessment charges and other-than-temporary impairment losses on securities for the year. The decrease in earnings per share in 2009 was primarily the result of lower net income for the year. The following table shows the Company's annualized performance ratios for the years ended December 31, 2009, 2008 and 2007:

	2009		2008		2007	
Return on average assets	.74	%	1.03	%	1.03	%
Return on average common equity	9.56	%	12.87	%	13.06	%
Average common equity to average assets	9.59	%	8.00	%	7.90	%

Total assets at December 31, 2009, 2008, and 2007 were $1,095.2 million, $1,049.7 million, and $1,016.3 million, respectively. The increase in net assets during 2009 was primarily due to an increase in federal funds sold by the Company and increases in available-for-sale securities, offset by decreases in net loans. Net loan balances decreased to $691.1 million at December 31, 2009, from $733.8 million at December 31, 2008 and compared to $740.1 million at December 31, 2007. The decrease in 2009 of $42.7 million or 5.8% was due to reduced loan demand as a result of the sluggish economy. Total deposit balances increased to $840.4 million at December 31, 2009 from $806.4 million at December 31, 2008 and from $770.6 million at December 31, 2007. The increase in 2009 was primarily due to increased balances in money market deposits and savings accounts.

Net interest margin, defined as net interest income divided by average interest-earning assets, was 3.40% for 2009, 3.73% for 2008 and 3.43% for 2007. The decrease in interest margin during 2009 was the result of a greater decrease in interest-earning asset rates compared to the decrease in borrowing and deposit rates and a greater level of liquidity maintained by the Company during 2009. The decrease in interest margin during 2008 was the result of greater decrease in borrowing and deposit rates compared to the decrease in interest-earning asset rates.

Net interest income decreased slightly to $35.6 million in 2009 from $35.7 million in 2008 and $31.5 million in 2007. The ability of the Company to continue to grow net interest income is largely dependent on management's ability to succeed in its overall business development efforts. Management expects these efforts to continue but does not intend to compromise credit quality and prudent management of the maturities of interest-earning assets and interest-paying liabilities in order to achieve growth.

Non-interest income decreased to $13.5 million in 2009 compared to $15.3 million in 2008 and $14.7 million in 2007. The primary reasons for the decrease of $1.8 million or 11.9% from 2008 to 2009 were decreases in trust revenues and brokerage commissions and other-than-temporary impairment charges on investment securities offset by a $1 million gain on the sale of the Bank's merchant card servicing portfolio. The primary reasons for the increase of $.6 million or 4.1% from 2007 to 2008 were increases in ATM and debit card transaction fees during 2008 compared to 2007, and approximately $291,000 in proceeds on life insurance the Company maintained on former executive and director, Daniel E. Marvin, Jr., who died in April of 2008.

Non-interest expenses increased $1.7 million, to $33.2 million in 2009 compared to $31.5 million in 2008 and $30.1 million in 2007. The primary factor for the increase during 2009 was an increase in FDIC insurance assessments. The primary factors in the increase during 2008 were additional salaries and benefits expense as a result of merit increases for continuing employees, increases in loan collection expenses and the write down of the DeLand property of $132,000 during the first quarter of 2008.

Following is a summary of the factors that contributed to the changes in net income (in thousands):

	2009 vs 2008	2008 vs 2007
Net interest income	$(150)	$4,220
Provision for loan losses	(35)	(2,697)
Other income, including securities transactions	(1,809)	603
Other expenses	(1,752)	(1,405)
Income taxes	1,436	(356)
Increase (decrease) in net income	$(2,310)	$365

Credit quality is an area of importance to the Company. Year-end total nonperforming loans were $12.7 million at December 31, 2009 compared to $7.3 million at December 31, 2008 and $7.5 million at December 31, 2007. The increase in 2009 occurred as a result of loans that became nonperforming during the year due to continued deterioration in economic conditions including increased unemployment, reduction in cash flow from increased vacancies in commercial properties, and declines in property values. Other real estate owned balances totaled $2.9 million at December 31, 2009 compared to $2.4 million at December 31, 2008. The Company's provision for loan losses was $3,594,000 for 2009 compared to $3,559,000 for 2008. At December 31, 2009, the composition of the loan portfolio remained similar to 2008. Loans secured by both commercial and residential real estate comprised 74% of the loan portfolio as of December 31, 2009 and 2008.

The Company also held investments in four trust preferred securities with a fair value of $3.2 million and unrealized losses of $4.6 million at December 31, 2009 compared to a fair value of $5.4 million and unrealized losses of $4 million at December 31, 2008. During 2009, the Company recorded $1.8 million of other-than-temporary impairment charges for the credit portion of the unrealized losses of these securities. The loss established a new, lower amortized cost basis for these securities and reduced non-interest income. See Note 4 – "Investment Securities" for additional details regarding these investments.

The Company's capital position remains strong and the Company has consistently maintained regulatory capital ratios above the "well-capitalized" standards. The Company's Tier 1 capital ratio to risk weighted assets ratio at December 31, 2009, 2008, and 2007 was 14.57%, 11.02%, and 10.32%, respectively. The Company's total capital to risk weighted assets ratio at December 31, 2009, 2008, and 2007 was 15.76%, 11.99%, and 11.13%, respectively. The increase in 2009 was primarily the result of an increase in retained earnings due to the Company's net income and the issuance of $24,635,000 of Series B 9% Non-Cumulative Perpetual Convertible Preferred Stock. (See "Preferred Stock" in Note 1 to consolidated financial statements for more detailed information.) The increase in 2008 was primarily the result of an increase in retained earnings due to the Company's increase in net income and changes in federal banking and thrift regulatory agencies rules that permit banking organizations to reduce the amount of goodwill that must be deducted from tier 1 capital by any associated deferred tax liability.

The Company's liquidity position remains sufficient to fund operations and meet the requirements of borrowers, depositors, and creditors. The Company maintains various sources of liquidity to fund its cash needs. See "Liquidity" herein for a full listing of its sources and anticipated significant contractual obligations.

The Company enters into financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include lines of credit, letters of credit and other commitments to extend credit. The total outstanding commitments at December 31, 2009, 2008 and 2007 were $132.9 million, $152.9 million and $152.7 million, respectively. See Note 18 – "Commitments and Contingent Liabilities" herein for further information.

Critical Accounting Policies and Use of Significant Estimates

The Company has established various accounting policies that govern the application of U.S. generally accepted accounting principles in the preparation of the Company's financial statements. The significant accounting policies of the Company are described in the footnotes to the consolidated financial statements. Certain accounting policies involve significant judgments and assumptions by management that have a material impact on the carrying value of certain assets and liabilities; management considers such accounting policies to be critical accounting policies. The judgments and assumptions used by management are based on historical experience and other factors, which are believed to be reasonable under the circumstances. Because of the nature of the judgments and assumptions made by management, actual results could differ from these judgments and assumptions, which could have a material impact on the carrying values of assets and liabilities and the results of operations of the Company.

Allowance for Loan Losses. The Company believes the allowance for loan losses is the critical accounting policy that requires the most significant judgments and assumptions used in the preparation of its consolidated financial statements. An estimate of potential losses inherent in the loan portfolio are determined and an allowance for those losses is established by considering factors including historical loss rates, expected cash flows and estimated collateral values. In assessing these factors, the Company use organizational history and experience with credit decisions and related outcomes. The allowance for loan losses represents the best estimate of losses inherent in the existing loan portfolio. The allowance for loan losses is increased by the provision for loan losses charged to expense and reduced by loans charged off, net of recoveries. The Company evaluates the allowance for loan losses quarterly. If the underlying assumptions later prove to be inaccurate based on subsequent loss evaluations, the allowance for loan losses is adjusted.

The Company estimates the appropriate level of allowance for loan losses by separately evaluating impaired and nonimpaired loans. A specific allowance is assigned to an impaired loan when expected cash flows or collateral do not justify the carrying amount of the loan. The methodology used to assign an allowance to a nonimpaired loan is more subjective. Generally, the allowance assigned to nonimpaired loans is determined by applying historical loss rates to existing loans with similar risk characteristics, adjusted for qualitative factors including the volume and severity of identified classified loans, changes in economic conditions, changes in credit policies or underwriting standards, and changes in the level of credit risk associated with specific industries and markets. Because the economic and business climate in any given industry or market, and its impact on any given borrower, can change rapidly, the risk profile of the loan portfolio is continually assessed and adjusted when appropriate. Notwithstanding these procedures, there still exists the possibility that the assessment could prove to be significantly incorrect and that an immediate adjustment to the allowance for loan losses would be required.

Other Real Estate Owned. Other real estate owned acquired through loan foreclosure are initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. The adjustment at the time of foreclosure is recorded through the allowance for loan losses. Due to the subjective nature of establishing the fair value when the asset is acquired, the actual fair value of the other real estate owned or foreclosed asset could differ from the original estimate. If it is determined that fair value temporarily declines subsequent to foreclosure, a valuation allowance is recorded through noninterest expense. Operating costs associated with the assets after acquisition are also recorded as noninterest expense. Gains and losses on the disposition of other real estate owned and foreclosed assets are netted and posted to other noninterest expense.

Investment in Debt and Equity Securities. The Company classifies its investments in debt and equity securities as either held-to-maturity or available-for-sale in accordance with Statement of Financial Accounting Standards (SFAS) No. 115, “Accounting for Certain Investments in Debt and Equity Securities,” which was codified into ASC 320. Securities classified as held-to-maturity are recorded at cost or amortized cost. Available-for-sale securities are carried at fair value. Fair value calculations are based on quoted market prices when such prices are available. If quoted market prices are not available, estimates of fair value are computed using a variety of techniques, including extrapolation from the quoted prices of similar instruments or recent trades for thinly traded securities, fundamental analysis, or through obtaining purchase quotes. Due to the subjective nature of the valuation process, it is possible that the actual fair values of these investments could differ from the estimated amounts, thereby affecting the financial position, results of operations and cash flows of the Company. If the estimated value of investments is less than the cost or amortized cost, the Company evaluates whether an event or change in circumstances has occurred that may have a significant adverse effect on the fair value of the investment. If such an event or change has occurred and the Company determines that the impairment is other-than-temporary, a further determination is made as to the portion of impairment that is related to credit loss. The impairment of the investment that is related to the credit loss is expensed in the period in which the event or change occurred. The remainder of the impairment is recorded in other comprehensive income.

Deferred Income Tax Assets/Liabilities. The Company’s net deferred income tax asset arises from differences in the dates that items of income and expense enter into our reported income and taxable income. Deferred tax assets and liabilities are established for these items as they arise. From an accounting standpoint, deferred tax assets are reviewed to determine if they are realizable based on the historical level of taxable income, estimates of future taxable income and the reversals of deferred tax liabilities. In most cases, the realization of the deferred tax asset is based on future profitability. If the Company were to experience net operating losses for tax purposes in a future period, the realization of deferred tax assets would be evaluated for a potential valuation reserve.

Additionally, the Company reviews its uncertain tax positions annually under FASB Interpretation No. 48 (FIN No. 48), “Accounting for Uncertainty in Income Taxes,” codified within ASC 740. An uncertain tax position is recognized as a benefit only if it is "more likely than not" that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount actually recognized is the largest amount of tax benefit that is greater than 50% likely to be recognized on examination. For tax positions not meeting the "more likely than not" test, no tax benefit is recorded. A significant amount of judgment is applied to determine both whether the tax position meets the "more likely than not" test as well as to determine the largest amount of tax benefit that is greater than 50% likely to be recognized. Differences between the position taken by management and that of taxing authorities could result in a reduction of a tax benefit or increase to tax liability, which could adversely affect future income tax expense.

Impairment of Goodwill and Intangible Assets. Core deposit and customer relationships, which are intangible assets with a finite life, are recorded on the Company’s balance sheets. These intangible assets were capitalized as a result of past acquisitions and are being amortized over their estimated useful lives of up to 15 years. Core deposit intangible assets, with finite lives will be tested for impairment when changes in events or circumstances indicate that its carrying amount may not be recoverable. Core deposit intangible assets were tested for impairment during 2009 as part of the goodwill impairment test and no impairment was deemed necessary.

As a result of the Company’s acquisition activity, goodwill, an intangible asset with an indefinite life, was reflected on the balance sheets in prior periods. Goodwill is evaluated for impairment annually, unless there are factors present that indicate a potential impairment, in which case, the goodwill impairment test is performed more frequently than annually.

Fair Value Measurements. The fair value of a financial instrument is defined as the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. The Company estimates the fair value of a financial instrument using a variety of valuation methods. Where financial instruments are actively traded and have quoted market prices, quoted market prices are used for fair value. When the financial instruments are not actively traded, other observable market inputs, such as quoted prices of securities with similar characteristics, may be used, if available, to determine fair value. When observable market prices do not exist, the Company estimates fair value. The Company's valuation methods consider factors such as liquidity and concentration concerns. Other factors such as model assumptions, market dislocations, and unexpected correlations can affect estimates of fair value. Imprecision in estimating these factors can impact the amount of revenue or loss recorded.

SFAS No. 157, "Fair Value Measurements", which was codified into ASC 820, establishes a framework for measuring the fair value of financial instruments that considers the attributes specific to particular assets or liabilities and establishes a three-level hierarchy for determining fair value based on the transparency of inputs to each valuation as of the fair value measurement date. The three levels are defined as follows:

- Level 1 — quoted prices (unadjusted) for identical assets or liabilities in active markets.
- Level 2 — inputs include quoted prices for similar assets and liabilities in active markets, quoted prices of identical or similar assets or liabilities in markets that are not active, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.
- Level 3 — inputs that are unobservable and significant to the fair value measurement.

At the end of each quarter, the Company assesses the valuation hierarchy for each asset or liability measured. From time to time, assets or liabilities may be transferred within hierarchy levels due to changes in availability of observable market inputs to measure fair value at the measurement date. Transfers into or out of hierarchy levels are based upon the fair value at the beginning of the reporting period. A more detailed description of the fair values measured at each level of the fair value hierarchy can be found in Note 12 – "Disclosures of Fair Values of Financial Instruments."

Properties

On September 29, 2007, the Company closed its facilities located at 435 South Hamilton, Sullivan, Illinois in the IGA and at 220 North Highway Avenue, DeLand, Illinois. The customers and operations of both of these facilities were moved to other facilities in Sullivan and Monticello, Illinois. These actions did not have a material impact on the Company's consolidated financial statements.

During the first quarter of 2008, the Company obtained an independent appraisal of the DeLand property in anticipation of possibly donating or selling this property. Subsequently, the Company adjusted its carrying value of the property to the appraised value which resulted in a loss of $132,000 in the consolidated financial statements. The property was sold during the first quarter of 2009 for its appraised value of $50,000.

Temporary Liquidity Guarantee Program

On October 14, 2008, the FDIC announced the Temporary Liquidity Guarantee Program (TLGP). The final rule was adopted on November 21, 2008. The FDIC stated that the purpose of these actions is to strengthen confidence and encourage liquidity in the banking system by guaranteeing newly issued senior unsecured debt of 31 days or greater, of banks, thrifts, and certain holding companies, and by providing full FDIC insurance coverage for all non-interest bearing transaction accounts, regardless of dollar amount. Inclusion in the program was voluntary. Institutions participating in the senior unsecured debt portion of the program are assessed fees based on a sliding scale, depending on length of maturity. Shorter-term debt has a lower fee structure and longer-term debt has a higher fee. The range is from 50 basis points on debt of 180 days or less, to a maximum of 100 basis points for debt with maturities of one year or longer, on an annualized basis. A 10-basis point surcharge is added to a participating institution's current insurance assessment in exchange for final coverage for all transaction accounts.

First Mid Bank elected to participate in both parts of the TLGP, the Transaction Account Guarantee Program and the Debt Guarantee Program. The FDIC’s Transaction Account Guarantee Program, provides, without charge to depositors, a full guarantee on all non-interest bearing transaction accounts held by any depositor, regardless of dollar amount, through June 30, 2010. Participation in the Transaction Account Guarantee Program cost the Company 10 basis points annually on the amount of the deposits. The FDIC’s Debt Guarantee Program, which expired in October 2009, provided for the guarantee of eligible newly issued senior unsecured debt of participating entities, but the Company and the Bank did not issue any debt under this program.

Federal Deposit Insurance Corporation Insurance Coverage

As an FDIC-insured institution, First Mid Bank is required to pay deposit insurance premium assessments to the FDIC.

On October 3, 2008, the FDIC temporarily increased the standard maximum deposit insurance amount (SMDIA) from $100,000 to $250,000 per depositor. On May 20, 2009, the Helping Families Save Their Homes Act extended the temporary increase in the SMDIA through December 31, 2013. This extension of the temporary $250,000 coverage limit became effective immediately upon the President’s signature. The legislation provides that the SMDIA will return to $100,000 on January 1, 2014. The additional cost of the increase to the SMDIA, assessed on a quarterly basis, is a 10 basis point annualized surcharge (2.5 basis points quarterly) on balances in non-interest bearing transaction accounts that exceed $250,000. The Company has expensed $49,000 for this program in 2009.

On February 27, 2009, the FDIC adopted a final rule modifying the risk-based assessment system and setting initial base assessment rates beginning April 1, 2009, at 12 to 45 basis points and, due to extraordinary circumstances, extended the period of the restoration plan to increase the deposit insurance fund to seven years. Also on February 27, 2009, the FDIC issued final rules on changes to the risk-based assessment system. The final rules both increase base assessment rates and incorporate additional assessments for excess reliance on brokered deposits and FHLB advances. The new rates would increase annual assessment rates from 5 to 7 basis points to 7 to 24 basis points. This new assessment took effect April 1, 2009. The Company has expensed $1,260,000 for this assessment in 2009.

Also on February 27, 2009, the FDIC adopted an interim rule to impose a 20 basis point emergency special assessment payable September 30, 2009 based on the second quarter 2009 assessment base, to help shore up the Deposit Insurance Fund ("DIF"). This assessment equates to a one-time cost of $200,000 per $100 million in assessment base. The interim rule also allows the Board to impose possible additional special assessments of up to 10 basis points thereafter to maintain public confidence in the DIF. Subsequently, the FDIC's Treasury borrowing authority increased from $30 billion to $100 billion, allowing the agency to cut the planned special assessment from 20 to 10 basis points. On May 22, 2009, the FDIC adopted a final rule which established a special assessment of five basis points on each FDIC-insured depository institutions assets, minus it Tier 1 capital, as of September 30, 2009. The assessment was capped at 10 basis points of an institution's domestic deposits so that no institution would pay an amount higher than they would have under the interim rule. This special assessment was collected September 30, 2009. The Company expensed $522,000 as of June 30, 2009 for this special assessment.

In addition to its insurance assessment, each insured bank was subject, in 2009, to quarterly debt service assessments in connection with bonds issued by a government corporation that financed the federal savings and loan bailout. The Company expensed $112,000 during 2009 for this assessment.

On September 29, 2009, the FDIC Board proposed a Deposit Insurance Fund restoration plan that required banks 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. Under the plan—which applies to all banks except those with liquidity problems—banks were assessed through 2010 according to the risk-based premium schedule adopted earlier this year. Beginning January 1, 2011, the base rate increases by 3 basis points. The Company recorded a prepaid expense asset of $4,855,000 as of December 31, 2009 as a result of this plan. This asset will be amortized to non-interest expense over the next three years.

Results of Operations

Net Interest Income

The largest source of operating revenue for the Company is net interest income. Net interest income represents the difference between total interest income earned on earning assets and total interest expense paid on interest-bearing liabilities. The amount of interest income is dependent upon many factors, including the volume and mix of earning assets, the general level of interest rates and the dynamics of changes in interest rates. The cost of funds necessary to support earning assets varies with the volume and mix of interest-bearing liabilities and the rates paid to attract and retain such funds.

The Company’s average balances, interest income and expense and rates earned or paid for major balance sheet categories are set forth in the following table (dollars in thousands):

	Year Ended December 31, 2009			Year Ended December 31, 2008			Year Ended December 31, 2007		
	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate
ASSETS									
Interest-bearing deposits	$ 59,597	$ 161	0.27%	$ 26,697	$ 423	1.59%	$ 265	$ 13	5.02%
Federal funds sold	54,630	66	0.12%	19,266	336	1.75%	4,012	201	5.00%
Investment securities									
Taxable	207,025	8,073	3.90%	151,752	7,725	5.09%	169,425	8,448	4.99%
Tax-exempt (1)	23,384	963	4.12%	20,312	834	4.11%	17,242	712	4.13%
Loans (2) (3)	701,521	42,146	6.01%	740,083	47,748	6.45%	728,790	50,557	6.94%
Total earning assets	1,046,157	51,409	4.91%	958,110	57,066	5.96%	919,734	59,931	6.52%
Cash and due from banks	18,634			19,433			19,361		
Premises and equipment	15,333			15,160			15,888		
Other assets	37,105			36,433			36,365		
Allowance for loan losses	(8,560)			(6,402)			(6,118)		
Total assets	$1,108,669			$1,022,734			$985,230		
LIABILITIES AND STOCKHOLDERS’ EQUITY									
Deposits:									
Demand deposits, interest-bearing	$332,751	2,843	0.85%	$288,057	3,635	1.26%	$271,117	6,459	2.38%
Savings deposits	109,305	938	0.86%	74,236	680	0.92%	60,654	349	0.58%
Time deposits	301,987	9,189	3.04%	313,729	12,277	3.91%	325,397	14,783	4.54%
Securities sold under agreements to repurchase	72,589	129	0.18%	61,108	872	1.43%	54,962	2,419	4.40%
FHLB advances	36,175	1,612	4.46%	41,370	1,991	4.81%	34,912	1,728	4.95%
Federal funds purchased	3	-	.47%	-	-	-%	3,907	206	5.27%
Subordinated debentures	20,620	1,104	5.36%	20,620	1,396	6.77%	20,620	1,570	7.61%
Other debt	1,498	22	1.48%	15,113	493	3.26%	14,345	915	6.39%
Total interest-bearing liabilities	874,928	15,837	1.81%	814,233	21,344	2.62%	785,914	28,429	3.62%
Demand deposits	119,537			119,764			114,393		
Other liabilities	7,909			6,944			7,136		
Stockholders’ equity	106,295			81,793			77,787		
Total liabilities & equity	$1,108,669			$1,022,734			$985,230		
Net interest income		$35,572			$35,722			$31,502	
Net interest spread			3.10%			3.34%			2.90%

Impact of non-interest bearing funds	.30%	.39%	.53%
Net yield on interest-earning assets	3.40%	3.73%	3.43%

(1) The tax-exempt income is not recorded on a tax equivalent basis.
(2) Nonaccrual loans have been included in the average balances.
(3) Includes loans held for sale.

Changes in net interest income may also be analyzed by segregating the volume and rate components of interest income and interest expense. The following table summarizes the approximate relative contribution of changes in average volume and interest rates to changes in net interest income for the past two years (in thousands):

	2009 Compared to 2008 Increase – (Decrease)			2008 Compared to 2007 Increase – (Decrease)		
	Total Change	Volume (1)	Rate (1)	Total Change	Volume (1)	Rate (1)
Earning Assets:						
Interest-bearing deposits	$(262)	$264	$(526)	$410	$425	$(15)
Federal funds sold	(270)	238	(508)	135	337	(202)
Investment securities:						
Taxable	348	2,412	(2,064)	(723)	(890)	167
Tax-exempt (2)	129	127	2	122	126	(4)
Loans (3)	(5,602)	(2,426)	(3,176)	(2,809)	780	(3,589)
Total interest income	(5,657)	615	(6,272)	(2,865)	778	(3,643)
Interest-Bearing Liabilities:						
Deposits:						
Demand deposits, interest-bearing	(792)	507	(1,299)	(2,824)	381	(3,205)
Savings deposits	258	305	(47)	331	92	239
Time deposits	(3,088)	(445)	(2,643)	(2,506)	(515)	(1,991)
Securities sold under agreements to repurchase	(743)	139	(882)	(1,547)	244	(1,791)
FHLB advances	(379)	(240)	(139)	263	313	(50)
Federal funds purchased	-	-	-	(206)	(206)	-
Subordinated debentures	(292)	-	(292)	(174)	-	(174)
Other debt	(471)	(293)	(178)	(422)	48	(470)
Total interest expense	(5,507)	(27)	(5,480)	(7,085)	357	(7,442)
Net interest income	$(150)	$642	$(792)	$4,220	$421	$3,799

(1) Changes attributable to the combined impact of volume and rate have been allocated proportionately to the change due to volume and the change due to rate.
(2) The tax-exempt income is not recorded on a tax equivalent basis.
(3) Nonaccrual loans are not material and have been included in the average balances.

Net interest income decreased $150,000, or .4% in 2009, compared to an increase of $4,220,000, or 13.4% in 2008. The decrease in net interest income in 2009 was primarily due to a greater decline in rates on interest-bearing assets than the decline in rates on interest-bearing liabilities and the Company maintained a greater amount of liquidity at a reduced margin. The increase in net interest income in 2008 was primarily due to a greater decline in rates on interest-bearing liabilities then the decline in rates on interest-bearing assets.

In 2009, average earning assets increased by $88.0 million, or 9.2%, and average interest-bearing liabilities increased $60.7 million or 7.5% compared with 2008. In 2008, average earning assets increased by $38.4 million, or 4.2%, and average interest-bearing liabilities increased $28.3 million or 3.6% compared with 2007. Changes in average balances are shown below:

- Average interest-bearing deposits held by the Company increased $32.9 million or 123.2% in 2009 compared to 2008. In 2008, average interest-bearing deposits held by the Company increased $26.4 million or 9962.3% compared to 2007.

- Average federal funds sold increased $35.4 million or 183.7% in 2009 compared to 2008. In 2008, average federal funds sold increased $15.3 million or 381.4% compared to 2007.

- Average loans decreased by $38.6 million or 5.2% in 2009 compared to 2008. In 2008, average loans increased by $11.3 million or 1.6% compared to 2007.

- Average securities increased by $58.3 million or 33.9% in 2009 compared to 2008. In 2008, average securities decreased by $14.6 million or 7.8% compared to 2007.

- Average deposits increased by $68.0 million or 10.1% in 2009 compared to 2008. In 2008, average deposits increased by $18.9 million or 2.9% compared to 2007.

- Average securities sold under agreements to repurchase increased by $11.5 million or 18.8% in 2009 compared to 2008. In 2008, average securities sold under agreements to repurchase increased by $6.1 million or 11.1% compared to 2007.

- Average borrowings and other debt decreased by $18.8 million or 24.4% in 2009 compared to 2008. In 2008, average borrowings and other debt increased by $3.3 million or 4.5% compared to 2007.

- The federal funds rate remained at a range of 0-.25% at December 31, 2009 and 2008. The federal funds rate was 4.25% at December 31, 2007.

- Net interest margin decreased to 3.40% compared to 3.73% in 2008 and 3.43% in 2007. Asset yields decreased by 105 basis points in 2009, while interest-bearing liabilities decreased by 81 basis points.

To compare the tax-exempt yields on interest-earning assets to taxable yields, the Company also computes non-GAAP net interest income on a tax equivalent basis (TE) where the interest earned on tax-exempt securities is adjusted to an amount comparable to interest subject to normal income taxes, assuming a federal tax rate of 34% (referred to as the tax equivalent adjustment). The TE adjustments to net interest income for 2009, 2008 and 2007 were $497,000, $430,000 and $366,000, respectively. The net yield on interest-earning assets (TE) was 3.46% in 2009, 3.79% in 2008 and 3.48% in 2007.

Provision for Loan Losses

The provision for loan losses in 2009 was $3,594,000 compared to $3,559,000 in 2008 and $862,000 in 2007. Nonperforming loans increased to $12,720,000 at December 31, 2009 from $7,285,000 at December 31, 2008 and compared to $7,481,000 at December 31, 2007. The increase in 2009 occurred as a result of loans that became nonperforming during the year due to continued deterioration in economic conditions including increased unemployment, reduction in cash flow from increased vacancies in commercial properties and declines in property values. Net charge-offs were $1,719,000 during 2009, $2,090,000 during 2008, and $620,000 during 2007. For information on loan loss experience and nonperforming loans, see “Nonperforming Loans and Repossessed Assets” and “Loan Quality and Allowance for Loan Losses” herein.

Other Income

An important source of the Company’s revenue is derived from other income. The following table sets forth the major components of other income for the last three years (in thousands):

				$ Change From Prior Year	
	2009	2008	2007	2009	2008
Trust	$2,229	$2,666	$2,607	$(437)	$59

Brokerage	424	574	528	(150)	46
Insurance commissions	1,912	1,978	1,950	(66)	28
Service charges	4,952	5,571	5,621	(619)	(50)
Securities gains	637	293	256	344	37
Impairment losses on securities	(1,812)	-	-	(1,812)	-
Gain on sale of merchant banking portfolio	1,000	-	-	1,000	-
Mortgage banking	664	437	482	227	(45)
Other	3,449	3,745	3,217	(296)	528
Total other income	$13,455	$15,264	$14,661	$(1,809)	$603

Total non-interest income decreased to $13,455,000 in 2009 compared to $15,264,000 in 2008 and $14,661,000 in 2007. The primary reasons for the more significant year-to-year changes in other income components are as follows:

- Trust revenues decreased $437,000 or 16.4% to $2,229,000 in 2009 from $2,666,000 in 2008, compared to $2,607,000 in 2007. The decrease from 2008 to 2009 in trust revenues was due to a decrease in revenues from employee benefits accounts and the overall decline in equity prices for most of 2009. Trust assets were $459.1 million at December 31, 2009 compared to $413.8 million and $453.9 million at December 31, 2008 and 2007, respectively.

- Revenue from brokerage annuity sales decreased $150,000 or 26.1% to $424,000 in 2009 from $574,000 in 2008, compared to $528,000 in 2007. The decrease from 2008 to 2009 was due a reduction in commissions received from the sale of annuities.

- Insurance commissions decreased $66,000 or 3.3% to $1,912,000 in 2009 from $1,978,000 in 2008, compared to $1,950,000 in 2007. The decrease from 2008 to 2009 was due to a decrease in commissions received on sales of business property and casualty insurance.

- Fees from service charges decreased $619,000 or 11.1% to $4,952,000 in 2009 from $5,571,000 in 2008, compared to $5,621,000 in 2007. This decrease from 2008 to 2009 was primarily the result of a decrease in the number of overdrafts.

- Net securities gains in 2009 were $637,000 compared to net securities gains of $293,000 in 2008, and $256,000 in 2007. Several securities in the investment portfolio were sold to improve the overall portfolio mix and the margin in 2009, 2008 and 2007.

- During 2009, the Company recorded other-than-temporary impairment charges amounting to $1,812,000 for its investments in four trust preferred securities. See Note 4 - “Investment Securities” for a more detailed description of these charges.

- During the first quarter of 2009, the Company had a $1 million gain on the sale of First Mid Bank’s merchant card servicing portfolio. There were no gains on sales of other assets during 2008 or 2007.

- Mortgage banking income increased $227,000 or 51.9% to $664,000 in 2009 from $437,000 in 2008, compared to $482,000 in 2007. This increase from 2008 to 2009 was due to a increase in the volume of fixed rate loans originated and sold by First Mid Bank. Loans sold balances are as follows:

  - $63 million (representing 552 loans) in 2009
  - $46 million (representing 381 loans) in 2008
  - $48 million (representing 421 loans) in 2007

- Other income decreased $296,000 or 7.9% to $3,449,000 in 2009 from $3,745,000 in 2008, compared to $3,217,000 in 2007. This decrease from 2008 to 2009 was primarily due to proceeds from a life insurance policy received in 2008 that was not received in 2009 and decreased merchant card income due to sale of First Mid Bank’s merchant card servicing portfolio during the first quarter of 2009.

Other Expense

The major categories of other expense include salaries and employee benefits, occupancy and equipment expenses and other operating expenses associated with day-to-day operations. The following table sets forth the major components of other expense for the last three years (in thousands):

				$ Change From Prior Year	
	2009	2008	2007	2009	2008
Salaries and benefits	$16,830	$16,876	$16,408	$(46)	$468
Occupancy and equipment	4,989	4,959	4,831	30	128
Amortization of other intangibles	730	766	821	(36)	(55)
Other real estate owned, net	470	234	82	236	152
FDIC insurance assessment expense	1,943	158	91	1,785	67

Stationery and supplies	563	557	547	6	10
Legal and professional fees	2,021	1,820	1,641	201	179
Marketing and promotion	963	847	911	116	(64)
Other	4,703	5,243	4,723	(540)	520
Total other expense	$33,212	$31,460	$30,055	$1,752	$1,405

Total non-interest expense increased to $33,212,000 in 2009 from $31,460,000 in 2008 and $30,055,000 in 2007. The primary reasons for the more significant year-to-year changes in other expense components are as follows:

- Salaries and employee benefits, the largest component of other expense, decreased $46,000 or .3% to $16,830,000 in 2009 from $16,876,000 in 2008, compared to $16,408,000 in 2007. The decrease in 2009 was as primarily due to a reduction in incentive compensation expense as a result of not achieving desired objectives in 2009 compared to during the year 2008. There were 347 full-time equivalent employees at December 31, 2009 compared to 343 at December 31, 2008 and 346 at December 31, 2007.

- Occupancy and equipment expense increased $30,000 or .6% to $4,989,000 in 2009 from $4,959,000 in 2008, compared to $4,831,000 in 2007. The increase in 2009 was primarily due to the addition of two new leased facilities in Decatur and Champaign added during the fourth quarter of 2009. In 2008, this increase primarily due to increases in rent and building expenses for new brokerage offices and expenses for computer software and software maintenance during the first quarter of 2009.

- Amortization of other intangibles expense decreased $36,000 in 2009 due to complete amortization of one core deposit intangible in the second quarter of 2009.

- Net other real estate owned expense increased $236,000 or 100.9% to $470,000 in 2009 from $234,000 in 2008, compared to $82,000 in 2007. The increase in 2009 is primarily due to increased losses on sales of these properties due to further economic deterioration during the year.

- FDIC insurance expense increased $1,785,000 or 1129.7% to $1,943,000 in 2009 from $158,000 in 2008, compared to $91,000 in 2007. The increase in 2009 was due to increases in FDIC assessment rates during 2009 as well as a special assessment during the second quarter of 2009 which amounted to approximately $522,000.

- Other operating expenses decreased $540,000 or 10.3% to 4,703,000 in 2009 from $5,243,000 in 2008, compared to $4,723,000 in 2007. In 2008, this increase was due to the write down of property in DeLand, Illinois to its appraised value during the second quarter of 2008 and decreases in various other expenses during 2009.

- On a net basis, all other categories of operating expenses increased $323,000 or 10.0% to $3,547,000 in 2009 from $3,224,000 in 2008, compared to $3,099,000 in 2007. In 2009, the increase was primarily due to increases in legal and other professional expenses associated with loan collections and marketing and promotion expenses.

Income Taxes

Income tax expense amounted to $4,007,000 in 2009 compared to $5,443,000 in 2008 and $5,087,000 in 2007. Effective tax rates were 32.8%, 34.1% and 33.4%, respectively, for 2009, 2008 and 2007.

The Company adopted the provisions of FASB Interpretation No. 48 (FIN 48), "Accounting for Uncertainty in Income Taxes," which was codified within ASC 740, on January 1, 2007. The implementation of FIN 48 did not impact the Company's financial statements. The Company files U.S. federal and state of Illinois income tax returns. The Company is no longer subject to U.S. federal or state income tax examinations by tax authorities for years before 2006.

Analysis of Balance Sheets

Loans

The loan portfolio (net of unearned discount) is the largest category of the Company's earning assets. The following table summarizes the composition of the loan portfolio for the last five years (in thousands):

	2009	% Outstanding Loans		2008	2007	2006	2005
Construction and land development	$28,041	4.0	%	$40,362	$55,581	$47,309	$36,712
Farm loans	62,330	8.9	%	65,647	61,898	59,420	51,023
1-4 Family residential properties	180,415	25.7	%	200,204	193,065	189,068	156,762
Multifamily residential properties	19,467	2.8	%	23,833	30,795	29,847	33,005
Commercial real estate	226,400	32.3	%	217,307	203,282	205,932	187,452

Loans secured by real estate	516,653	73.7	%	547,353	544,621	531,576	464,954
Agricultural loans	54,144	7.7	%	54,098	51,793	50,526	41,048
Commercial and industrial loans	105,351	15.0	%	109,324	116,176	105,799	104,981
Consumer loans	20,815	3.0	%	25,806	29,903	29,765	23,562
All other loans	3,787	.6	%	5,357	5,668	5,902	3,588
Total loans	$700,750	100.0	%	$741,938	$748,161	$723,568	$638,133

Loan balances decreased by $41.2 million or 5.6% from December 31, 2008 to December 31, 2009 due to a decrease in most loan type balances. Balances of loans sold into the secondary market were $63 million in 2009, compared to $46 million in 2008. The balance of real estate loans held for sale, included in the balances shown above, amounted to $149,000 and $537,000 as of December 31, 2009 and 2008, respectively.

Commercial and commercial real estate loans generally involve higher credit risks than residential real estate and consumer loans. Because payments on loans secured by commercial real estate or equipment are often dependent upon the successful operation and management of the underlying assets, repayment of such loans may be influenced to a great extent by conditions in the market or the economy. The Company does not have any sub-prime mortgages or credit card loans outstanding which are also generally considered to be higher credit risk.

The following table summarizes the loan portfolio geographically by branch region as of December 31, 2009 and 2008 (dollars in thousands):

	2009		2008	
	Principal balance	% Outstanding loans	Principal balance	% Outstanding loans
Mattoon region	$144,521	20.6 %	$152,897	20.6 %
Charleston region	58,890	8.4 %	59,227	8.0 %
Sullivan region	68,802	9.8 %	76,181	10.3 %
Effingham region	89,141	12.7 %	93,940	12.7 %
Decatur region	212,908	30.4 %	222,895	30.0 %
Highland region	126,488	18.1 %	136,798	18.4 %
Total all regions	$700,750	100.0 %	$741,938	100.0 %

Loans are geographically dispersed among these regions located in central and southwestern Illinois. While these regions have experienced some economic stress during 2009, the Company does not consider these locations high risk areas since these regions have not experienced the significant declines in real estate values seen in other areas in the United States.

The Company does not have a concentration, as defined by the regulatory agencies, in construction and land development loans or commercial real estate loans as a percentage of total risk-based capital for the periods shown above. At December 31, 2009, the Company did have industry loan concentrations in excess of 25% of total risk-based capital in the following industries as of December 31, 2009 and 2008 (dollars in thousands):

	2009		2008	
	Principal balance	% Outstanding loans	Principal balance	% Outstanding Loans
Other grain farming	$102,515	14.63 %	$97,082	13.08 %
Lessors of non-residential buildings	72,016	10.28 %	68,987	9.30 %
Lessors of residential buildings & dwellings	44,232	6.31 %	48,648	6.56 %
Hotels and motels	50,788	7.25 %	45,518	6.14 %

The Company had no further industry loan concentrations in excess of 25% of total risk-based capital.

The following table presents the balance of loans outstanding as of December 31, 2009, by contractual maturities (in thousands):

	Maturity (1)			
	One year or less(2)	Over 1 through 5 years	Over 5 years	Total
Construction and land development	$25,986	$1,962	$93	$28,041
Farm loans	10,727	41,235	10,368	62,330
1-4 Family residential properties	26,374	101,033	53,008	180,415
Multifamily residential properties	2,122	10,250	7,095	19,467

Commercial real estate	24,758	164,181	37,461	226,400
Loans secured by real estate	89,967	318,661	108,025	516,653
Agricultural loans	39,264	14,401	479	54,144
Commercial and industrial loans	62,267	38,350	4,734	105,351
Consumer loans	4,584	15,402	829	20,815
All other loans	598	1,491	1,698	3,787
Total loans	$196,680	$388,305	$115,765	$700,750

(1) Based upon remaining contractual maturity.

(2) Includes demand loans, past due loans and overdrafts.

As of December 31, 2009, loans with maturities over one year consisted of $477 million in fixed rate loans and $27 million in variable rate loans. The loan maturities noted above are based on the contractual provisions of the individual loans. The Company has no general policy regarding renewals and borrower requests, which are handled on a case-by-case basis.

Nonperforming Loans and Repossessed Assets

Nonperforming loans include: (a) loans accounted for on a nonaccrual basis; (b) accruing loans contractually past due ninety days or more as to interest or principal payments; and (c) loans not included in (a) and (b) above which are defined as “restructured loans”. Repossessed assets include primarily repossessed real estate and automobiles.

The Company’s policy is to discontinue the accrual of interest income on any loan for which principal or interest is ninety days past due. The accrual of interest is discontinued earlier when, in the opinion of management, there is reasonable doubt as to the timely collection of interest or principal. Once interest accruals are discontinued, accrued but uncollected interest is charged to current year income. Subsequent receipts on non-accrual loans are recorded as a reduction of principal, and interest income is recorded only after principal recovery is reasonably assured. Nonaccrual loans are returned to accrual status when, in the opinion of management, the financial position of the borrower indicates there is no longer any reasonable doubt as to the timely collection of interest or principal.

Restructured loans are loans on which, due to deterioration in the borrower’s financial condition, the original terms have been modified in favor of the borrower or either principal or interest has been forgiven.

Repossessed assets represent property acquired as the result of borrower defaults on loans. These assets are recorded at estimated fair value, less estimated selling costs, at the time of foreclosure or repossession. Write-downs occurring at foreclosure are charged against the allowance for loan losses. On an ongoing basis, properties are appraised as required by market indications and applicable regulations. Write-downs for subsequent declines in value are recorded in non-interest expense in other real estate owned along with other expenses related to maintaining the properties.

The following table presents information concerning the aggregate amount of nonperforming loans and repossessed assets (in thousands):

	December 31,				
	2009	2008	2007	2006	2005
Nonaccrual loans	$12,720	$7,285	$7,460	$3,639	$3,458
Restructured loans which are performing in accordance with revised terms	-	-	21	29	-
Total nonperforming loans	12,720	7,285	7,481	3,668	3,458
Repossessed assets	2,896	2,400	524	1,396	420
Total nonperforming loans and repossessed assets	$15,616	$9,685	$8,005	$5,064	$3,878
Nonperforming loans to loans, before allowance for loan losses	1.82 %	.98 %	1.00 %	.51 %	.54 %
Nonperforming loans and repossessed assets to loans, before allowance for loan losses	2.23 %	1.31 %	1.07 %	.70 %	.61 %

The $5,435,000 increase in nonaccrual loans during 2009 resulted from the net of $8,297,000 of loans put on nonaccrual status, offset by $1,620,000 of loans transferred to other real estate owned, $323,000 of loans charged off and $919,000 of loans becoming current or paid-off. The primary increase in nonaccrual loans was in commercial real estate which increased $4,917,000 during 2009 due to insufficient cash flow of various borrowers. The following table summarizes the composition of nonaccrual loans (in thousands):

	December 31, 2009			December 31, 2008		
	Balance	% of Total		Balance	% of Total	
Construction and land development	$2,064	16.2	%	$2,889	39.7	%
Farm loans	1,355	10.6	%	1,355	18.6	%
1-4 Family residential properties	1,968	15.5	%	1,105	15.2	%
Multifamily residential properties	487	3.8	%	220	3.0	%
Commercial real estate	6,063	47.7	%	1,146	15.7	%
Loans secured by real estate	11,937	93.8	%	6,715	92.2	%
Agricultural loans	-	-		177	2.4	%
Commercial and industrial loans	783	6.2	%	345	4.7	%
Consumer loans	-	-		48	0.7	%
Total loans	$12,720	100.0	%	$7,285	100.0	%

Interest income that would have been reported if nonaccrual and restructured loans had been performing totaled $672,000, $274,000 and $426,000 for the years ended December 31, 2009, 2008 and 2007, respectively.

The $496,000 increase in repossessed assets during 2009 resulted from the net of $2,930,000 of additional assets repossessed, $165,000 of further write-downs of repossessed assets to current market value and $2,269,000 of repossessed assets sold. The following table summarizes the composition of repossessed assets (in thousands):

	December 31, 2009			December 31, 2008		
	Balance	% of Total		Balance	% of Total	
Construction and land development	$1,252	16.2	%	$1,873	39.7	%
1-4 Family residential properties	945	15.5	%	351	15.2	%
Commercial real estate	665	47.7	%	164	15.7	%
Total real estate	2,862	93.8	%	2,388	92.2	%
Other collateral	34	-		12	0.7	%
Total repossessed collateral	$2,896	100.0	%	$2,400	100.0	%

Repossessed assets sold during 2009 resulted in a net loss of $225,000, of which $221,000 was related to real estate asset sales and $4,000 was related to other repossessed asset sales. Repossessed assets sold during 2008 resulted in a net loss of $69,000, of which $55,000 was related to real estate asset sales and $14,000 was related to other repossessed asset sales. Repossessed assets sold during 2007 resulted in a net gain of $37,000, of which $29,000 was related to real estate asset sales and $8,000 was related to other repossessed asset sales.

Loan Quality and Allowance for Loan Losses

The allowance for loan losses represents management's estimate of the reserve necessary to adequately account for the estimate of potential losses inherent in the current portfolio. The provision for loan losses is the charge against current earnings that is determined by management as the amount needed to maintain an adequate allowance for loan losses. In determining the adequacy of the allowance for loan losses, and therefore the provision to be charged to current earnings, management relies predominantly on a disciplined credit review and approval process that extends to the full range of the Company's credit exposure. The review process is directed by overall lending policy and is intended to identify, at the earliest possible stage, borrowers who might be facing financial difficulty. Once identified, the magnitude of exposure to individual borrowers is quantified in the form of specific allocations of the allowance for loan losses. Management considers collateral values and guarantees in the determination of such specific allocations. Additional factors considered by management in evaluating the overall adequacy of the allowance include historical net loan losses, the level and composition of nonaccrual, past due and renegotiated loans, trends in volumes and terms of loans, effects of changes in risk selection and underwriting standards or lending practices, lending staff changes, concentrations of credit, industry conditions and the current economic conditions in the region where the Company operates.

Given the current state of the economy, management did assess the impact of the recession on each category of loans and adjusted historical loss factors for more recent economic trends. Management utilizes a five-year loss history as one component in assessing the probability of inherent future losses. Given the decline in economic conditions, management also increased its allocation to various loan categories for economic factors during 2008 and 2009. Some of the economic factors include the potential for reduced cash flow for commercial operating loans from reduction in sales or increased operating costs, decreased occupancy rates for commercial buildings, reduced levels of home sales for commercial land developments, the decline in and uncertainty regarding grain prices and increased operating costs for farmers, and increased levels of unemployment and bankruptcy impacting consumer's ability to pay. Each of these economic uncertainties was taken into consideration in developing the level of the reserve. Management considers the allowance for loan losses a critical accounting policy.

Management recognizes there are risk factors that are inherent in the Company's loan portfolio. All financial institutions face risk factors in their loan portfolios because risk exposure is a function of the business. The

Company's operations (and therefore its loans) are concentrated in east central Illinois, an area where agriculture is the dominant industry. Accordingly, lending and other business relationships with agriculture-based businesses are critical to the Company's success. At December 31, 2009, the Company's loan portfolio included $116.5 million of loans to borrowers whose businesses are directly related to agriculture. Of this amount, $102.5 million was concentrated in other grain farming. Total loans to borrowers whose businesses are directly related to agriculture decreased $3.2 million from $119.7 million at December 31, 2008 while loans concentrated in other grain farming increased $6 million from $113.7 million at December 31, 2008. While the Company adheres to sound underwriting practices, including collateralization of loans, any extended period of low commodity prices, significantly reduced yields on crops and/or reduced levels of government assistance to the agricultural industry could result in an increase in the level of problem agriculture loans and potentially result in loan losses within the agricultural portfolio.

In addition, the Company has $50.8 million of loans to motels and hotels. The performance of these loans is dependent on borrower specific issues as well as the general level of business and personal travel within the region. While the Company adheres to sound underwriting standards, a prolonged period of reduced business or personal travel could result in an increase in nonperforming loans to this business segment and potentially in loan losses. The Company also has $72.0 million of loans to lessors of non-residential buildings and $44.2 million of loans to lessors of residential buildings and dwellings.

Analysis of the allowance for loan losses for the past five years and of changes in the allowance for these periods is summarized as follows (dollars in thousands):

	2009	2008	2007	2006	2005
Average loans outstanding, net of unearned income	$701,521	$740,083	$728,790	$691,726	$610,781
Allowance-beginning of year	$7,587	$6,118	$5,876	$4,648	$4,621
Balance added through acquisitions	-	-	-	1,405	-
Charge-offs:					
Real estate-mortgage	1,240	1,640	368	231	122
Commercial, financial and agricultural	287	479	180	595	757
Installment	176	119	100	142	278
Other	176	184	215	188	130
Total charge-offs	1,879	2,422	863	1,156	1,287
Recoveries:					
Real estate-mortgage	6	75	9	8	63
Commercial, financial and agricultural	27	98	48	30	75
Installment	31	38	33	49	42
Other	96	121	153	132	43
Total recoveries	160	332	243	219	223
Net charge-offs	1,719	2,090	620	937	1,064
Provision for loan losses	3,594	3,559	862	760	1,091
Allowance-end of year	$9,462	$7,587	$6,118	$5,876	$4,648
Ratio of net charge-offs to average loans	.25%	.28%	.09%	.14%	.17%
Ratio of allowance for loan losses to loans outstanding (at end of year)	1.35%	1.02%	.82%	.81%	.73%
Ratio of allowance for loan losses to nonperforming loans	74.4%	104.1%	81.8%	160.2%	134.4%

The ratio of the allowance for loan losses to non-performing loans is 74.4% as of December 31, 2009 compared to 104.1% as of December 31, 2008. While the balance of non-performing loans reflects the total loan balance, the allowance for loan losses reflects only the portion of the loan balance that is an estimated potential loss. Therefore the increase in non-performing loans, which was greater than the increase in the allowance for loan losses required to account for probable losses, led to the decline of this ratio. The increase in 2009 occurred as a result of loans that became nonperforming during the year due to continued deterioration in economic conditions including increased unemployment, reduction in cash flow from increased vacancies in commercial properties and declines in property values. The current economic environment and the increase in estimated probable losses in the loan portfolio resulted in the increased allowance balance.

The Company minimizes credit risk by adhering to sound underwriting and credit review policies. These policies are reviewed at least annually, and the Board of Directors approves all changes. Senior management is actively involved in business development efforts and the maintenance and monitoring of credit underwriting and approval. The loan review system and controls are designed to identify, monitor and address asset quality problems in an accurate and timely manner. At least quarterly, the Board of Directors reviews the status of problem loans. In addition to internal policies and controls, regulatory authorities periodically review asset quality and the overall adequacy of the allowance for loan losses.

During 2009, the Company had net charge-offs of $1,719,000 compared to $2,090,000 in 2008 and $620,000 in 2007. During 2009, the Company's significant charge-offs included $173,000 on commercial loans of two borrowers,

$107,000 of real estate mortgage loans of one borrower and $902,000 of commercial real estate mortgage loans of four borrowers. During 2008, the Company's significant charge-offs included $204,000 on commercial loans of one borrower, $200,000 of real estate mortgage loans of one borrower and $1,181,000 of commercial real estate mortgage loans of three borrowers. During 2007, the Company's significant charge-offs included $165,000 on commercial loans of three borrowers, $66,000 of real estate mortgage loans of one borrower and $250,000 of commercial real estate mortgage loans of two borrowers.

At December 31, 2009, the allowance for loan losses amounted to $9,462,000, or 1.35% of total loans, and 74.4% of nonperforming loans. At December 31, 2008, the allowance for loan losses amounted to $7,587,000, or 1.02% of total loans, and 104.1% of nonperforming loans. Given the increase in non-performing loans and the current state of the economy, management's estimate of probable losses in the loan portfolio has increased and resulted in an increase in the ratio of the allowance for loan losses to total loans.

The allowance is allocated to the individual loan categories by a specific allocation for all classified loans plus a percentage of loans not classified based on historical losses and other factors. The allowance for loan losses, in management's judgment, is allocated as follows to cover probable loan losses (dollars in thousands):

	December 31, 2009		December 31, 2008		December 31, 2007	
	Allowance for loan losses	% of loans to total loans	Allowance for loan losses	% of loans to total loans	Allowance for loan losses	% of loans to total loans
Residential real estate	$488	28.5 %	$510	30.2 %	$214	29.9 %
Commercial / Commercial real estate	7,429	51.3 %	5,345	49.5 %	3,828	50.1 %
Agricultural / Agricultural real estate	315	16.6 %	223	16.1 %	531	15.2 %
Consumer	312	3.0 %	358	3.5 %	404	4.0 %
Other	97	.5 %	78	.7 %	22	.8 %
Total allocated	8,641		6,514		4,999	
Unallocated	821	N/A	1,073	N/A	1,119	N/A
Allowance at end of year	$9,462	100.0 %	$7,587	100.0 %	$6,118	100.0 %

	December 31, 2006		December 31, 2005	
	Allowance for loan losses	% of loans to total loans	Allowance for loan losses	% of loans to total loans
Residential real estate	$215	30.3 %	$134	29.7 %
Commercial / Commercial real estate	3,395	49.6 %	2,519	51.6 %
Agricultural / Agricultural real estate	607	15.2 %	730	14.4 %
Consumer	382	4.1 %	319	3.7 %
Other	26	.8 %	18	.6 %
Total allocated	4,625		3,720	
Unallocated	1,251	N/A	928	N/A
Allowance at end of year	$5,876	100.0 %	$4,648	100.0 %

The allowance allocated to commercial and commercial real estate loans increased $2.1 million from 2008 during 2009 and $1.5 million from 2007 during 2008. This resulted from an increase in the balance of impaired and classified loans and an increase in the allocation percent for this loan category. These increases were due to the ongoing poor economy which has led to increased vacancies in commercial real estate and deficient cash flows from business operations.

The unallocated allowance represents an estimate of the probable, inherent, but yet undetected, losses in the loan portfolio. It is based on factors that cannot necessarily be associated with a specific credit or loan category and represents management's estimate to ensure that the overall allowance of loan losses appropriately reflects a margin for the imprecision necessarily inherent in the estimates of expected credit losses.   Fluctuations in the unallocated portion of the allowance result from qualitative factors such as economic conditions, expansionary activities, and portfolio composition that influence the level of risk in the portfolio but are not specifically quantified.

Securities

The Company's overall investment objectives are to insulate the investment portfolio from undue credit risk, maintain adequate liquidity, insulate capital against changes in market value and control excessive changes in earnings while optimizing investment performance. The types and maturities of securities purchased are primarily based on the Company's current and projected liquidity and interest rate sensitivity positions.

The following table sets forth the year-end amortized cost of the Company's securities for the last three years (dollars in thousands):

	December 31,								
	2009			2008			2007		
		Weighted Average			Weighted Average			Weighted Average	
	Amount	Yield		Amount	Yield		Amount	Yield	
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$89,640	3.27	%	$72,074	4.72	%	$106,175	4.82	%
Obligations of states and political subdivisions	23,530	4.13	%	22,042	4.10	%	17,820	4.15	%
Mortgage-backed securities	111,301	4.36	%	61,102	5.66	%	49,798	5.33	%
Trust preferred securities	7,758	4.22	%	9,328	6.23	%	9,587	6.30	%
Other securities	6,166	4.56	%	6,210	4.56	%	35	-	%
Total securities	$238,395	3.93	%	$170,756	5.05	%	$183,415	4.96	%

At December 31, 2009, the Company's investment portfolio showed an increase of $67.6 million from December 31, 2008 primarily due to the purchase of several U.S. Treasury securities and obligations of U.S. government corporations and agencies securities as well as several mortgage-backed securities. When purchasing investment securities, the Company considers its overall liquidity and interest rate risk profile, as well as the adequacy of expected returns relative to the risks assumed.

The table below presents the credit ratings as of December 31, 2009, for all investment securities:

	Amortized Cost	Estimated Fair Value	Average Credit Rating of Fair Value at December 31, 2009 (1)					
			AAA	AA +/-	A +/-	BBB +/-	< BBB -	Not rated
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$ 89,640	$ 90,974	$90,974	$-	$-	$-	$-	$-
Obligations of state and political subdivisions	23,530	24,185	1,686	13,362	2,393	2,850	-	3,894

Mortgage-backed securities (2)	111,301	114,519	-	-	-	-	-	114,519
Trust preferred securities	7,758	3,155	-	-	-	-	3,155	-
Other securities	6,166	6,333	-	-	3,216	3,102	-	15
Total investments	$ 238,395	$ 239,166	$ 92,660	$ 13,362	$ 5,609	$ 5,952	$ 3,155	$ 118,428

(1) Credit ratings reflect the lowest current rating assigned by a nationally recognized credit rating agency.

(2) Mortgage-backed securities include mortgage-backed securities (MBS) and collateralized mortgage obligation (CMO) issues from the following government sponsored enterprises: FHLMC, FNMA, GNMA and FHLB. While MBS and CMOs are no longer explicitly rated by credit rating agencies, the industry recognizes that they are backed by agencies which have an implied government guarantee.

The trust preferred securities are four trust preferred pooled securities issued by FTN Financial Securities Corp. ("FTN"). The following table contains information regarding these securities as of December 31, 2009:

Deal name	PreTSL I	PreTSL II	PreTSL VI	PreTSL XXVIII
Class	Mezzanine	Mezzanine	Mezzanine	C-1
Book value	$1,229,829	$1,547,376	$280,837	$4,699,801
Fair value	$948,496	$1,087,828	$188,287	$930,223
Unrealized gains/(losses)	$(281,333)	$(459,548)	$(92,550)	$(3,769,578)
Other-than-temporary impairment recorded in earnings	$220,000	$1,531,531	$44,146	$16,303
Lowest credit rating assigned	Caa1	Ca	Caa1	Ca
Number of performing banks	26	24	3	34
Number of issuers in default	3	4	-	4
Number of issuers in deferral	3	7	2	7
Defaults & deferrals as a % of performing collateral	24.9%	32.7%	68.7%	16.1%
Discount margin	9.740%	9.685%	1.800%	1.289%
Recovery assumption (1)	15%	15%	15%	15%
Prepayment assumption	0%	0%	0%	0%

(1) With 2 year lag

Other-than-temporary Impairment of Securities

Declines in the fair value, or unrealized losses, of all available for sale investment securities, are reviewed to determine whether the losses are either a temporary impairment or an other-than-temporary impairment (OTTI). Temporary adjustments are recorded when the fair value of a security fluctuates from its historical cost. Temporary adjustments are recorded in accumulated other comprehensive income, and impact the Company's equity position. Temporary adjustments do not impact net income. A recovery of available for sale security prices also is recorded as an adjustment to other comprehensive income for securities that are temporarily impaired, and results in a positive impact to the Company's equity position.

OTTI is recorded when the fair value of an available for sale security is less than historical cost, and it is probable that all contractual cash flows will not be collected. Investment securities are evaluated for OTTI on at least a quarterly basis. In conducting this assessment, the Company evaluates a number of factors including, but not limited to:

- how much fair value has declined below amortized cost;
- how long the decline in fair value has existed;
- the financial condition of the issuers;
- contractual or estimated cash flows of the security;
- underlying supporting collateral;
- past events, current conditions and forecasts;
- significant rating agency changes on the issuer; and
- the Company's intent and ability to hold the security for a period of time sufficient to allow for any anticipated recovery in fair value.

If the Company intends to sell the security or if it is more likely than not the Company will be required to sell the security before recovery of its amortized cost basis, the entire amount of OTTI is recorded to noninterest income, and therefore, results in a negative impact to net income. Because the available for sale securities portfolio is recorded at fair value, the conclusion as to whether an investment decline is other-than-temporarily impaired, does not significantly impact the Company's equity position, as the amount of the temporary adjustment has already been reflected in accumulated other comprehensive income/loss.

If the Company does not intend to sell the security and it is not more-likely-than-not it will be required to sell the security before recovery of its amortized cost basis only the amount related to credit loss is recognized in earnings. In determining the portion of OTTI that is related to credit loss, the Company compares the present value of cash flows expected to be collected from the security with the amortized cost basis of the security. The remaining portion of OTTI, related to other factors, is recognized in other comprehensive earnings, net of applicable taxes. The Company recognized $1.8 million of OTTI in earnings during 2009. There was no OTTI recorded during 2008 or 2007.

The term "other-than-temporary" is not intended to indicate that the decline is permanent, but indicates that the prospects for a near-term recovery of value are not necessarily favorable, or that there is a general lack of evidence to support a realizable value equal to or greater than the carrying value of the investment. See Note 4- "Investment Securities" to the Financial Statements for a discussion of the Company's evaluation and subsequent charges for OTTI.

Deposits

Funding of the Company's earning assets is substantially provided by a combination of consumer, commercial and public fund deposits. The Company continues to focus its strategies and emphasis on retail core deposits, the major component of funding sources. The following table sets forth the average deposits and weighted average rates for 2009, 2008 and 2007 (dollars in thousands):

	2009		2008		2007	
	Average Balance	Weighted Average Rate	Average Balance	Weighted Average Rate	Average Balance	Weighted Average Rate
Demand deposits:						
Non-interest bearing	$119,537	-	$119,764	-	$114,393	-
Interest bearing	332,751	1.26 %	288,057	1.26 %	271,117	1.98 %
Savings	109,305	.92 %	74,236	.92 %	60,654	.58 %
Time deposits	301,987	3.91 %	313,729	3.91 %	325,397	4.54 %
Total average deposits	$863,580	2.08 %	$795,786	2.08 %	$771,561	2.66 %

	December 31,		
(dollars in thousands)	2009	2008	2007
High month-end balances of total deposits	$906,853	$810,756	$784,597
Low month-end balances of total deposits	831,157	777,337	756,222

In 2009, the average balance of deposits increased by $67.8 million from 2008. The increase was primarily attributable to increases in money market and savings account balances. Average non-interest bearing deposits decreased by $.2 million, average money market account balances increased by $35.3 million, and NOW account balances increased by $4.4 million offset by a decline in consumer CD balances. In 2008, the average balance of deposits increased by $24.2 million from 2007. The increase was primarily attributable to increases in savings account balances. Average non-interest bearing deposits increased by $5.4 million, average money market account balances increased by $4.7 million, and NOW account balances increased by $12.2 million offset by a decline in consumer CD balances.

In 2009, the Company's significant deposits included brokered CDs and deposit relationships with various public entities. As of December 31, 2009, the Company had three brokered CDs which totaled $15 million. Five public entities had total balances of $25.3 million in various checking accounts and time deposits as of December 31, 2009. These balances are subject to change depending upon the cash flow needs of the public entity.

The following table sets forth the maturity of time deposits of $100,000 or more (in thousands):

	December 31,		
	2009	2008	2007
3 months or less	$24,951	$24,922	$17,883
Over 3 through 6 months	8,622	18,189	25,339
Over 6 through 12 months	29,852	61,421	47,160
Over 12 months	18,267	24,865	7,670
Total	$81,692	$129,397	$98,052

The balance of time deposits of $100,000 or more decreased $47.7 million from December 31, 2008 to December 31, 2009. The decrease in balances was primarily attributable to a decrease in time deposits. The balance of time deposits of $100,000 or more increased $38.2 million from December 31, 2007 to December 31, 2008. The increase in balances was primarily attributable to an increase in brokered CD balances.

Balances of time deposits of $100,000 or more includes brokered CDs, time deposits maintained for public entities, and consumer time deposits. The balance of brokered CDs was $15 million as of December 31, 2009 and 2008. The Company also maintains time deposits for the State of Illinois with balances of $41,000, $4.4 million and $3 million as of December 31, 2009, 2008 and 2007, respectively. The State of Illinois deposits are subject to bid annually and could increase or decrease in any given year.

Repurchase Agreements and Other Borrowings

Securities sold under agreements to repurchase are short-term obligations of First Mid Bank. First Mid Bank collateralizes these obligations with certain government securities that are direct obligations of the United States or one of its agencies. First Mid Bank offers these retail repurchase agreements as a cash management service to its corporate customers. Other borrowings consist of Federal Home Loan Bank ("FHLB") advances, federal funds purchased, junior subordinated debentures and loans (short-term or long-term debt) that the Company has outstanding.

Information relating to securities sold under agreements to repurchase and other borrowings for the last three years is presented below (dollars in thousands):

	2009	2008	2007
At December 31:			
Securities sold under agreements to repurchase	$80,386	$80,708	$68,300
Federal Home Loan Bank advances:			
Fixed term – due in one year or less	10,000	5,000	15,000
Fixed term – due after one year	22,750	32,750	37,750
Junior subordinated debentures	20,620	20,620	20,620
Debt due after one year	-	13,000	14,500
Total	$133,756	$152,078	$156,170
Average interest rate at year end	2.10 %	3.16 %	3.96 %
Maximum Outstanding at Any Month-end			
Federal funds purchased	$-	$-	$14,100
Securities sold under agreements to repurchase	83,826	80,708	68,300
Federal Home Loan Bank advances:			
Overnight	-	-	7,000
Fixed term – due in one year or less	15,000	5,000	20,000
Fixed term – due after one year	32,750	37,750	37,750
Junior subordinated debentures	20,620	20,620	20,620
Debt due after one year	13,000	16,500	16,500
Averages for the Year			
Federal funds purchased	3	-	3,907
Securities sold under agreements to repurchase	72,589	61,108	54,962
Federal Home Loan Bank advances:			
Overnight	-	-	58
Fixed term – due in one year or less	10,041	5,098	8,905
Fixed term – due after one year	26,134	36,275	25,950
Junior subordinated debentures	20,620	20,620	20,620
Debt due after one year	1,498	15,111	14,345
Total	$130,885	$138,212	$128,747
Average interest rate during the year	2.19 %	3.64 %	5.31 %

FHLB advances represent borrowings by First Mid Bank to economically fund loan demand. The fixed term advances consist of $32.75 million as follows:

- $5 million advance at 4.58% with a 5-year maturity, due March 22, 2010
- $2.5 million advance at 5.46% with a 3-year maturity, due June 12, 2010
- $2.5 million advance at 5.12% with a 3-year maturity, due June 12, 2010, one year lockout, callable quarterly
- $3 million advance at 5.98% with a 10-year maturity, due March 1, 2011

- $5 million advance at 4.82% with a 5-year maturity, due January 19, 2012, two year lockout, callable quarterly
- $5 million advance at 4.69% with a 5-year maturity, due February 23, 2012, two year lockout, callable quarterly
- $4.75 million advance at 1.60% with a 5-year maturity, due December 24, 2012
- $5 million advance at 4.58% with a 10-year maturity, due July 14, 2016, one year lockout, callable quarterly

At December 31, 2009 and 2008, outstanding loan balances included $0 and $13 million, respectively, on a revolving credit agreement with The Northern Trust Company. This loan was renegotiated on April 24, 2009. The revolving credit agreement has a maximum available balance of $20 million with a term of one year from the date of closing. The interest rate (2.3% at December 31, 2009) is floating at 2.25% over the federal funds rate. The loan is unsecured and subject to a borrowing agreement containing requirements for the Company and First Mid Bank to maintain various operating and capital ratios. The Company was in compliance with all of the existing covenants at December 31, 2009 except the Company's return on assets ratio was .74% as of December 31, 2009 which was below the covenant ratio required of .75%. The Company has received a waiver from Northern Trust Company for this covenant as of December 31, 2009. The Company and First Mid Bank were in compliance with the existing covenants at December 31, 2008 and 2007.

On February 27, 2004, the Company completed the issuance and sale of $10 million of floating rate trust preferred securities through Trust I, a statutory business trust and wholly-owned unconsolidated subsidiary of the Company, as part of a pooled offering. The Company established Trust I for the purpose of issuing the trust preferred securities. The $10 million in proceeds from the trust preferred issuance and an additional $310,000 for the Company's investment in common equity of the Trust, a total of $10,310 000, was invested in junior subordinated debentures of the Company. The underlying junior subordinated debentures issued by the Company to Trust I mature in 2034, bear interest at three-month London Interbank Offered Rate ("LIBOR") plus 280 basis points, reset quarterly, and are callable, at the option of the Company, at par on or after April 7, 2009. At December 31, 2009 and 2008 the rate was 3.10% and 6.56%, respectively. The Company used the proceeds of the offering for general corporate purposes.

On April 26, 2006, the Company completed the issuance and sale of $10 million of fixed/floating rate trust preferred securities through Trust II, a statutory business trust and wholly-owned unconsolidated subsidiary of the Company, as part of a pooled offering. The Company established Trust II for the purpose of issuing the trust preferred securities. The $10 million in proceeds from the trust preferred issuance and an additional $310,000 for the Company's investment in common equity of Trust II, a total of $10,310 000, was invested in junior subordinated debentures of the Company. The underlying junior subordinated debentures issued by the Company to Trust II mature in 2036, bear interest at a fixed rate of 6.98% (three-month LIBOR plus 160 basis points) paid quarterly and convert to floating rate (LIBOR plus 160 basis points) after June 15, 2011. The net proceeds to the Company were used for general corporate purposes, including the Company's acquisition of Mansfield.

The trust preferred securities issued by Trust I and Trust II are included as Tier 1 capital of the Company for regulatory capital purposes. On March 1, 2005, the Federal Reserve Board adopted a final rule that allows the continued limited inclusion of trust preferred securities in the calculation of Tier 1 capital for regulatory purposes. The final rule provided a five-year transition period, ending September 30, 2009, for application of the revised quantitative limits. On March 17, 2009, the Federal Reserve Board adopted an additional final rule that delayed the effective date of the new limits on inclusion of trust preferred securities in the calculation of Tier 1 capital until September 30, 2011. The Company does not expect the application of the revised quantitative limits to have a significant impact on its calculation of Tier 1 capital for regulatory purposes or its classification as well-capitalized.

Interest Rate Sensitivity

The Company seeks to maximize its net interest margin while maintaining an acceptable level of interest rate risk. Interest rate risk can be defined as the amount of forecasted net interest income that may be gained or lost due to changes in the interest rate environment, a variable over which management has no control. Interest rate risk, or sensitivity, arises when the maturity or repricing characteristics of assets differ significantly from the maturity or repricing characteristics of liabilities.

The Company monitors its interest rate sensitivity position to maintain a balance between rate-sensitive assets and rate-sensitive liabilities. This balance serves to limit the adverse effects of changes in interest rates. The Company's asset/liability management committee (ALCO) oversees the interest rate sensitivity position and directs the overall allocation of funds.

In the banking industry, a traditional way to measure potential net interest income exposure to changes in interest rates is through a technique known as "static GAP" analysis which measures the cumulative differences between the amounts of assets and liabilities maturing or repricing at various intervals. By comparing the volumes of interest-bearing assets and liabilities that have contractual maturities and repricing points at various times in the future, management can gain insight into the amount of interest rate risk embedded in the balance sheet.

The following table sets forth the Company's interest rate repricing gaps for selected maturity periods at December 31, 2009 (dollars in thousands):

	Rate Sensitive Within							
	1 year	1-2 years	2-3 years	3-4 years	4-5 years	Thereafter	Total	Fair Value
Interest-earning assets:								
Federal funds sold and other interest-bearing deposits	$79,512	$-	$-	$-	$-	$-	$79,512	$79,544
Taxable investment securities	15,319	10,295	11,366	1,070	10,275	166,657	214,982	214,982
Nontaxable investment securities	1,298	658	539	830	822	20,027	24,174	24,184
Loans	341,473	115,288	99,471	113,003	15,685	15,830	700,750	708,409
Total	$437,602	$126,241	$111,376	$114,903	$26,782	$202,514	$1,019,418	$1,027,119
Interest-bearing liabilities:								
Savings and N.O.W. accounts	$64,862	$16,846	$17,507	$24,783	$25,541	$151,882	$301,421	$301,421
Money market accounts	169,908	1,201	1,235	1,602	1,635	8,643	184,224	184,224
Other time deposits	185,553	17,513	9,813	8,704	4,221	235	226,039	227,366
Short-term borrowings/debt	80,386	-	-	-	-	-	80,386	80,389
Long-term borrowings/debt	20,310	3,000	25,060	-	-	5,000	53,370	55,068
Total	$521,019	$38,560	$53,615	$35,089	$31,397	$165,760	$845,440	$848,468
Rate sensitive assets – rate sensitive liabilities	$(83,417)	$87,681	$57,761	$79,814	$(4,615)	$36,754	$173,978	
Cumulative GAP	$(83,417)	$4,264	$62,025	$141,839	$137,224	$173,978		
Cumulative amounts as % of total rate sensitive assets	-8.2%	8.6%	5.7%	7.8%	-0.5%	3.6%		
Cumulative Ratio	-8.2%	0.4%	6.1%	13.9%	13.5%	17.1%		

The static GAP analysis shows that at December 31, 2009, the Company was liability sensitive, on a cumulative basis, through the twelve-month time horizon. This indicates that future increases in interest rates, if any, could have an adverse effect on net interest income. Conversely, future decreases in interest rates could have a positive effect on net interest income. There are several ways the Company measures and manages the exposure to interest rate sensitivity, static GAP analysis being one. The Company's ALCO also uses other financial models to project interest income under various rate scenarios and prepayment/extension assumptions consistent with First Mid Bank's historical experience and with known industry trends. ALCO meets at least monthly to review the Company's exposure to interest rate changes as indicated by the various techniques and to make necessary changes in the composition terms and/or rates of the assets and liabilities. Based on all information available, management does not believe that changes in interest rates which might reasonably be expected to occur in the next twelve months will have a material, adverse effect on the Company's net interest income.

Capital Resources

At December 31, 2009, stockholders' equity increased $28.4 million or 34.4% to $111,221,000 from $82,778,000 as of December 31, 2008. During 2009, the Company sold to certain accredited investors including directors, executive officers, and certain major customers and holders of the Company's common stock, $24,635,000, in the aggregate, of a newly authorized series of its preferred stock designated as Series B 9% Non-Cumulative Perpetual Convertible Preferred Stock. See "Preferred Stock" in Note 1 to consolidated financial statements for more detailed information.

Additionally, during 2009 net income contributed $8,214,000 to equity before the payment of dividends to stockholders. The change in the market value of available-for-sale investment securities increased stockholders' equity by $880,000, net of tax. Additional purchases of treasury stock (160,803 shares at an average cost of $19.42 per share) decreased stockholders' equity by $3,122,000.

Stock Plans

On June 29, 2007, the Company effected a three-for-two stock split in the form of a 50% stock dividend. All share and per share information has been restated to reflect the split.

Deferred Compensation Plan

The Company follows the provisions of the Emerging Issues Task Force Issue No. 97-14, "Accounting for Deferred Compensation Arrangements Where Amounts Earned Are Held in a Rabbi Trust and Invested" ("EITF 97-14"), which was codified into ASC 710, for purposes of the First Mid-Illinois Bancshares, Inc. Deferred Compensation Plan ("DCP"). At December 31, 2009, the Company classified the cost basis of its common stock issued and held in trust in connection with the DCP of approximately $2,894,000 as treasury stock. The Company also classified the cost basis of its related deferred compensation obligation of approximately $2,894,000 as an equity instrument (deferred compensation).

The DCP was effective as of June 1984. The purpose of the DCP is to enable directors, advisory directors, and key employees the opportunity to defer a portion of the fees and cash compensation paid by the Company as a means of maximizing the effectiveness and flexibility of compensation arrangements. The Company invests all participants' deferrals in shares of common stock. Dividends paid on the shares are credited to participants' DCP accounts and invested in additional shares. The Company issued, pursuant to DCP:

- 9,916 common shares during 2009
- 7,600 common shares during 2008
- 10,651 common shares during 2007.

First Retirement and Savings Plan

The First Retirement and Savings Plan ("401(k) plan") was effective beginning in 1985. Employees are eligible to participate in the 401(k) plan after six months of service with the Company. The Company offers common stock as an investment option for participants of the 401(k) plan. The Company issued, pursuant to the 401(k) plan:

- 19,000 common shares during 2009
- 7,161 common shares during 2008
- 3,087 common shares during 2007.

Dividend Reinvestment Plan

The Dividend Reinvestment Plan ("DRIP") was effective as of October 1994. The purpose of the DRIP is to provide participating stockholders with a simple and convenient method of investing cash dividends paid by the Company on its common and preferred shares into newly issued common shares of the Company. All holders of record of the Company's common or preferred stock are eligible to voluntarily participate in the DRIP. The DRIP is administered by Computershare Investor Services, LLC and offers a way to increase one's investment in the Company. Of the $2,329,000 in common stock dividends paid during 2009, $807,000 or 34.7% was reinvested into shares of common stock of the Company through the DRIP. Of the $1,822,000 in preferred stock dividends paid during 2009, $48,000 or 2.6% was reinvested into shares of common stock through the DRIP. Events that resulted in common shares being reinvested in the DRIP:

- During 2009, 42,044 common shares were issued from common stock dividends and 2,617 common shares were issued from preferred stock dividends
- During 2008, 31,684 common shares were issued from common stock dividends
- During 2007, 28,788 common shares were issued from common stock dividends.

Stock Incentive Plan

At the Annual Meeting of Stockholders held May 23, 2007, the stockholders approved the First Mid-Illinois Bancshares, Inc. 2007 Stock Incentive Plan (“SI Plan”). The SI Plan was implemented to succeed the Company’s 1997 Stock Incentive Plan, which had a ten-year term that expired October 21, 2007. The SI Plan is intended to provide a means whereby directors, employees, consultants and advisors of the Company and its Subsidiaries may sustain a sense of proprietorship and personal involvement in the continued development and financial success of the Company and its Subsidiaries, thereby advancing the interests of the Company and its stockholders. Accordingly, directors and selected employees, consultants and advisors may be provided the opportunity to acquire shares of Common Stock of the Company on the terms and conditions established herein in the SI Plan. This SI Plan is more fully described in Note 15- “Stock Option Plan.”

A maximum of 300,000 shares are authorized under the SI Plan. Options to acquire shares are awarded at an exercise price equal to the fair market value of the shares on the date of grant and have a 10-year term. Options granted to employees vest over a four-year period and options granted to directors vest at the time they are issued.

The Company has awarded the following stock options:

- The Company awarded no options during the year ended December 31, 2009
- In December 2008, the Company awarded 27,500 options at an option price of $23.00
- In December 2007, the Company awarded 32,000 options at an option price of $26.10.

Effective January 1, 2006, the Company adopted the fair value recognition provisions of SFAS No. 123R, Accounting for Stock-Based Compensation," which was codified into ASC 718, using the modified prospective application method. Accordingly, after January 1, 2006, the Company began expensing the fair value of stock options granted, modified, repurchased or cancelled. Additionally, compensation cost for a portion of the awards for which requisite services had not yet been rendered that were outstanding as of January 1, 2006 are being recognized as the requisite service is rendered. As a result of this adoption, the Company's income before income taxes and net income for the year ended December 31, 2009 includes stock option compensation cost of $53,000 and $51,000, respectively, which represents $.01 impact on basic and diluted earnings per share for the year. The Company's income before income taxes and net income for the year ended December 31, 2008 includes stock option compensation cost of $58,000 and $57,000, respectively, which represents $.01 impact on basic and diluted earnings per share for the year.

Stock Repurchase Program

Since August 5, 1998, the Board of Directors has approved repurchase programs pursuant to which the Company may repurchase a total of approximately $56.7 million of the Company's common stock. The repurchase programs approved by the Board of Directors are as follows:

- On August 5, 1998, repurchases of up to 3%, or $2 million, of the Company's common stock.
- In March 2000, repurchases up to an additional 5%, or $4.2 million of the Company's common stock.
- In September 2001, repurchases of $3 million of additional shares of the Company's common stock.
- In August 2002, repurchases of $5 million of additional shares of the Company's common stock.
- In September 2003, repurchases of $10 million of additional shares of the Company's common stock.
- On April 27, 2004, repurchases of $5 million of additional shares of the Company's common stock.
- On August 23, 2005, repurchases of $5 million of additional shares of the Company's common stock.
- On August 22, 2006, repurchases of $5 million of additional shares of the Company's common stock.
- On February 27, 2007, repurchases of $5 million of additional shares of the Company's common stock.
- On November 13, 2007, repurchases of $5 million of additional shares of the Company's common stock.
- On December 16, 2008, repurchases of $2.5 million of additional shares of the Company's common stock.
- On May 26, 2009, repurchases of $5 million of additional shares of the Company's common stock.

During 2009, the Company repurchased 160,803 shares (2.6% of common shares) at a total price of $3,122,000. During 2008, the Company repurchased 262,877 shares (4.3% of common shares) at a total price of $6,784,000. As of December 31, 2009, approximately $3,417,000 remains available for purchase under the repurchase programs. Treasury stock is further affected by activity in the DCP.

Capital Ratios

Minimum regulatory requirements for highly-rated banks that do not expect significant growth is 8% for the Total Capital to Risk-Weighted Assets ratio and 3% for the Tier 1 Capital to Average Assets ratio. Other institutions, not considered highly-rated, are required to maintain a ratio of Tier 1 Capital to Risk-Weighted Assets of 4% to 5% depending on their particular circumstances and risk profiles. The Company and First Mid Bank have capital ratios above the minimum regulatory capital requirements and, as of December 31, 2009, the Company and First Mid Bank had capital ratios above the levels required for categorization as well-capitalized under the capital adequacy guidelines established by the bank regulatory agencies.

A tabulation of the Company and First Mid Bank's capital ratios as of December 31, 2009 follows:

	Total Capital to Risk-Weighted Assets	Tier One Capital to Risk-Weighted Assets	Tier One Capital to Average Assets
First Mid-Illinois Bancshares, Inc. (Consolidated)	15.76%	14.57%	10.63%
First Mid-Illinois Bank & Trust, N.A.	14.50%	13.31%	9.67%

Liquidity

Liquidity represents the ability of the Company and its subsidiaries to meet all present and future financial obligations arising in the daily operations of the business. Financial obligations consist of the need for funds to meet extensions of credit, deposit withdrawals and debt servicing. The Company's liquidity management focuses on the ability to obtain funds economically through assets that may be converted into cash at minimal costs or through other sources. The Company's other sources for cash include overnight federal fund lines, FHLB advances, deposits of the State of Illinois, the ability to borrow at the Federal Reserve Bank, and the Company's operating line of credit with The Northern Trust Company. Details for the sources include:

- First Mid Bank has $25 million available in overnight federal fund lines, including $10 million from U.S. Bank, N.A. and $15 million from The Northern Trust Company. Availability of the funds is subject to the First Mid Bank's meeting minimum regulatory capital requirements for total capital to risk-weighted assets and Tier 1 capital to total assets. As of December 31, 2009, First Mid Bank met these regulatory requirements.

- In addition, the Company has a revolving credit agreement in the amount of $20 million with The Northern Trust Company. The Company had an outstanding balance of $0 with $20 million in available funds as of December 31, 2009. This loan was renegotiated on April 24, 2009. The revolving credit agreement has a maximum available balance of $20 million with a term of one year from the date of closing. The interest rate (2.3% at December 31, 2009) is floating at 2.25% over the federal funds rate. The loan is unsecured and subject to a borrowing agreement containing requirements for the Company and First Mid Bank to maintain various operating and capital ratios. The Company was in compliance with all of the existing covenants at December 31, 2009 except the Company's return on assets ratio was .74% as of December 31, 2009 which was below the covenant ratio required of .75%. The Company received a waiver from Northern Trust Company for this covenant as of December 31, 2009.

- First Mid Bank can also borrow from the FHLB as a source of liquidity. Availability of the funds is subject to the pledging of collateral to the FHLB. Collateral that can be pledged includes one-to-four family residential real estate loans and securities. At December 31, 2009, the excess collateral at the FHLB could support approximately $60.4 million of additional advances.

- First Mid Bank is also a member of the Federal Reserve System and can borrow funds provided sufficient collateral is pledged.

- First Mid Bank also receives deposits from the State of Illinois. The receipt of these funds is subject to competitive bid and requires collateral to be pledged at the time of placement.

Management monitors its expected liquidity requirements carefully, focusing primarily on cash flows from:

- lending activities, including loan commitments, letters of credit and mortgage prepayment assumptions;
- deposit activities, including seasonal demand of private and public funds;
- investing activities, including prepayments of mortgage-backed securities and call assumptions on U.S. Treasuries and agencies; and
- operating activities, including scheduled debt repayments and dividends to stockholders.

The following table summarizes significant contractual obligations and other commitments at December 31, 2009 (in thousands):

	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Time deposits	$226,039	$179,548	$29,100	$17,155	$236

Debt	20,620	-	-	-	20,620
Other borrowings	113,137	105,387	7,750	-	-
Operating leases	2,963	531	978	779	675
Supplemental retirement liability	903	50	200	200	453
	$363,662	$285,516	$38,028	$18,134	$21,984

For the year ended December 31, 2009, net cash of $8.3 million and $35.4 million was provided from operating activities and financing activities, respectively and $30.6 million was used in investing activities. In total, cash and cash equivalents increased by $13.1 million since year-end 2008. Generally, during 2009, the increase in cash balances was due to an increase in interest-bearing deposits held by the Company and federal funds sold.

For the year ended December 31, 2008, net cash was provided from operating activities, investing activities and financing activities ($15.2 million, $15.8 million and $24.5 million, respectively). Thus, cash and cash equivalents increased by $55.5 million since year-end 2007. Generally, during 2008, the increase in cash balances was due to an increase in interest-bearing deposits held by the Company and federal funds sold.

For the years ended December 31, 2009 and 2008, the Company also had issued $10 million of floating rate trust preferred securities through each of Trust I and Trust II. See heading "Repurchase Agreements and Other Borrowings" for a more detailed description.

Effects of Inflation

Unlike industrial companies, virtually all of the assets and liabilities of the Company are monetary in nature. As a result, interest rates have a more significant impact on the Company's performance than the effects of general levels of inflation. Interest rates do not necessarily move in the same direction or experience the same magnitude of changes as goods and services, since such prices are affected by inflation. In the current economic environment, liquidity and interest rate adjustments are features of the Company's assets and liabilities that are important to the maintenance of acceptable performance levels. The Company attempts to maintain a balance between monetary assets and monetary liabilities, over time, to offset these potential effects.

Adoption of New Accounting Guidance

In June 2009, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 168, "The FASB Accounting Standards CodificationTM and the Hierarchy of Generally Accepted Accounting Principles—a replacement of FASB Statement No. 162." Effective for financial statements issued for interim and annual periods ending after September 15, 2009, the FASB Accounting Standards CodificationTM ("ASC") is now the source of authoritative U.S. GAAP recognized by the FASB to be applied by nongovernmental entities. Rules and interpretive releases of the Securities and Exchange Commission ("SEC") under the authority of federal securities laws are also sources of authoritative GAAP for SEC registrants. The ASC superseded all then-existing non-SEC accounting and reporting standards. All other non-grandfathered non-SEC accounting literature not included in the ASC became non-authoritative. Following this Statement, the FASB will no longer issue new standards in the form of Statements, FASB Staff Positions ("FSP") or Emerging Issues Task Force Abstracts. Instead, it will issue Accounting Standards Updates. The FASB will not consider Accounting Standards Updates as authoritative in their own right. Accounting Standards Updates will serve only to update the ASC, provide background information about the guidance, and provide the bases for conclusions on the change(s) in the ASC. This SFAS was codified within ASC 105.

In April 2009, the FASB issued FSP FAS 157-4, "Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly," which was codified into ASC 820. This FSP provides additional guidance for estimating fair value in accordance with SFAS No. 157, "Fair Value Measurements," when the volume and level of activity for the asset or liability have significantly decreased. This FSP also includes guidance on identifying circumstances that indicate a transaction is not orderly.

In April 2009, the FASB issued FSP FAS 115-2 and FSP FAS 124-2, "Recognition and Presentation of Other-Than-Temporary Impairments," which were codified into ASC 320. This FSP amends the other-than-temporary-impairment ("OTTI") guidance in U.S. GAAP for debt securities to make the guidance more operational and to improve the presentation and disclosure of OTTI on debt and equity securities in the financial statements. This FSP does not amend existing recognition and measurement guidance related to OTTI of equity securities. FSP FAS 115-2 and 124-2 was effective for interim and annual periods ending after June 15, 2009, with early adoption permitted for periods ending after March 15, 2009 if FSP FAS 157-4 was adopted early as well. The Company elected to adopt FSP FAS 115-2 and 124-2 and FSP FAS 157-4 as of March 31, 2009. See discussion in Note 4 - "Investment Securities" for more detailed information.

In April 2009, the FASB issued FSP FAS 107-1 and APB 28-1, "Interim Disclosures about Fair Value of Financial Instruments," which were codified into ASC 825. This FSP amends SFAS No. 107, "Disclosures about Fair Value of Financial Instruments," to require disclosures about fair value of financial instruments for interim reporting periods of publicly traded companies as well as in annual financial statements. This FSP also amends Accounting Principles Board ("APB") Opinion No. 28, "Interim Financial Reporting," to require those disclosures in summarized financial information at interim reporting periods. FSP FAS 107-1 and APB 28-1 was effective for interim and annual periods ending after June 15, 2009. The implementation of FSP FAS 107-1 and APB-28-1 did not have a material impact on the Company's consolidated financial statements.

In April 2009, the FASB issued FSP FAS 141(R)-1, "Accounting for Assets Acquired and Liabilities Assumed in a Business Combination That Arise from Contingencies" which was codified into ASC 805. This FSP amends and clarifies SFAS No. 141(R), "Business Combinations," to address application issues raised by preparers, auditors, and members of the legal profession on initial recognition and measurement, subsequent measurement and accounting, and disclosure of assets and liabilities arising from contingencies in a business combination. This FSP was effective for assets or liabilities arising from contingencies in business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. There has been no impact during 2009 from adoption of FSP FAS 141(R)-1 on January 1, 2009.

In June 2009, the FASB issued SFAS No. 166, "Accounting for Transfers of Financial Assets—an amendment of FASB Statement No. 140" which was codified into ASC 860. SFAS No. 166 seeks to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets; the effects of a transfer on its financial position, financial performance, and cash flows; and a transferor's continuing involvement, if any, in transferred financial assets. SFAS No. 166 addresses (1) practices that have developed since the issuance of SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities," that are not consistent with the original intent and key requirements of that Statement and (2) concerns of financial statement users that many of the financial assets (and related obligations) that have been derecognized should continue to be reported in the financial statements of transferors. This Statement must be applied as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafter. Earlier application is prohibited. This Statement must be applied to transfers occurring on or after the effective date. The impact of adoption is not expected to be material.

In June 2009, the FASB issued SFAS No. 167, "Amendments to FASB Interpretation No. 46(R)" which was codified into ASC 810. SFAS No. 167 seeks to improve financial reporting by enterprises involved with variable interest entities by addressing (1) the effects on certain provisions of FASB Interpretation No. 46 (revised December 2003), "Consolidation of Variable Interest Entities," as a result of the elimination of the qualifying special-purpose entity concept in SFAS No. 166, and (2) constituent concerns about the application of certain key provisions of Interpretation 46(R), including those in which the accounting and disclosures under the Interpretation do not always provide timely and useful information about an enterprise's involvement in a variable interest entity. This Statement shall be effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period, and for interim and annual reporting periods thereafter. Earlier application is prohibited. The impact of adoption is not expected to be material.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company's market risk arises primarily from interest rate risk inherent in its lending, investing and deposit taking activities, which are restricted to First Mid Bank. The Company does not currently use derivatives to manage market or interest rate risks. For a discussion of how management of the Company addresses and evaluates interest rate risk see also "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations – Interest Rate Sensitivity."

Based on the financial analysis performed as of December 31, 2009, which takes into account how the specific interest rate scenario would be expected to impact each interest-earning asset and each interest-bearing liability, the Company estimates that changes in the prime interest rate would impact First Mid Bank's performance as follows:

	Increase (Decrease) In		
December 31, 2009	Net Interest Income	Net Interest Income	Return On Average Equity
Prime rate is 3.25%	$(000)	(%)	2009=8.47%
Prime rate increase of:			
200 basis points to 5.25%	$(1,406)	(5.5)%	(1.13)%
100 basis points to 4.25%	(764)	(3.0)%	(.61)%
Prime rate decrease of:			
200 basis points to 2.25%	(1,191)	(4.6)%	(.96)%
100 basis points to 1.25%	(242)	(.9)%	(.19)%

The following table shows the same analysis performed as of December 31, 2008:

	Increase (Decrease) In		
December 31, 2008	Net Interest Income	Net Interest Income	Return On Average Equity
Prime rate is 3.25%	$(000)	(%)	2008=10.97%
Prime rate increase of:			
200 basis points to 5.25%	$(446)	(1.8)%	(.37)%
100 basis points to 4.25%	(492)	(2.0)%	(.41)%
Prime rate decrease of:			
200 basis points to 2.25%	872	3.6%	.71%
100 basis points to 1.25%	446	1.8%	.36%

First Mid Bank's Board of Directors has adopted an interest rate risk policy that establishes maximum decreases in the percentage change in net interest margin of 5% in a 100 basis point rate shift and 10% in a 200 basis point rate shift.

No assurance can be given that the actual net interest income would increase or decrease by such amounts in response to a 100 or 200 basis point increase or decrease in the prime rate because it is also affected by many other factors. The results above are based on one-time “shock” moves and do not take into account any management response or mitigating action.

Interest rate sensitivity analysis is also used to measure the Company’s interest risk by computing estimated changes in the Economic Value of Equity (EVE) of First Mid Bank under various interest rate shocks. EVE is determined by calculating the net present value of each asset and liability category by rate shock. The net differential between assets and liabilities is the Economic Value of Equity. EVE is an expression of the long-term interest rate risk in the balance sheet as a whole.

The following table presents First Mid Bank's projected change in EVE for the various rate shock levels at December 31, 2009 and 2008 (in thousands). All market risk sensitive instruments presented in the tables are held-to-maturity or available-for-sale. First Mid Bank has no trading securities.

	Changes In Interest Rates (basis points)		Change in Economic Value of Equity: Amount of Change ($000)	Change in Economic Value of Equity: Percent of Change
December 31, 2009	+200	bp	$3,670	1.7%
	+100	bp	3,530	1.7%
	-200	bp	(24,633)	(11.7)%
	-100	bp	(11,941)	(5.7)%
December 31, 2008	+200	bp	$10,065	6.5%
	+100	bp	9,835	6.4%
	-200	bp	(15,396)	(10.0)%
	-100	bp	(3,121)	(2.0)%

As indicated above, at December 31, 2009, in the event of a sudden and sustained increase in prevailing market interest rates, First Mid Bank's EVE would be expected to increase, and in the event of a sudden and sustained decrease in prevailing market interest rates, First Mid Bank's EVE would be expected to decrease. At December 31, 2009, First Mid Bank's estimated changes in EVE were within the First Mid Bank's policy guidelines that normally allow for a change in capital of +/-10% from the base case scenario under a 100 basis point shock and +/- 20% from the base case scenario under a 200 basis point shock.

Computation of prospective effects of hypothetical interest rate changes are based on numerous assumptions, including relative levels of market interest rates, loan prepayments and declines in deposit balances, and should not be relied upon as indicative of actual results. Further, the computations do not contemplate any actions First Mid Bank may undertake in response to changes in interest rates.

Certain shortcomings are inherent in the method of analysis presented in the computation of EVE. Actual values may differ from those projections set forth in the table, should market conditions vary from assumptions used in the preparation of the table. Certain assets, such as adjustable-rate loans, have features that restrict changes in interest rates on a short-term basis and over the life of the asset. In addition, the proportion of adjustable-rate loans in First Mid Bank's portfolio change in future periods as market rates change. Further, in the event of a change in interest rates, prepayment and early withdrawal levels would likely deviate significantly from those assumed in the table. Finally, the ability of many borrowers to repay their adjustable-rate debt may decrease in the event of an interest rate increase.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Consolidated Balance Sheets		
December 31, 2009 and 2008		
(In thousands, except share data)	2009	2008
Assets		
Cash and due from banks		
Non-interest bearing	$ 20,243	$ 17,077
Interest bearing	19,512	31,266
Federal funds sold	60,000	38,300
Cash and cash equivalents	99,755	86,643
Investment securities:		
Available-for-sale, at fair value	238,697	169,476
Held-to-maturity, at amortized cost (estimated fair value of		
$469 and $610 at December 31, 2009 and 2008, respectively)	459	599
Loans held for sale	149	537
Loans	700,601	741,401
Less allowance for loan losses	(9,462)	(7,587)
Net loans	691,139	733,814
Interest receivable	6,871	7,161
Other real estate owned	2,862	2,388
Premises and equipment, net	15,487	14,985
Goodwill, net	17,363	17,363
Intangible assets, net	2,832	3,562
Other assets	19,541	13,172
Total assets	$ 1,095,155	$ 1,049,700
Liabilities and Stockholders' Equity		
Deposits:		
Non-interest bearing	$ 128,726	$ 119,986
Interest bearing	711,684	686,368
Total deposits	840,410	806,354
Securities sold under agreements to repurchase	80,386	80,708
Interest payable	861	1,616
FHLB borrowings	32,750	37,750
Other borrowings	-	13,000
Junior subordinated debentures	20,620	20,620
Other liabilities	8,907	6,874
Total liabilities	983,934	966,922
Stockholders' Equity		
Preferred stock, no par value, authorized 1,000,000 shares; issued 4,927 shares in 2009	24,635	-
Common stock, $4 par value; authorized 18,000,000 shares;		
issued 7,364,959 shares in 2009 and 7,254,117 shares in 2008	29,460	29,017
Additional paid-in capital	26,811	25,289
Retained earnings	62,144	58,059
Deferred compensation	2,894	2,787
Accumulated other comprehensive income (loss)	464	(416)
Less treasury stock at cost, 1,282,076 shares in 2009 and 1,121,273 shares in 2008	(35,187)	(31,958)
Total stockholders' equity	111,221	82,778
Total liabilities and stockholders' equity	$ 1,095,155	$ 1,049,700

See accompanying notes to consolidated financial statements.

Consolidated Statements of Income			
For the years ended December 31, 2009, 2008 and 2007			
(In thousands, except per share data)	2009	2008	2007
Interest income:			
Interest and fees on loans	$42,146	$47,748	$50,557
Interest on investment securities:			
Taxable	8,073	7,725	8,448
Exempt from federal income tax	963	834	712
Interest on federal funds sold	66	336	201
Interest on deposits with other financial institutions	161	423	13
Total interest income	51,409	57,066	59,931
Interest expense:			
Interest on deposits	12,970	16,592	21,591
Interest on securities sold under agreements to repurchase	129	872	2,419
Interest on FHLB advances	1,612	1,991	1,729
Interest on federal funds purchased	-	-	206
Interest on other borrowings	22	493	914
Interest on subordinated debt	1,104	1,396	1,570
Total interest expense	15,837	21,344	28,429
Net interest income	35,572	35,722	31,502
Provision for loan losses	3,594	3,559	862
Net interest income after provision for loan losses	31,978	32,163	30,640
Other income:			
Trust revenues	2,229	2,666	2,607
Brokerage commissions	424	574	528
Insurance commissions	1,912	1,978	1,950
Service charges	4,952	5,571	5,621
Securities gains, net	637	293	256
Total other-than-temporary impairment losses on securities	(2,465)	-	-
Portion of loss recognized in other comprehensive loss (before taxes)	653	-	-
Other-than-temporary impairment losses recognized in earnings	(1,812)	-	-
Gain on sale of merchant banking portfolio	1,000	-	-
Mortgage banking revenue, net	664	437	482
Other	3,449	3,745	3,217
Total other income	13,455	15,264	14,661
Other expense:			
Salaries and employee benefits	16,830	16,876	16,408
Net occupancy and equipment expense	4,989	4,959	4,831
Net other real estate owned expense	470	234	82
FDIC insurance expense	1,943	158	91
Amortization of other intangible assets	730	766	821
Stationery and supplies	563	557	547
Legal and professional	2,021	1,820	1,641
Marketing and promotion	963	847	911
Other	4,703	5,243	4,723
Total other expense	33,212	31,460	30,055
Income before income taxes	12,221	15,967	15,246
Income taxes	4,007	5,443	5,087
Net income	$8,214	$10,524	$10,159

Dividends on preferred shares	1,821	-	-
Net income available to common stockholders	$6,393	$10,524	$10,159
Per common share data:			
Basic earnings per share	$1.04	$1.69	$1.60
Diluted earnings per share	1.04	1.67	1.57
Cash dividends per share	.38	.38	.38

See accompanying notes to consolidated financial statements.

Consolidated Statements of Changes in Stockholders' Equity
For the years ended December 31, 2009, 2008 and 2007
(In thousands, except share and per share data)

	Preferred Stock	Common Stock	Additional Paid-In-Capital	Retained Earnings	Deferred Compensation	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total
December 31, 2006	$ -	$ 22,808	$21,261	$68,625	$2,629	$19	$(39,556)	$75,786
Comprehensive income:								
Net income	-	-	-	10,159	-	-	-	10,159
Net unrealized change in available-for-sale investment securities	-	-	-	-	-	1,077	-	1,077
Total Comprehensive Income								11,236
Cash dividends on common stock ($.38 per share)	-	-	-	(2,375)	-	-	-	(2,375)
Issuance of 28,778 common shares pursuant to the Dividend Reinvestment Plan	-	77	713	-	-	-	-	790
Issuance of 10,651 common shares pursuant to the Deferred Compensation Plan	-	32	254	-	-	-	-	286
Issuance of 3,087 common shares pursuant to the First Retirement & Savings Plan	-	11	71	-	-	-	-	82
Purchase of 237,128 treasury shares	-	-	-	-	-	-	(6,481)	(6,481)
Deferred compensation	-	-	-	-	(61)	-	61	-
Tax benefit related to deferred compensation distributions	-	-	409	-	-	-	-	409
Issuance of 39,801 common shares pursuant to the exercise of stock options	-	119	322	-	-	-	-	441
Tax benefit related to exercise of incentive stock options	-	-	153	-	-	-	-	153
Tax benefit related to exercise of non-qualified stock options	-	-	64	-	-	-	-	64
	-	-	61	-	-	-	-	61

Vested stock options compensation expense								
Retirement of 1,500,000 treasury shares	-	(4,000)	-	(17,021)	-	-	21,021	-
3-for-2 stock split in the form of 50% stock dividend	-	9,493	-	(9,493)	-	-	-	-
December 31, 2007	$ -	$ 28,540	$23,308	$49,895	$2,568	$1,096	$(24,955)	$80,452
Comprehensive income:								
Net income	-	-	-	10,524	-	-	-	10,524
Net unrealized change in available-for-sale investment securities	-	-	-	-	-	(1,512)	-	(1,512)
Total Comprehensive Income	-							9,012
Cash dividends on common stock ($.38 per share)	-	-	-	(2,360)	-	-	-	(2360)
Issuance of 31,684 common shares pursuant to the Dividend Reinvestment Plan	-	127	697	-	-	-	-	824
Issuance of 7,600 common shares pursuant to the Deferred Compensation Plan	-	31	158	-	-	-	-	189
Issuance of 7,161 common shares pursuant to the First Retirement & Savings Plan	-	29	145	-	-	-	-	174
Purchase of 262,877 treasury shares	-	-	-	-	-	-	(6,784)	(6,784)
Deferred compensation	-	-	-	-	219	-	(219)	-
Tax benefit related to deferred compensation distributions	-	-	34	-	-	-	-	34
Issuance of 72,559 common shares pursuant to the exercise of stock options	-	290	483	-	-	-	-	773
Tax benefit related to exercise of incentive stock options	-	-	263	-	-	-	-	263
Tax benefit related to exercise of non-qualified stock options	-	-	143	-	-	-	-	143
Vested stock options compensation expense	-	-	58	-	-	-	-	58
December 31, 2008	$ -	$ 29,017	$25,289	$58,059	$2,787	$(416)	$(31,958)	$82,778

Consolidated Statements of Changes in Stockholders' Equity								
For the years ended December 31, 2009, 2008 and 2007						Accumulated		
(In thousands, except share and per share data)			Additional			Other		
	Preferred	Common	Paid-In-	Retained	Deferred	Comprehensive	Treasury	
	Stock	Stock	Capital	Earnings	Compensation	Income (Loss)	Stock	Total
December 31, 2008	$ -	$ 29,017	$25,289	$58,059	$2,787	$(416)	$(31,958)	$82,778
Comprehensive income:								
Net income	-	-	-	8,214	-	-	-	8,214
Net unrealized change in available-for-sale investment securities	-	-	-	-	-	880	-	880
Total Comprehensive Income								9,094
Cash dividends on preferred stock ($370 per share)	-	-	-	(1,821)	-	-	-	(1,821)
Cash dividends on common stock ($.38 per share)	-	-	-	(2,308)	-	-	-	(2,308)
Issuance of 4,927 shares of preferred stock	24,635	-	-	-	-	-	-	24,635
Issuance of 44,661 common shares pursuant to the Dividend Reinvestment Plan	-	179	674	-	-	-	-	853
Issuance of 9,916 common shares pursuant to the Deferred Compensation Plan	-	40	136	-	-	-	-	176
Issuance of 19,000 common shares pursuant to the First Retirement & Savings Plan	-	75	255	-	-	-	-	330
Purchase of 160,803 treasury shares	-	-	-	-	-	-	(3,122)	(3,122)
Deferred compensation	-	-	-	-	107	-	(107)	-
	-	-	67	-	-	-	-	67

Tax benefit related to deferred compensation distributions								
Issuance of 37,266 common shares pursuant to the exercise of stock options	-	149	239	-	-	-	-	388
Tax benefit related to exercise of incentive stock options	-	-	19	-	-	-	-	19
Tax benefit related to exercise of non-qualified stock options	-	-	79	-	-	-	-	79
Vested stock options compensation expense	-	-	53	-	-	-	-	53
December 31, 2009	$ 24,635	$ 29,460	$26,811	$62,144	$2,894	$464	$(35,187)	$111,221

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows			
For the years ended December 31, 2009, 2008 and 2007			
(In thousands)	2009	2008	2007
Cash flows from operating activities:			
Net income	$8,214	$10,524	$10,159
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for loan losses	3,594	3,559	862
Depreciation, amortization and accretion, net	3,070	2,234	1,845
Compensation expense for vested stock options	53	58	61
Gain on investment securities, net	(637)	(293)	(256)
Other-than-temporary impairment losses on securities recognized in earnings	1,812	-	-
Loss on sales of other real property owned, net	353	153	7
Loss on write own of fixed assets	80	132	-
Gain on sale of merchant banking portfolio	(1,000)	-	-
Gain on sales of loans held for sale, net	(727)	(520)	(560)
Deferred income taxes	(1,515)	(631)	(218)
Decrease in accrued interest receivable	290	1,148	108
Decrease in accrued interest payable	(755)	(648)	(181)
Origination of loans held for sale	(62,904)	(44,103)	(47,714)
Proceeds from sales of loans held for sale	64,019	46,060	48,534
Increase in other assets	(7,145)	(2,467)	(188)
Increase in other liabilities	1,522	24	176
Net cash provided by operating activities	8,324	15,230	12,635
Cash flows from investing activities:			
Proceeds from sales of securities available-for-sale	38,275	2,322	14,007
Proceeds from maturities of securities available-for-sale	63,321	90,439	64,172
Proceeds from maturities of securities held-to-maturity	140	580	145
Purchases of securities available-for-sale	(171,440)	(80,243)	(80,478)
Net decrease (increase) in loans	39,081	2,696	(25,473)
Purchases of premises and equipment	(1,954)	(1,082)	(856)
Proceeds from sales of other real property owned	1,987	1,100	1,274
Net cash provided by (used in) investing activities	(30,590)	15,812	(27,209)
Cash flows from financing activities:			
Net increase (decrease) in deposits	34,056	35,771	(12)
Decrease in federal funds purchased	-	-	(6,800)
Increase (decrease)in repurchase agreements	(322)	12,408	1,607
Proceeds from short-term FHLB advances	-	-	69,000
Repayment of short-term FHLB advances	-	(10,000)	(61,000)
Proceeds from long-term FHLB advances	-	-	24,750
Repayment of long-term FHLB advances	(5,000)	(5,000)	-
Proceeds from long-term debt	-	5,000	9,000
Repayment of long-term debt	(13,000)	(6,500)	(5,500)
Proceeds from issuance of common stock	894	1,136	809
Proceeds from issuance of preferred stock	24,635	-	-
Purchase of treasury stock	(3,122)	(6,784)	(6,481)
Dividends paid on preferred stock	(1,242)	-	-
Dividends paid on common stock	(1,521)	(1,553)	(1,512)
Net cash provided by financing activities	35,378	24,478	23,861

Increase in cash and cash equivalents	13,112	55,520	9,287
Cash and cash equivalents at beginning of year	86,643	31,123	21,836
Cash and cash equivalents at end of year	$99,755	$86,643	$31,123

	2009	2008	2007
Supplemental disclosures of cash flow information			
Cash paid during the year for:			
Interest	$16,592	$21,992	$28,610
Income taxes	4,596	6,086	4,306
Supplemental disclosure of noncash investing and financing activities:			
Loans transferred to real estate owned	$2,847	$2,900	$625
Dividends reinvested in common shares	853	824	790
Net tax benefit related to option and deferred compensation plans	165	440	626

See accompanying notes to consolidated financial statements.

Notes To Consolidated Financial Statements
December 31, 2009, 2008 and 2007
(Table dollar amounts in thousands, except share data)

Note 1 – Summary of Significant Accounting Policies

Basis of Accounting and Consolidation

The accompanying consolidated financial statements include the accounts of First Mid-Illinois Bancshares, Inc. ("Company") and its wholly-owned subsidiaries: Mid-Illinois Data Services, Inc. ("MIDS"), First Mid-Illinois Bank & Trust, N.A. ("First Mid Bank") and The Checkley Agency, Inc. ("Checkley"). All significant intercompany balances and transactions have been eliminated in consolidation. Certain amounts in the prior years' consolidated financial statements have been reclassified to conform to the 2009 presentation and there was no impact on net income or stockholders' equity from these reclassifications. The Company operates as a one-segment entity for financial reporting purposes. The accounting and reporting policies of the Company conform to accounting principles generally accepted in the United States of America. Following is a description of the more significant of these policies.

Current Economic Conditions

The current protracted economic decline continues to present financial institutions with circumstances and challenges, which in some cases have resulted in large and unanticipated declines in the fair values of investments and other assets, constraints on liquidity and capital and significant credit quality problems, including severe volatility in the valuation of real estate and other collateral supporting loans.

The accompanying financial statements have been prepared using values and information currently available to the Company.

Given the volatility of current economic conditions, the values of assets and liabilities recorded in the financial statements could change rapidly, resulting in material future adjustments in asset values, the allowance for loan losses and capital that could negatively impact the Company's ability to meet regulatory capital requirements and maintain sufficient liquidity.

At December 31, 2009, the Company held $226.4 million in commercial real estate loans and $28 million in construction and land development loans. Due to national, state and local economic conditions, values for commercial and development real estate have declined, and the market for these properties is depressed.

At December 31, 2009, the Company held $54 million in agricultural production loans and $62 million in agricultural real estate loans. Values of agricultural real estate in the current market have declined due to locally depressed markets which has significantly affected the repayment ability for some agricultural loan customers.

In addition, the Company has $50.8 million of loans in the hospitality (motels and hotels) industry. Due to national, state and local economic conditions, values for commercial real estate and, specifically hotel properties, have declined and the market for these properties is depressed. The performance of these loans is also dependent on borrower specific issues as well as the general level of business and personal travel within the region.

The Company also has $72.0 million of loans to lessors of non-residential buildings and $44.2 million of loans to lessors of residential buildings and dwellings. Due to national, state and local economic conditions, values for commercial real estate have declined and the market for these properties is also depressed.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires the Company to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. The Company uses estimates and employs the judgments of management in determining the amount of its allowance for loan losses and income tax accruals and deferrals, in its fair value measurements of investment securities, and in the evaluation of impairment of loans, goodwill, investment securities, and fixed assets. As with any estimate, actual results could differ from these estimates. Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses. In connection with the determination of the allowance for loan losses, management obtains independent appraisals for significant properties.

Fair Value Measurements

The fair value of a financial instrument is defined as the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. The Company estimates the fair value of a financial instrument using a variety of valuation methods. Where financial instruments are actively traded and have quoted market prices, quoted market prices are used for fair value. When the financial instruments are not actively traded, other observable market inputs, such as quoted prices of securities with similar characteristics, may be used, if available, to determine fair value. When observable market prices do not exist, the Company estimates fair value. The Company’s valuation methods consider factors such as liquidity and concentration concerns. Other factors such as model assumptions, market dislocations, and unexpected correlations can affect estimates of fair value. Imprecision in estimating these factors can impact the amount of revenue or loss recorded.

SFAS No. 157, Fair Value Measurements, which was codified into ASC 820, establishes a framework for measuring the fair value of financial instruments that considers the attributes specific to particular assets or liabilities and establishes a three-level hierarchy for determining fair value based on the transparency of inputs to each valuation as of the fair value measurement date. The three levels are defined as follows:

- Level 1 — quoted prices (unadjusted) for identical assets or liabilities in active markets.
- Level 2 — inputs include quoted prices for similar assets and liabilities in active markets, quoted prices of identical or similar assets or liabilities in markets that are not active, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.
- Level 3 — inputs that are unobservable and significant to the fair value measurement.

At the end of each quarter, the Company assesses the valuation hierarchy for each asset or liability measured. From time to time, assets or liabilities may be transferred within hierarchy levels due to changes in availability of observable market inputs to measure fair value at the measurement date. Transfers into or out of hierarchy levels are based upon the fair value at the beginning of the reporting period. A more detailed description of the fair values measured at each level of the fair value hierarchy can be found in Note 12 – "Disclosures of Fair Values of Financial Instruments."

Cash and Cash Equivalents

For purposes of reporting cash flows, cash equivalents include non-interest bearing and interest bearing cash and due from banks and federal funds sold. Generally, federal funds are sold for one-day periods.

Investment Securities

The Company classifies its debt securities into one or more of three categories: held-to-maturity, available-for-sale, or trading. Held-to-maturity securities are those which management has the positive intent and ability to hold to maturity. Available-for-sale securities are those securities which management may sell prior to maturity as a result of changes in interest rates, prepayment factors, or as part of the Company's overall asset and liability strategy. Trading securities are those securities bought and held principally for the purpose of selling them in the near term. The Company had no securities designated as trading during 2009, 2008 or 2007.

Held-to-maturity securities are recorded at cost adjusted for amortization of premiums and accretion of discounts to the earlier of the call date or maturity date using the interest method. Available-for-sale securities are recorded at fair value. Unrealized holding gains and losses, net of the related income tax effect, are excluded from income and reported as a separate component of stockholders' equity. If a decrease in the fair value of a security is expected to be other than temporary, then the security is written down to its fair value through a charge to income and a new cost basis is established for the security.

Realized gains and losses on the sale of investment securities are recorded using the specific identification method.

Effective April 2009, the Company adopted new accounting guidance (ASC 320-10) related to recognition and presentation of other-than-temporary impairment ("OTTI"). When the Company does not intend to sell a debt security, and it is more likely than not, the Company will not have to sell the security before recovery of its cost basis, it recognizes the credit component of an OTTI of a debt security in earnings and the remaining portion in other comprehensive income. For held-to-maturity debt securities, the amount of an OTTI recorded in other comprehensive income for the noncredit portion of a previous OTTI is amortized prospectively over the remaining life of the security on the basis of the timing of future estimated cash flows of the security.

As a result of this guidance, the Company's consolidated statement of income as of December 31, 2009, reflects the full impairment (that is, the difference between the security's amortized cost basis and fair value) on debt securities that the Company intends to sell or would more likely than not be required to sell before the expected recovery of the amortized cost basis. For available-for-sale and held-to-maturity debt securities that management has no intent to sell and believes that it more likely than not will not be required to sell prior to recovery, only the credit loss component of the impairment is recognized in earnings, while the noncredit loss is recognized in accumulated other comprehensive income. The credit loss component recognized in earnings is identified as the amount of principal cash flows not expected to be received over the remaining term of the security as projected based on cash flow projections.

Prior to the adoption of the recent accounting guidance in April 2009, management considered, in determining whether OTTI exists, (1) the length of time and the extent to which fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer(s) and (3) the intent and ability of the Company to retain its investment in the security for a period sufficient to allow for any anticipated recovery in fair value.

Loans

Loans are stated at the principal amount outstanding net of unearned discounts, unearned income and the allowance for loan losses. Unearned income includes deferred loan origination fees reduced by loan origination costs and is amortized to interest income over the life of the related loan using methods that approximate the effective interest rate method. Interest on substantially all loans is credited to income based on the principal amount outstanding.

The Company's policy is to discontinue the accrual of interest income on any loan that becomes ninety days past due as to principal or interest or earlier when, in the opinion of management there is reasonable doubt as to the timely collection of principal or interest. Nonaccrual loans are returned to accrual status when, in the opinion of management, the financial position of the borrower indicates there is no longer any reasonable doubt as to the timely collectibility of interest or principal.

Loans expected to be sold are classified as held for sale in the consolidated financial statements and are recorded at the lower of aggregate cost or market value, taking into consideration future commitments to sell the loans.

Allowance for Loan Losses

The allowance for loan losses is maintained at a level deemed appropriate by management to provide for probable losses inherent in the loan portfolio. The allowance is based on a continuing review of the loan portfolio, the underlying value of the collateral securing the loans, current economic conditions and past loan loss experience. Loans that are deemed to be uncollectible are charged off to the allowance. The provision for loan losses and recoveries are credited to the allowance.

Management, considering current information and events regarding the borrowers' ability to repay their obligations, considers a loan to be impaired when it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the note agreement, including principal and interest. The amount of the impairment is measured based on the fair value of the collateral, if the loan is collateral dependent, or alternatively, at the present value of expected future cash flows discounted at the loan's effective interest rate. Certain homogeneous loans such as residential real estate mortgage and installment loans are excluded from the impaired loan provisions. Interest income on impaired loans is recorded when cash is received and only if principal is considered to be fully collectible.

Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization is charged to expense and determined principally by the straight-line method over the estimated useful lives of the assets.

The estimated useful lives for each major depreciable classification of premises and equipment are as follows:

Buildings and improvements	20 - 40 years
Leasehold improvements	5-15 years
Furniture and equipment	3-7 years

Goodwill and Intangible Assets

The Company has goodwill from business combinations, identifiable intangible assets assigned to core deposit relationships and customer lists acquired, and intangible assets arising from the rights to service mortgage loans for others.

Identifiable intangible assets generally arise from branches acquired that the Company accounted for as purchases. Such assets consist of the excess of the purchase price over the fair value of net assets acquired, with specific amounts assigned to core deposit relationships and customer lists primarily related to insurance agency. Intangible assets are amortized by the straight-line method over various periods up to fifteen years. Management reviews intangible assets for possible impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

In accordance with the provisions of SFAS No. 142, "Goodwill and Other Intangible Assets," codified into ASC 350, the Company performed testing of goodwill for impairment as of September 30, 2009 and determined that, as of that date, goodwill was not impaired. Management also concluded that the remaining amounts and amortization periods were appropriate for all intangible assets.

Other Real Estate Owned

Other real estate owned acquired through loan foreclosure are initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. The adjustment at the time of foreclosure is recorded through the allowance for loan losses. Due to the subjective nature of establishing the fair value when the asset is acquired, the actual fair value of the other real estate owned or foreclosed asset could differ from the original estimate. If it is determined that fair value temporarily declines subsequent to foreclosure, a valuation allowance is recorded through noninterest expense. Operating costs associated with the assets after acquisition are also recorded as noninterest expense. Gains and losses on the disposition of other real estate owned and foreclosed assets are netted and posted to other noninterest expense.

Federal Home Loan Bank Stock

Federal Home Loan Bank stock is a required investment for institutions that are members of the Federal Home Loan Bank system. The required investment in the common stock is based on a predetermined formula.

The Company owns approximately $3.7 million of Federal Home Loan Bank of Chicago (FHLB) stock included in other assets as of December 31, 2009 and 2008. During the third quarter of 2007, the FHLB received a Cease and Desist Order from its regulator, the Federal Housing Finance Board. The FHLB will continue to provide liquidity and funding through advances; however, the order prohibited capital stock repurchases and redemptions until a time to be determined by the Federal Housing Finance Board and requires Federal Housing Finance Board approval for dividends. On July 24, 2008, the Federal Housing Finance Board amended the order to allow the FHLB to repurchase or redeem any capital stock issued to support new advances after the repayment of those new advances if certain conditions are met. The amended order, however, provides that the Director of the Office of Supervision of the Federal Housing Finance Board may direct the FHLB to halt the repurchase of redemption of capital stock if, in his sole discretion, the continuation of such transactions would be inconsistent with maintaining the capital adequacy of the FHLB and its safe and sound operations. With regard to dividends, the FHLB continues to assess its dividend capacity each quarter and make appropriate request for approval. There were no dividends paid by the FHLB during 2009 or 2008. The Company evaluated its cost investment in FHLB stock and deemed it was ultimately recoverable.

Temporary Liquidity Guarantee Program

On October 14, 2008, the FDIC announced the Temporary Liquidity Guarantee Program (TLGP). The final rule was adopted on November 21, 2008. The FDIC stated that the purpose of these actions is to strengthen confidence and encourage liquidity in the banking system by guaranteeing newly issued senior unsecured debt of 31 days or greater, of banks, thrifts, and certain holding companies, and by providing full FDIC insurance coverage for all non-interest bearing transaction accounts, regardless of dollar amount. Inclusion in the program was voluntary. Institutions participating in the senior unsecured debt portion of the program are assessed fees based on a sliding scale, depending on length of maturity. Shorter-term debt has a lower fee structure and longer-term debt has a higher fee. The range is from 50 basis points on debt of 180 days or less, to a maximum of 100 basis points for debt with maturities of one year or longer, on an annualized basis. A 10-basis point surcharge is added to a participating institution's current insurance assessment in exchange for final coverage for all transaction accounts.

First Mid Bank elected to participate in both parts of the TLGP, the Transaction Account Guarantee Program and the Debt Guarantee Program. The FDIC’s Transaction Account Guarantee Program, provides, without charge to depositors, a full guarantee on all non-interest bearing transaction accounts held by any depositor, regardless of dollar amount, through June 30, 2010. Participation in the Transaction Account Guarantee Program cost the Company 10 basis points annually on the amount of the deposits. The FDIC’s Debt Guarantee Program, which expired in October 2009, provided for the guarantee of eligible newly issued senior unsecured debt of participating entities, but the Company and the Bank did not issue any debt under this program.

Federal Deposit Insurance Corporation Insurance Coverage

As an FDIC-insured institution, First Mid Bank is required to pay deposit insurance premium assessments to the FDIC. On October 3, 2008, the FDIC temporarily increased the standard maximum deposit insurance amount (SMDIA) from $100,000 to $250,000 per depositor. On May 20, 2009, the Helping Families Save Their Homes Act extended the temporary increase in the SMDIA through December 31, 2013. This extension of the temporary $250,000 coverage limit became effective immediately upon the President’s signature. The legislation provides that the SMDIA will return to $100,000 on January 1, 2014. The additional cost of the increase to the SMDIA, assessed on a quarterly basis, is a 10 basis point annualized surcharge (2.5 basis points quarterly) on balances in non-interest bearing transaction accounts that exceed $250,000. The Company has expensed $49,000 for this program in 2009.

On February 27, 2009, the FDIC adopted a final rule modifying the risk-based assessment system and setting initial base assessment rates beginning April 1, 2009, at 12 to 45 basis points and, due to extraordinary circumstances, extended the period of the restoration plan to increase the deposit insurance fund to seven years. Also on February 27, 2009, the FDIC issued final rules on changes to the risk-based assessment system. The final rules both increase base assessment rates and incorporate additional assessments for excess reliance on brokered deposits and FHLB advances. The new rates would increase annual assessment rates from 5 to 7 basis points to 7 to 24 basis points. This new assessment took effect April 1, 2009. First Mid Bank’s assessment rate at December 31, 2009 was 13.27 basis points. The Company has expensed $1,260,000 for this assessment in 2009.

Also on February 27, 2009, the FDIC adopted an interim rule to impose a 20 basis point emergency special assessment payable September 30, 2009 based on the second quarter 2009 assessment base, to help shore up the Deposit Insurance Fund (“DIF”). This assessment equates to a one-time cost of $200,000 per $100 million in assessment base. The interim rule also allows the Board to impose possible additional special assessments of up to 10 basis points thereafter to maintain public confidence in the DIF. Subsequently, the FDIC’s Treasury borrowing authority increased from $30 billion to $100 billion, allowing the agency to cut the planned special assessment from 20 to 10 basis points. On May 22, 2009, the FDIC adopted a final rule which established a special assessment of five basis points on each FDIC-insured depository institutions assets, minus it Tier 1 capital, as of September 30, 2009. The assessment was capped at 10 basis points of an institution’s domestic deposits so that no institution would pay an amount higher than they would have under the interim rule. This special assessment was collected September 30, 2009. The Company expensed $522,000 as of June 30, 2009 for this special assessment.

In addition to its insurance assessment, each insured bank was subject, in 2009, to quarterly debt service assessments in connection with bonds issued by a government corporation that financed the federal savings and loan bailout. The Company expensed $112,000 during 2009 for this assessment.

On September 29, 2009, the FDIC Board proposed a Deposit Insurance Fund restoration plan that required banks 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. Under the plan—which applies to all banks except those with liquidity problems—banks were assessed through 2010 according to the risk-based premium schedule adopted earlier this year. Beginning January 1, 2011, the base rate increase by 3 basis points. The Company recorded a prepaid expense asset of $4,855,000 as of December 31, 2009 as a result of this plan. This asset will be amortized to non-interest expense over the next three years.

Income Taxes

The Company and its subsidiaries file consolidated federal and state income tax returns with each organization computing its taxes on a separate company basis. Amounts provided for income tax expense are based on income reported for financial statement purposes rather than amounts currently payable under tax laws.

Deferred tax assets and liabilities are recognized for future tax consequences attributable to the temporary differences existing between the financial statement carrying amounts of assets and liabilities and their respective tax basis, as well as operating loss and tax credit carry forwards. To the extent that current available evidence about the future raises doubt about the realization of a deferred tax asset, a valuation allowance is established. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized as an increase or decrease in income tax expense in the period in which such change is enacted.

Additionally, the Company reviews its uncertain tax positions annually under FASB Interpretation No. 48 (FIN No. 48), “Accounting for Uncertainty in Income Taxes,” codified within ASC 740. An uncertain tax position is recognized as a benefit only if it is "more likely than not" that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount actually recognized is the largest amount of tax benefit that is greater than 50% likely to be recognized on examination. For tax positions not meeting the "more likely than not" test, no tax benefit is recorded. A significant amount of judgment is applied to determine both whether the tax position meets the "more likely than not" test as well as to determine the largest amount of tax benefit that is greater than 50% likely to be recognized. Differences between the position taken by management and that of taxing authorities could result in a reduction of a tax benefit or increase to tax liability, which could adversely affect future income tax expense.

Trust Department Assets

Assets held in fiduciary or agency capacities are not included in the consolidated balance sheets since such items are not assets of the Company or its subsidiaries. Fees from trust activities are recorded on an cash basis over the period in which the service is provided. Fees are a function of the market value of assets managed and administered, the volume of transactions, and fees for other services rendered, as set forth in the underlying client agreement with the Trust & Wealth Management Division of First Mid Bank. This revenue recognition involves the use of estimates and assumptions, including components that are calculated based on asset valuations and transaction volumes. Any out of pocket expenses or services not typically covered by the fee schedule for trust activities are charged directly to the trust account on a gross basis as trust revenue is incurred. At December 31, 2009, the Company managed or administered 1,117 accounts with assets totaling approximately $459,149,000. At December 31, 2008, the Company managed or administered 1,115 accounts with assets totaling approximately $413,754,000.

Preferred Stock

During 2009, the Company sold to certain accredited investors including directors, executive officers, and certain major customers and holders of the Company’s common stock, $24,635,000, in the aggregate, of a newly authorized series of its preferred stock designated as Series B 9% Non-Cumulative Perpetual Convertible Preferred Stock. The Series B Preferred Stock had an issue price of $5,000 per share and no par value per share. The Series B Preferred Stock was issued in a private placement exempt from registration pursuant to Regulation D of the Securities Act of 1933, as amended.

The Series B Preferred Stock pays non-cumulative dividends semiannually in arrears, when, as and if authorized by the Board of Directors of the Company, at a rate of 9% per year. Holders of the Series B Preferred Stock will have no voting rights, except with respect to certain fundamental changes in the terms of the Series B Preferred Stock and certain other matters. In addition, if dividends on the Series B Preferred Stock are not paid in full for four dividend periods, whether consecutive or not, the holders of the Series B Preferred Stock, acting as a class with any other of the Company’s securities having similar voting rights, will have the right to elect two directors to the Company’s Board of Directors. The terms of office of these directors will end when the Company has paid or set aside for payment full semi-annually dividends for four consecutive dividend periods.

Each share of the Series B Preferred Stock may be converted at any time at the option of the holder into shares of the Company’s common stock. The number of shares of common stock into which each share of the Series B Preferred Stock is convertible is the $5,000 liquidation preference per share divided by the Conversion Price of $21.94. The Conversion Price is subject to adjustment from time to time pursuant to the terms of the Certificate of Designations. If at the time of conversion, there are any authorized, declared and unpaid dividends with respect to a converted share of Series B Preferred Stock, the holder will receive cash in lieu of the dividends, and a holder will receive cash in lieu of fractional shares of common stock following conversion.

After five years, the Company may, at its option but subject to the Company's receipt of any required prior approvals from the Board of Governors of the Federal Reserve System or any other regulatory authority, redeem the Series B Preferred Stock. Any redemption will be in exchange for cash in the amount of $5,000 per share, plus any authorized, declared and unpaid dividends, without accumulation of any undeclared dividends.

The Company also has the right at any time on or after the fifth anniversary of the original issuance date of the Series B Preferred Stock to require the conversion of all (but not less than all) of the Series B Preferred Stock into shares of common stock if, on the date notice of mandatory conversion is given to holders, the book value of the Company's common stock equals or exceeds 115% of the book value of the Company's common stock at September 30, 2008. "Book value of the Company's common stock" at any date means the result of dividing the Company's total common stockholders' equity at that date, determined in accordance with U.S. generally accepted accounting principles, by the number of shares of common stock then outstanding, net of any shares held in the treasury. The book value of the Company's common stock at September 30, 2008 was $13.03, and 115% of this amount is approximately $14.98. The book value of the Company's common stock at December 31, 2009 was $14.23.

Stock Split

On June 29, 2007, the Company effected a three-for-two stock split in the form of a 50% stock dividend. Accordingly, an entry was made for $9,493,000 to increase the common stock account and decrease the retained earnings account. Par value remained at $4 per share. The stock split increased the Company's outstanding common shares from 4,249,056 to 6,373,495 shares. All share and per share amounts have been restated for years prior to 2007 to give retroactive recognition to the stock split.

Treasury Stock

Treasury stock is stated at cost. Cost is determined by the first-in, first-out method.

Stock Options

Effective January 1, 2006, the Company adopted the fair value recognition provisions of SFAS No. 123R, Accounting for Stock-Based Compensation," which was codified into ASC 718, using the modified prospective application method. Accordingly, after January 1, 2006, the Company began expensing the fair value of stock options granted, modified, repurchased or cancelled. Additionally, compensation cost for a portion of the awards for which requisite services had not yet been rendered that were outstanding as of January 1, 2006 are being recognized as the requisite service is rendered. As a result of this adoption, the Company's income before income taxes and net income for the year ended December 31, 2009 includes stock option compensation cost of $53,000 and $51,000, respectively, which represents $.01 impact on basic and diluted earnings per share for the year. The Company's income before income taxes and net income for the year ended December 31, 2008 includes stock option compensation cost of $58,000 and $57,000, respectively, which represents $.01 impact on basic and diluted earnings per share for the year.

Comprehensive Income

Comprehensive income consists of net income and other comprehensive income, net of applicable income taxes. Other comprehensive income includes unrealized appreciation (depreciation) on available-for-sale securities and unrealized appreciation (depreciation) on available-for-sale securities for which a portion of an other-than-temporary impairment has been recognized in income.

The Company's comprehensive income for the years ended December 31, 2009, 2008 and 2007 is as follows:

	2009	2008	2007
Net income	$8,214	$10,524	$10,159
Other comprehensive income (loss):			
Unrealized gains (losses) on securities available-for-sale	2,732	(2,184)	2,020
Unrealized losses on securities available-for-sale for which a portion of an other-than-temporary impairment has been recognized in income	(2,465)	-	-
Other-than-temporary impairment losses recognized in earnings	1,812	-	-
Reclassification adjustment for realized gains included in income	(637)	(293)	(256)
Other comprehensive income (loss) before taxes	1,442	(2,477)	1,764
Tax benefit (expense)	(562)	965	(687)
Total other comprehensive income (loss)	880	(1,512)	1,077
Comprehensive income	$9,094	$9,012	$11,236

The components of accumulated other comprehensive income (loss) included in stockholders' equity are as follows:

December 31, 2009	Unrealized Gain (Loss) on Available for Sale Securities	Other-Than-Temporary Impairment Losses	Total
Net unrealized gains on securities available-for-sale	$5,364	$ -	$5,364
Other-than-temporary impairment losses on securities	-	(4,603)	(4,603)
Tax benefit (expense)	(2,091)	1,794	(297)
Balance at December 31, 2009	$3,273	$ (2,809)	$464

December 31, 2008	Unrealized Gain (Loss) on Available for Sale Securities	Other-Than-Temporary Impairment Losses	Total
Net unrealized gains (losses) on securities available-for-sale	$(681)	$ -	$(681)
Tax benefit (expense)	265	-	265
Balance at December 31, 2008	$(416)	$ -	$(416)

See Note 4 – “Investment Securities” for more detailed information regarding unrealized losses on available-for-sale securities.

Note 2 – Earnings Per Share

A three-for-two stock split was effected on June 29, 2007, in the form of a 50% stock dividend for the stockholders of record at the close of business on June 18, 2007. Accordingly, information with respect to shares of common stock and earnings per share has been restated for current and prior periods presented to fully reflect the stock split. Basic earnings per share ("EPS") is calculated as net income divided by the weighted average number of common shares outstanding. Diluted EPS is computed using the weighted average number of common shares outstanding, increased by the assumed conversion of the Company's stock options, unless anti-dilutive.

The components of basic and diluted earnings per common share for the years ended December 31, 2009, 2008 and 2007 are as follows:

	2009	2008	2007
Basic Earnings per Common Share:			
Net income	$8,214,000	$10,524,000	$10,159,000
Preferred stock dividends	(1,821,000)	-	-
Net income available to common stockholders	$6,393,000	$10,524,000	$10,159,000
Weighted average common shares outstanding	6,131,314	6,231,438	6,356,772
Basic earnings per common share	$1.04	$1.69	$1.60
Diluted Earnings per Common Share:			
Net income available to common stockholders	$6,393,000	$10,524,000	$10,159,000
Effect of assumed preferred stock conversion	-	-	-
Net income applicable to diluted earnings per share	$6,393,000	$10,524,000	$10,159,000
Weighted average common shares outstanding	6,131,314	6,231,438	6,356,772
Dilutive potential common shares:			
Assumed conversion of stock options	35,879	75,976	125,521
Assumed conversion of preferred stock	-	-	-
Diluted weighted average common shares outstanding	6,167,193	6,307,414	6,482,293
Diluted earnings per common share	$1.04	$1.67	$1.57

The following shares were not considered in computing diluted earnings per share for the years ended December 31, 2009, 2008 and 2007 because they were anti-dilutive:

	2009	2008	2007
Stock options to purchase shares of common stock	202,970	124,813	124,813
Average dilutive potential common shares associated with convertible preferred stock	1,031,982	--	--

Note 3 – Cash and Due from Banks

Aggregate cash and due from bank balances of $686,000, $808,000 and $392,000 were maintained in satisfaction of statutory reserve requirements of the Federal Reserve Bank at December 31, 2009, 2008 and 2007, respectively.

Note 4 – Investment Securities

The amortized cost, gross unrealized gains and losses and estimated fair values of available-for-sale and held-to-maturity securities by major security type at December 31, 2009 and 2008 were as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
2009				
Available-for-sale:				
U.S. Treasury securities and obligations of U.S. government corporations and Agencies	$89,640	$1,386	$(52)	$90,974
Obligations of states and political subdivisions	23,071	742	(97)	23,716
Mortgage-backed securities	111,301	3,343	(125)	114,519
Trust preferred securities	7,758	-	(4,603)	3,155
Other securities	6,166	187	(20)	6,333
Total available-for-sale	$237,936	$5,658	$(4,897)	$238,697
Held-to-maturity:				
Obligations of states and political subdivisions	$459	$10	$-	$469
2008				
Available-for-sale:				
U.S. Treasury securities and obligations of U.S. government corporations and Agencies	$72,074	$2,567	$(9)	$74,632
Obligations of states and political subdivisions	21,443	106	(627)	20,922
Mortgage-backed securities	61,102	1,715	(15)	62,802
Trust preferred securities	9,328	-	(3,950)	5,378
Other securities	6,210	-	(468)	5,742
Total available-for-sale	$170,157	$4,388	$(5,069)	$169,476
Held-to-maturity:				
Obligations of states and political subdivisions	$599	$11	$-	$610

The trust preferred securities are four trust preferred pooled securities issued by FTN Financial Securities Corp. ("FTN"). The unrealized losses of these securities, which have maturities ranging from four years to twenty nine years, is primarily due to their long-term nature, a lack of demand or inactive market for these securities, and concerns regarding the underlying financial institutions that have issued the trust preferred securities. See the heading "Trust Preferred Securities" below for further information regarding these securities. Except as discussed below, management believes the declines in fair value for these securities are temporary.

Proceeds from sales of investment securities, realized gains and losses and income tax expense and benefit were as follows during the years ended December 31, 2009, 2008 and 2007:

	2009	2008	2007
Proceeds from sales	$38,275	$2,322	$14,007
Gross gains	637	293	256
Gross losses	-	-	-
Income tax expense	223	103	90

The following table indicates the expected maturities of investment securities classified as available-for-sale and held-to-maturity, presented at amortized cost, at December 31, 2009 (dollars in thousands) and the weighted average yield for each range of maturities. Mortgage-backed securities are aged according to their weighted average life. All other securities are shown at their contractual maturity.

	One year or less	After 1 through 5 years	After 5 through 10 years	After 10 years	Total
Available-for-sale:					
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$50,227	$29,483	$9,930	$-	$89,640
Obligations of state and political subdivisions	2,795	3,868	16,078	330	23,071
Mortgage-backed securities	5,557	90,572	15,172	-	111,301
Trust preferred securities	1,511	6,247	-	-	7,758
Other securities	-	6,131	-	35	6,166
Total investments	$60,090	$136,301	$41,180	$365	$237,936
Weighted average yield	3.48 %	3.98 %	4.41 %	4.07 %	3.93 %
Full tax-equivalent yield	3.57 %	4.04 %	5.18 %	6.06 %	4.12 %
Held-to-maturity:					
Obligations of state and political subdivisions	$408	$51	$-	$-	$459
Weighted average yield	5.21 %	4.75 %	- %	- %	5.16 %
Full tax-equivalent yield	7.77 %	6.58 %	- %	- %	7.64 %

The weighted average yields are calculated on the basis of the amortized cost and effective yields weighted for the scheduled maturity of each security. Full tax-equivalent yields have been calculated using a 34% tax rate. With the exception of obligations of the U.S. Treasury and other U.S. government agencies and corporations, there were no investment securities of any single issuer the book value of which exceeded 10% of stockholders' equity at December 31, 2009.

Investment securities carried at approximately $185,357,000 and $152,598,000 at December 31, 2009 and 2008, respectively, were pledged to secure public deposits and repurchase agreements and for other purposes as permitted or required by law.

The following table presents the aging of gross unrealized losses and fair value by investment category as of December 31, 2009 and 2008:

	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
December 31, 2009:						
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$90,974	$(52)	$-	$-	$90,974	$(52)

Obligations of states and political subdivisions	23,015	(40)	1,170	(57)	24,185	(97)
Mortgage-backed securities	114,431	(124)	88	(1)	114,519	(125)
Trust preferred securities	-	-	3,155	(4,603)	3,155	(4,603)
Corporate bonds	6,318	-	15	(20)	6,333	(20)
Total	$234,738	$(216)	$4,428	$(4,681)	$239,166	$(4,897)
December 31, 2008:						
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$68,925	$-	$5,707	$(9)	$74,632	$(9)
Obligations of states and political subdivisions	21,532	(627)	-	-	21,532	(627)
Mortgage-backed securities	62,802	(15)	-	-	62,802	(15)
Trust preferred securities	3,448	(842)	1,930	(3,108)	5,378	(3,950)
Corporate bonds	5,742	(468)			5,742	(468)
Total	$162,449	$(1,952)	$7,637	$(3,117)	$170,086	$(5,069)

Obligations of states and political subdivisions

At December 31, 2009, there were four obligations of states and political subdivisions issued by two municipalities with a fair value of $1,170,000 and unrealized losses of $57,000 in a continuous unrealized loss position for twelve months or more. This position was due to municipal rates increasing since the purchase of the securities resulting in the market value being lower than book value. The contractual terms of these investments do not permit the issuer to settle the securities at a price less than the amortized cost basis of the investments. Because the Company does not intend to sell these securities and it is not more-likely-than-not the Company will be required to sell these securities, before recovery of their amortized cost bases, which may be maturity, the Company does not consider these investments to be other than temporarily impaired at December 31, 2009.

Mortgage-backed Securities

At December 31, 2009, there was one mortgage-backed security issued by Federal Home Loan Mortgage Corporation with a fair value of $88,000 and unrealized losses of $583 in a continuous unrealized loss position for twelve months or more. This position was due to intermediate rates increasing since the purchase of these securities resulting in the market value of the security being lower than book value. Because the decline in market value is attributable to changes in interest rates and not credit quality, and because the Company does not intend to sell this security and it is not more-likely-than-not the Company will be required to sell this security before recovery of its amortized cost basis, which may be maturity, the Company does not consider this investment to be other than temporarily impaired at December 31, 2009.

Trust Preferred Securities

At December 31, 2009, there were four trust preferred securities with a fair value of $3,155,000 and unrealized losses of $4,603,000 in a continuous unrealized loss position for twelve months or more. These unrealized losses were primarily due to the long-term nature of the trust preferred securities, a lack of demand or inactive market for these securities, and concerns regarding the underlying financial institutions that have issued the trust preferred securities. The Company recorded a total of $1,812,000 of OTTI for these securities during 2009. This loss established a new, lower amortized cost basis for these securities and reduced non-interest income as of December 31, 2009. Because the Company does not intend to sell these securities and it is not more-likely-than-not that the Company will be required to sell these securities before recovery of their new, lower amortized cost basis, which may be maturity, the Company does not consider the remainder of the investment in these securities to be other-than-temporarily impaired at December 31, 2009. However, future downgrades or additional deferrals and defaults in these securities, in particular PreTSL XXVIII, could result in additional OTTI and consequently, have a material impact on future earnings.

Following are the details for each trust preferred security (in thousands):

	Book Value	Market Value	Unrealized Loss	Other-than-temporary Impairment Recorded
PreTSL I	$1,230	$949	$(281)	$220
PreTSL II	1,547	1,088	(459)	1,532
PreTSL VI	281	188	(93)	44
PreTSL XXVIII	4,700	930	(3,770)	16
Total	$7,758	$3,155	$(4,603)	$1,812

Other securities

At December 31, 2009, there was one corporate bond with a fair value of $15,000 and unrealized losses of $20,000 in a continuous unrealized loss position for twelve months or more. The long-term nature of this security has led to increased supply, while demand has decreased, leading to devaluation of the security. Management has evaluated this security and believes the decline in market value is liquidity, and not credit, related. Because the Company does not intend to sell this security and it is not more-likely-than-not the Company will be required to sell this security before recovery of its amortized cost basis, which may be maturity, the Company does not consider it to be other than temporarily impaired at December 31, 2009.

The Company does not believe any other individual unrealized loss as of December 31, 2009 represents OTTI. However, given the continued disruption in the financial markets, the Company may be required to recognize OTTI losses in future periods with respect to its available for sale investment securities portfolio. The amount and timing of any additional OTTI will depend on the decline in the underlying cash flows of the securities. Should the impairment of any of these securities become other-than-temporary, the cost basis of the investment will be reduced and the resulting loss recognized in the period the other-than-temporary impairment is identified.

Other-than-temporary Impairment

Upon acquisition of a security, the Company decides whether it is within the scope of the accounting guidance for beneficial interests in securitized financial assets or will be evaluated for impairment under the accounting guidance for investments in debt and equity securities.

The accounting guidance for beneficial interests in securitized financial assets provides incremental impairment guidance for a subset of the debt securities within the scope of the guidance for investments in debt and equity securities. For securities where the security is a beneficial interest in securitized financial assets, the Company uses the beneficial interests in securitized financial asset impairment model. For securities where the security is not a beneficial interest in securitized financial assets, the Company uses debt and equity securities impairment model.

The Company routinely conducts periodic reviews to identify and evaluate each investment security to determine whether OTTI has occurred. Economic models are used to determine whether OTTI has occurred on these securities. While all securities are considered, the securities primarily impacted by OTTI testing are pooled trust preferred securities. For each pooled trust preferred security in the investment portfolio (including but not limited to those whose fair value is less than their amortized cost basis), an extensive, regular review is conducted to determine if OTTI has occurred. Various inputs to the economic models are sued to determine if an unrealized loss is other-than-temporary. The most significant inputs are the following:

- Prepayments
- Defaults
- Loss severity

The pooled trust preferred securities relate to trust preferred securities issued by financial institutions. The pools typically consist of financial institutions throughout the United States. Other inputs may include the actual collateral attributes, which include credit ratings and other performance indicators of the underlying financial institutions including profitability, capital ratios, and asset quality.

To determine if the unrealized losses for pooled trust preferred securities is other-than-temporary, the Company projects total estimated defaults of the underlying assets (financial institutions) and multiplies that calculated amount by an estimate of realizable value upon sale in the marketplace (severity) in order to determine the projected collateral loss. The Company also evaluated the current credit enhancement underlying the bond to determine the impact on cash flows. If the Company determines that a given pooled trust preferred security position will be subject to a write-down or loss, the Company records the expected credit loss as a charge to earnings.

For those securities for which OTTI was determined to have occurred as of December 31, 2009 (that is, a determination was made that the entire amortized cost bases will not likely be recovered), the following assumptions were used to measure the amount of credit loss recognized in earnings. The Company's assumptions for the pooled trust preferred securities included default rates of 2% for the first two quarters of 2010, 1% for the third and fourth quarters of 2010 and the first quarter of 2011 and .375% for all quarters remaining over the life of the securities, a 15% recovery with a 2 year lag, and no prepayments.

Credit Losses Recognized on Investments

During 2009, the Company adopted the revisions to ASC 820, formerly FASB Staff Position ("FSP") 157-4, "Determining Fair Value when the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions that are Not Orderly " and FSP 157-3, "Determining the Fair Value of a Financial Asset When the market for That Asset is Not Active" and ASC 320, formerly FSP 115-2 and FAS 124-2, "Recognition and Presentation of Other-Than-Temporary Impairments." The effect of the adoption of these new standards for 2009 was an increase in net income of approximately $4.6 million before taxes or approximately $3 million after taxes.

As described above, some of the Company's investments in trust preferred securities have experienced fair value deterioration due to credit losses but are not otherwise other-than-temporarily impaired. The following table provides information about those trust preferred securities for which only a credit loss was recognized in income and other losses are recorded in other comprehensive income (loss) for the year ended December 31, 2009 (in thousands). There were no credit losses recorded in income for the years ended December 31, 2008 or 2007.

	Accumulated Credit Losses December 31, 2009
Credit losses on trust preferred securities held	
Beginning of year	$ -
Additions related to OTTI losses not previously recognized	1,812
Reductions due to sales	-
Reductions due to change in intent or likelihood of sale	-
Additions related to increases in previously recognized OTTI losses	-
Reductions due to increases in expected cash flows	-
End of year	$ 1,812

Maturities of investment securities were as follows at December 31, 2009 (in thousands). Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Estimated Fair Value
Available-for-sale:		
Due in one year or less	$54,533	$54,492
Due after one-five years	45,729	42,583
Due after five-ten years	26,008	26,767
Due after ten years	365	336
	126,635	124,178
Mortgage-backed securities	111,301	114,519
Total available-for-sale	$237,936	$238,697
Held-to-maturity:		
Due in one year or less	$408	$414
Due after one-five years	51	55
Due after five-ten years	-	-
Due after ten-years	-	-
Total held-to-maturity	$459	$469
Total investment securities	$238,395	$239,166

Note 5 – Loans

A summary of loans at December 31, 2009 and 2008 follows (in thousands):

	2009	2008
Construction and land development	$28,041	$40,362
Farm loans	62,330	65,647
1-4 Family residential properties	180,415	200,204
Multifamily residential properties	19,467	23,833
Commercial real estate	226,400	217,307
Loans secured by real estate	516,653	547,353
Agricultural loans	54,144	54,098
Commercial and industrial loans	105,351	109,324
Consumer loans	20,815	25,806
All other loans	3,787	5,357
Total loans	$700,750	$741,938

The real estate mortgage loan balance in the above table includes loans held for sale of $149,000 and $537,000 at December 31, 2009 and 2008, respectively.

The aggregate principal balances of nonaccrual, past due ninety days or more and renegotiated loans were $12,720,000 and $7,285,000 at December 31, 2009 and 2008, respectively. Interest income which would have been recorded under the original terms of such nonaccrual or renegotiated loans totaled $672,000, $274,000 and $426,000 in 2009, 2008 and 2007, respectively.

Impaired loans are defined as those loans where it is probable that amounts due according to contractual terms, including principal and interest, will not be collected. Both nonaccrual and restructured loans meet this definition. The Company evaluates all individual loans on nonaccrual or restructured with a balance over $100,000 for impairment. Impaired loans are measured by the Company at the present value of expected future cash flows or, alternatively, if the loan is collateral dependant, at the fair value of the collateral. Known losses of principal on these loans have been charged off. Interest income on nonaccrual loans is recognized only at the time cash is received. Interest income on restructured loans is recorded according to the most recently agreed upon contractual terms.

The following table presents information on impaired loans at December 31, 2009 and 2008:

	2009	2008
Impaired loans for which a specific allowance has been provided	$5,131	$696
Impaired loans for which no specific allowance has been provided	7,589	6,589
Total loans determined to be impaired	$12,720	$7,285
Allowance on impaired loans	$563	$160

	For the year ended December 31,	
	2009	2008
Average recorded investment in impaired loans	$9,912	$7,326
Cash basis interest income recognized from impaired loans	473	352

Most of the Company's business activities are with customers located within east central Illinois. At December 31, 2009, the Company's loan portfolio included $116.5 million of loans to borrowers whose businesses are directly related to agriculture. Of this amount, $102.5 million was concentrated in other grain farming. Total loans to borrowers whose businesses are directly related to agriculture decreased $3.2 million from $119.7 million at December 31, 2008 while loans concentrated in other grain farming increased $6 million from $113.7 million at December 31, 2008. While the Company adheres to sound underwriting practices, including collateralization of loans, any extended period of low commodity prices, significantly reduced yields on crops and/or reduced levels of government assistance to the agricultural industry could result in an increase in the level of problem agriculture loans and potentially result in loan losses within the agricultural portfolio.

In addition, the Company has $50.8 million of loans to motels and hotels. The performance of these loans is dependent on borrower specific issues as well as the general level of business and personal travel within the region. While the Company adheres to sound underwriting standards, a prolonged period of reduced business or personal travel could result in an increase in nonperforming loans to this business segment and potentially in loan losses. The Company also has $72.0 million of loans to lessors of non-residential buildings and $44.2 million of loans to lessors of residential buildings and dwellings.

Mortgage loans serviced by others for First Mid Bank are not included in the accompanying consolidated balance sheets. The unpaid principal balances of these loans at December 31, 2009 and 2008 were approximately $6,333,000 and $8,495,000, respectively.

Note 6 – Allowance for Loan Losses

Changes in the allowance for loan losses were as follows during the three years ended December 31, 2009, 2008 and 2007:

	2009	2008	2007
Balance, beginning of year	$7,587	$6,118	$5,876
Provision for loan losses	3,594	3,559	862
Recoveries	160	332	243
Charge-offs	(1,879)	(2,422)	(863)
Balance, end of year	$9,462	$7,587	$6,118

Note 7 – Premises and Equipment, Net

Premises and equipment at December 31, 2009 and 2008 consisted of:

	2009	2008
Land	$3,569	$3,524
Buildings and improvements	17,347	16,437
Furniture and equipment	13,223	12,072
Leasehold improvements	1,341	1,295
Construction in progress	-	450
Subtotal	35,480	33,778
Accumulated depreciation and amortization	19,993	18,793
Total	$15,487	$14,985

Construction in progress balances as of December 31, 2008, consisted primarily of expenditures related to the construction of a new facility in Arcola, Illinois completed during 2009. Depreciation and amortization expense was $1,538,000, $1,617,000 and $1,629,000 for the years ended December 31, 2009, 2008 and 2007, respectively.

Note 8 – Goodwill and Intangible Assets

The Company has goodwill from business combinations, intangible assets from branch acquisitions, identifiable intangible assets assigned to core deposit relationships and customer lists of insurance agencies acquired, and intangible assets arising from the rights to service mortgage loans for others. The following table presents gross carrying amount and accumulated amortization by major intangible asset class as of December 31, 2009 and 2008:

	2009		2008	
	Gross Carrying Value	Accumulated Amortization	Gross Carrying Value	Accumulated Amortization
Goodwill not subject to amortization	$21,123	$ 3,760	$21,123	$ 3,760
Intangibles from branch acquisition	3,015	2,563	3,015	2,362
Core deposit intangibles	5,936	3,953	5,936	3,614
Customer list intangibles	1,904	1,507	1,904	1,317
	$31,978	$ 11,783	$31,978	$ 11,053

Total amortization expense for the years ended December 31, 2009, 2008 and 2007 was as follows:

	2009	2008	2007
Intangibles from branch acquisitions	$201	$201	$200
Core deposit intangibles	339	374	431
Customer list intangibles	190	191	190
	$730	$766	$821

Estimated amortization expense for each of the five succeeding years is shown in the table below:

Estimated amortization expense:	
For period ended 12/31/10	$704
For period ended 12/31/11	$704
For period ended 12/31/12	$380
For period ended 12/31/13	$313
For period ended 12/31/14	$313

In accordance with the provisions of SFAS 142,"Goodwill and Other Intangible Assets," codified in ASC 350, the Company performed testing of goodwill for impairment as of September 30, 2009 and 2008, and determined, as of each of these dates, that goodwill was not impaired. Management also concluded that the remaining amounts and amortization periods were appropriate for all intangible assets.

Note 10 – Deposits

As of December 31, 2009 and 2008, deposits consisted of the following:

	2009	2008
Demand deposits:		

Non-interest bearing	$128,726	$119,986
Interest-bearing	169,480	152,340
Savings	131,941	88,502
Money market	184,224	121,809
Time deposits	226,039	323,717
Total deposits	$840,410	$806,354

Total interest expense on deposits for the years ended December 31, 2009, 2008 and 2007 was as follows:

	2009	2008	2007
Interest-bearing demand	$539	$1,100	$1,872
Savings	882	618	291
Money market	2,304	2,535	4,587
Time deposits	9,245	12,339	14,841
Total	$12,970	$16,592	$21,591

As of December 31, 2009, 2008 and 2007, the aggregate amount of time deposits in denominations of more than $100,000 and the total interest expense on such deposits was as follows:

	2009	2008	2007
Outstanding	$81,692	$129,397	$98,052
Interest expense for the year	3,857	4,416	4,652

The following table shows the amount of maturities for all time deposits as of December 31, 2009:

Less than 1 year	$179,548
1 year to 2 years	18,333
2 years to 3 years	10,767
3 years to 4 years	9,563
4 years to 5 years	7,592
Over 5 years	236
Total	$226,039

In 2009, the Company's significant deposits included brokered CDs and deposit relationships with various public entities. As of December 31, 2009, the Company had three brokered CDs which totaled $15 million. In addition, the Company maintains account relationships with various public entities throughout its market areas. Five public entities had total balances of $25.3 million in various checking accounts and time deposits as of December 31, 2009. These balances are subject to change depending upon the cash flow needs of the public entity.

Note 11 – Borrowings

As of December 31, 2009 and 2008 borrowings consisted of the following:

	2009	2008
Securities sold under agreements to repurchase	$80,386	$80,708
Federal Home Loan Bank advances:		
Fixed-term advances	32,750	37,750
Subordinated debentures	20,620	20,620
Other debt:		
Loans due in one year or less	-	-
Loans due after one year	-	13,000

Total	$133,756	$152,078

Aggregate annual maturities of long-term borrowings at December 31, 2009 are:

2010	$10,000
2011	3,000
2012	14,750
2013	-
2014	-
Thereafter	25,620
	$53,370

FHLB advances represent borrowings by First Mid Bank to economically fund loan demand. The fixed term advances totaling $32.75 million are as follows:

- $5 million advance at 4.58% with a 5-year maturity, due March 22, 2010
- $2.5 million advance at 5.46% with a 3-year maturity, due June 12, 2010
- $2.5 million advance at 5.12% with a 3-year maturity, due June 12, 2010, one year lockout, callable quarterly
- $3 million advance at 5.98% with a 10-year maturity, due March 1, 2011
- $5 million advance at 4.82% with a 5-year maturity, due January 19, 2012, two year lockout, callable quarterly
- $5 million advance at 4.69% with a 5-year maturity, due February 23, 2012, two year lockout, callable quarterly
- $4.75 million advance at 1.60% with a 5-year maturity, due December 24, 2012
- $5 million advance at 4.58% with a 10-year maturity, due July 14, 2016, one year lockout, callable quarterly

	2009	2008	2007
Securities sold under agreements to repurchase:			
Maximum outstanding at any month-end	$83,826	$80,708	$68,300
Average amount outstanding for the year	72,589	61,108	54,962

First Mid Bank has collateral pledge agreements whereby it has agreed to keep on hand at all times, free of all other pledges, liens, and encumbrances, whole first mortgages on improved residential property with unpaid principal balances aggregating no less than 133% of the outstanding advances and letters of credit ($0 on December 31, 2009) from the FHLB. The securities underlying the repurchase agreements are under the Company's control.

At December 31, 2009 and 2008, outstanding loan balances included $0 and $13 million, respectively, on a revolving credit agreement with The Northern Trust Company. This loan was renegotiated on April 24, 2009. The revolving credit agreement has a maximum available balance of $20 million with a term of one year from the date of closing. The interest rate (2.3% at December 31, 2009) is floating at 2.25% over the federal funds rate. The loan is unsecured and subject to a borrowing agreement containing requirements for the Company and First Mid Bank to maintain various operating and capital ratios. The Company was in compliance with all of the existing covenants at December 31, 2009 except the Company's return on assets ratio was .74% as of December 31, 2009 which was below the covenant ratio required of .75%. The Company has received a waiver from Northern Trust Company for this covenant as of December 31, 2009. The Company and First Mid Bank were in compliance with the existing covenants at December 31, 2008 and 2007.

On February 27, 2004, the Company completed the issuance and sale of $10 million of floating rate trust preferred securities through Trust I, a statutory business trust and wholly-owned unconsolidated subsidiary of the Company, as part of a pooled offering. The Company established Trust I for the purpose of issuing the trust preferred securities. The $10 million in proceeds from the trust preferred issuance and an additional $310,000 for the Company's investment in common equity of the Trust, a total of $10,310 000, was invested in junior subordinated debentures of the Company. The underlying junior subordinated debentures issued by the Company to Trust I mature in 2034, bear interest at three-month London Interbank Offered Rate ("LIBOR") plus 280 basis points, reset quarterly, and are callable, at the option of the Company, at par on or after April 7, 2009. At December 31, 2009 and 2008 the rate was 3.10% and 6.56%, respectively. The Company used the proceeds of the offering for general corporate purposes.

On April 26, 2006, the Company completed the issuance and sale of $10 million of fixed/floating rate trust preferred securities through Trust II, a statutory business trust and wholly-owned unconsolidated subsidiary of the Company, as part of a pooled offering. The Company established Trust II for the purpose of issuing the trust preferred securities. The $10 million in proceeds from the trust preferred issuance and an additional $310,000 for the Company's investment in common equity of Trust II, a total of $10,310 000, was invested in junior subordinated debentures of the Company. The underlying junior subordinated debentures issued by the Company to Trust II mature in 2036, bear interest at a fixed rate of 6.98% (three-month LIBOR plus 160 basis points) paid quarterly and convert to floating rate (LIBOR plus 160 basis points) after June 15, 2011. The net proceeds to the Company were used for general corporate purposes, including the Company's acquisition of Mansfield.

The trust preferred securities issued by Trust I and Trust II are included as Tier 1 capital of the Company for regulatory capital purposes. On March 1, 2005, the Federal Reserve Board adopted a final rule that allows the continued limited inclusion of trust preferred securities in the calculation of Tier 1 capital for regulatory purposes. The final rule provided a five-year transition period, ending September 30, 2009, for application of the revised quantitative limits. On March 17, 2009, the Federal Reserve Board adopted an additional final rule that delayed the effective date of the new limits on inclusion of trust preferred securities in the calculation of Tier 1 capital until September 30, 2011. The Company does not expect the application of the revised quantitative limits to have a significant impact on its calculation of Tier 1 capital for regulatory purposes or its classification as well-capitalized.

Note 12 – Regulatory Capital

The Company is subject to various regulatory capital requirements administered by the federal banking agencies. Bank holding companies follow minimum regulatory requirements established by the Federal Reserve Board. First Mid Bank follows similar minimum regulatory requirements established for national banks by the OCC. Failure to meet minimum capital requirements can result in the initiation of certain mandatory and possibly additional discretionary action by regulators that, if undertaken, could have a direct material effect on the Company's financial statements.
Quantitative measures established by each regulatory agency to ensure capital adequacy require the reporting institutions to maintain minimum amounts and ratios (set forth in the table below) of total and Tier 1 capital to risk-weighted assets, and of Tier 1 capital to average assets. Management believes, as of December 31, 2009 and 2008, that all capital adequacy requirements have been met.

As of December 31, 2009 and 2008, the most recent notification from the primary regulators categorized First Mid Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratios must be maintained as set forth in the table. At December 31, 2009, there are no conditions or events since the most recent notification that management believes have changed this categorization.

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2009						
Total Capital (to risk-weighted assets)						
Company	$ 123,977	15.76 %	$ 62,949	> 8.00%	N/A	N/A
First Mid Bank	112,982	14.50 %	62,367	> 8.00%	$ 77,958	> 10.00%
Tier 1 Capital (to risk-weighted assets)						
Company	114,635	14.57 %	31,474	> 4.00%	N/A	N/A
First Mid Bank	103,730	13.31 %	31,183	> 4.00%	46,775	> 6.00%
Tier 1 Capital (to average assets)						
Company	114,635	10.63 %	43,150	> 4.00%	N/A	N/A
First Mid Bank	103,730	9.67 %	42,886	> 4.00%	53,607	> 5.00%

December 31, 2008						
Total Capital (to risk-weighted assets)						
Company	$ 93,469	11.99 %	$ 62,364	> 8.00%	N/A	N/A
First Mid Bank	100,531	13.00 %	61,855	> 8.00%	$ 77,319	> 10.00%
Tier 1 Capital (to risk-weighted assets)						
Company	85,882	11.02 %	31,182	> 4.00%	N/A	N/A
First Mid Bank	92,944	12.02 %	30,927	> 4.00%	46,391	> 6.00%
Tier 1 Capital (to average assets)						
Company	85,882	8.41 %	40,845	> 4.00%	N/A	N/A
First Mid Bank	92,844	9.16 %	40,600	> 4.00%	50,750	> 5.00%

Note 13 – Disclosure of Fair Values of Financial Instruments

Effective January 1, 2008, the Company adopted SFAS No. 157, “Fair Value Measurements” which was codified into ASC 820. SFAS No. 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements.

SFAS No. 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. SFAS No. 157 also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

In accordance with SFAS No. 157, the Company groups its financial assets and financial liabilities measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels are:

Level 1	Valuations for assets and liabilities traded in active exchange markets, such as the New York Stock Exchange. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.
Level 2	Valuations for assets and liabilities traded in less active dealer or broker markets. Valuations are obtained from third party pricing services for identical or comparable assets or liabilities which use observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in active markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
Level 3	Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

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

Available-for-Sale Securities

The fair value of available-for-sale securities are determined by various valuation methodologies. Where quoted market prices are available in an active market, securities are classified within Level 1. Level 1 securities include exchange traded equities. If quoted market prices are not available, then fair values are estimated by using pricing models or quoted prices of securities with similar characteristics. Level 2 securities include U.S. Treasury securities, obligations of U.S. government corporations and agencies, obligations of states and political subdivisions, mortgage-backed securities, collateralized mortgage obligations and corporate bonds. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy and include subordinated tranches of collateralized mortgage obligations and investments in trust preferred securities.

The trust preferred securities are collateralized debt obligation securities that are backed by trust preferred securities issued by banks, thrifts, and insurance companies. The market for these securities at December 31, 2009 is not active and markets for similar securities are also not active. The inactivity was evidenced first by a significant widening of the bid-ask spread in the brokered markets in which trust preferred securities trade and then by a significant decrease in the volume of trades relative to historical levels. The new issue market is also inactive as no new trust preferred securities have been issued since 2007. There are currently very few market participants who are willing and or able to transact for these securities. The market values for these securities (and any securities other than those issued or guaranteed by the US Treasury) are very depressed relative to historical levels.

Given conditions in the debt markets today and the absence of observable transactions in the secondary and new issue markets, we determined:

- The few observable transactions and market quotations that are available are not reliable for purposes of determining fair value at December 31, 2009,
- An income valuation approach technique (present value technique) that maximizes the use of relevant observable inputs and minimizes the use of unobservable inputs will be equally or more representative of fair value than the market approach valuation technique used at prior measurement dates , and

- The Company's trust preferred securities will be classified within Level 3 of the fair value hierarchy because we determined that significant adjustments are required to determine fair value at the measurement date.

The following table presents the Company's assets that are measured at fair value on a recurring basis and the level within the FAS 157 hierarchy in which the fair value measurements fall as of December 31, 2009 and 2008 (in thousands):

		Fair Value Measurements Using		
December 31, 2009	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Available-for-sale securities:				
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$90,974	$-	$ 90,974	$ -
Obligations of states and political subdivisions	23,716	-	23,716	-
Mortgage-backed securities	114,519	-	114,444	75
Trust preferred securities	3,155	-	-	3,155
Other securities	6,333	15	6,318	-
Total available-for-sale securities	$238,697	$15	$ 235,452	$ 3,230

		Fair Value Measurements Using		
December 31, 2008	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Available-for-sale securities:				
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$74,632	$-	$ 74,632	$ -
Obligations of states and political subdivisions	20,922	-	20,922	-
Mortgage-backed securities	62,802	-	62,721	81
Trust preferred securities	5,378	-	-	5,378
Other securities	5,742	7	5,735	-
Total available-for-sale securities	$169,476	$7	$ 164,010	$ 5,459

The change in fair value of assets measured on a recurring basis using significant unobservable inputs (Level 3) for the year ended December 31, 2009 and 2008 is summarized as follows (in thousands):

	Available-for-Sale Securities		
December 31, 2009	Mortgaged-backed Securities	Trust Preferred Securities	Total
Beginning balance	$81	$5,378	$5,459
Transfers into Level 3	-	-	-
Transfers out of Level 3	-	-	-
Total gains or losses			
Included in net income	-	(1,812)	(1,812)
Included in other comprehensive income (loss)	2	(653)	(651)
Purchases, issuances, sales and settlements			
Purchases	-	-	-
Issuances	-	-	-
Sales	-	-	-
Settlements	(8)	242	234
Ending balance	$75	$3,155	$3,230
Total gains or losses for the period included in net income attributable to the change in unrealized gains or losses related to assets and liabilities still held at the reporting date	$-	$(1,812)	$(1,812)
December 31, 2008			
Beginning balance	$91	$9,400	$9,491
Transfers into Level 3	-	-	-
Transfers out of Level 3	-	-	-
Total gains or losses			
Included in net income	-	-	-
Included in other comprehensive income (loss)	184	(3,950)	(3,766)
Purchases, issuances, sales and settlements			

Purchases	-	-	-
Issuances	-	-	-
Sales	-	-	-
Settlements	(194)	(72)	(266)
Ending balance	$81	$5,378	$5,459
Total gains or losses for the period included in net income attributable to the change in unrealized gains or losses related to assets and liabilities still held at the reporting date	$-	$-	$-

Following is a description of the valuation methodologies used for assets measured at fair value on a nonrecurring basis and recognized in the accompanying balance sheets, as well as the general classification of such assets pursuant to the valuation hierarchy.

Impaired Loans (Collateral Dependent)

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

If the impaired loan is identified as collateral dependent, then the fair value method of measuring the amount of impairment is utilized. This method requires obtaining a current independent appraisal of the collateral and applying a discount factor to the value. Impaired loans that are collateral dependent are classified within Level 3 of the fair value hierarchy when impairment is determined using the fair value method.

Management establishes a specific reserve for loans that have an estimated fair value that is below the carrying value. The total carrying amount of loans for which a specific reserve has been established as of December 31, 2009 was $5,631,000 and a fair value of $5,068,000 resulting in specific loss exposures of $563,000.

When there is little prospect of collecting either principal or interest, loans, or portions of loans, may be charged-off to the allowance for loan losses. Losses are recognized in the period an obligation becomes uncollectible. The recognition of a loss does not mean that the loan has absolutely no recovery or salvage value, but rather that it is not practical or desirable to defer writing off the loan even though partial recovery may be effected in the future.

Foreclosed Assets Held For Sale

Other real estate owned acquired through loan foreclosure are initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. The adjustment at the time of foreclosure is recorded through the allowance for loan losses. Due to the subjective nature of establishing the fair value when the asset is acquired, the actual fair value of the other real estate owned or foreclosed asset could differ from the original estimate. If it is determined that fair value declines subsequent to foreclosure, a valuation allowance is recorded through noninterest expense. Operating costs associated with the assets after acquisition are also recorded as noninterest expense. Gains and losses on the disposition of other real estate owned and foreclosed assets are netted and posted to other noninterest expense. The total carrying amount of other real estate owned as of December 31, 2009 was $2,862,000. Other real estate owned measured at fair value on a nonrecurring basis in 2009 amounted to $1,020,000.

The following table presents the fair value measurement of assets measured at fair value on a nonrecurring basis and the level within the SFAS No. 157 fair value hierarchy in which the fair value measurements fall at December 31, 2009 and 2008 (in thousands):

		Fair Value Measurements Using		
December 31, 2009	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans (collateral dependent)	$5,068	$-	$ -	$ 5,068

Foreclosed assets held for sale	1,020	-	-	1,020

		Fair Value Measurements Using		
December 31, 2008	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans (collateral dependent)	$1,584	$-	$ -	$ 1,584

Other

The following methods were used to estimate the fair value of all other financial instruments recognized in the accompanying balance sheets at amounts other than fair value.

Cash and cash equivalents and Federal Reserve and Federal Home Loan Bank Stock

The carrying amount approximates fair value.

Held-to-maturity Securities

Fair value is based on quoted market prices, if available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

Loans

For loans with floating interest rates, it is assumed that the estimated fair values generally approximate the carrying amount balances. Fixed rate loans have been valued using a discounted present value of projected cash flow. The discount rate used in these calculations is the current rate at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. The carrying amount of accrued interest approximates it fair value.

Deposits

Deposits include demand deposits, savings accounts, NOW accounts and certain money market deposits. The carrying amount of these deposits approximates fair value. The fair value of fixed-maturity time deposits is estimated using a discounted cash flow calculation that applies the rates currently offered for deposits of similar remaining maturities.

Short-term Borrowings and Interest Payable

The carrying amount approximates fair value.

Long-term Debt and Federal Home Loan Bank Advances

Rates currently available to the Company for debt with similar terms and remaining maturities are used to estimate the fair value of existing debt.

The following table presents estimated fair values of the Company's financial instruments in accordance with FAS 107-1 and APB 28-1, codified with ASC 805.

	December 31, 2009		December 31, 2008	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial Assets				
Cash and cash equivalents	$39,755	$39,787	$48,343	$48,343
Federal funds sold	60,000	60,000	38,300	38,300
Available-for-sale securities	238,697	238,697	169,476	169,476
Held-to-maturity securities	459	469	599	610
Loans held for sale	149	149	537	537
Loans net of allowance for loan losses	691,139	698,798	733,814	752,735
Interest receivable	6,871	6,871	7,161	7,161
Federal Reserve Bank stock	1,368	1,368	1,366	1,366
Federal Home Loan Bank stock	3,727	3,727	3,727	3,727
Financial Liabilities				
Deposits	$840,410	$841,737	$806,354	$811,284
Securities sold under agreements to repurchase	80,386	80,389	80,708	80,720
Interest payable	861	861	1,616	1,616
Federal Home Loan Bank borrowings	32,750	34,448	37,750	40,763

Other borrowings	-	-	13,000	13,000
Junior subordinated debentures	20,620	20,620	20,620	20,620

Note 14—Deferred Compensation Plan

The Company follows the provisions of the EITF 97-14, which was codified into ASC 710, for purposes of the First Mid-Illinois Bancshares, Inc. Deferred Compensation Plan (“DCP”). At December 31, 2009, the Company classified the cost basis of its common stock issued and held in trust in connection with the DCP of approximately $2,894,000 as treasury stock. The Company also classified the cost basis of its related deferred compensation obligation of approximately $2,894,000 as an equity instrument (deferred compensation).

The DCP was effective as of June 1984. The purpose of the DCP is to enable directors, advisory directors, and key employees the opportunity to defer a portion of the fees and cash compensation paid by the Company as a means of maximizing the effectiveness and flexibility of compensation arrangements. The Company invests all participants' deferrals in shares of common stock. Dividends paid on the shares are credited to participants' DCP accounts and invested in additional shares. During 2009 and 2008 the Company issued 9,916 common shares and 7,600 common shares, respectively, pursuant to the DCP.

Note 15 – Stock Option Plan

At the Annual Meeting of Stockholders held May 23, 2007, the stockholders approved the First Mid-Illinois Bancshares, Inc. 2007 Stock Incentive Plan ("SI Plan"). The SI Plan was implemented to succeed the Company's 1997 Stock Incentive Plan, which had a ten-year term that expired October 21, 2007, under which there are still options outstanding. The SI Plan is intended to provide a means whereby directors, employees, consultants and advisors of the Company and its Subsidiaries may sustain a sense of proprietorship and personal involvement in the continued development and financial success of the Company and its Subsidiaries, thereby advancing the interests of the Company and its stockholders. Accordingly, directors and selected employees, consultants and advisors may be provided the opportunity to acquire shares of Common Stock of the Company on the terms and conditions established in the SI Plan.

A maximum of 300,000 shares are authorized under the SI Plan. This amount reflects the Company's stock split which occurred on June 29, 2007. Options to acquire shares are awarded at an exercise price equal to the fair market value of the shares on the date of grant and have a 10-year term. Options granted to employees vest over a four-year period and options granted to directors vest at the time they are issued.

The fair value of options granted is estimated on the grant date using the Black-Scholes option-pricing model. There were no options granted during 2009. The following assumptions were used in estimating the fair value for options granted in 2008 and 2007. Expected volatility is based on historical volatility of the Company's stock and other factors. The Company uses historical data to estimate option exercise and employee termination within the valuation model; separate groups of employees who have similar historical exercise behavior are considered separately for valuation purposes. The expected term of options granted is derived from the output of the option valuation model and represents the period of time that options granted are expected to be outstanding. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of the grant.

	2008		2007	
Average expected volatility	13.4	%	13.2	%
Average expected dividend yield	1.6	%	1.4	%
Average expected term	5.9 yrs		5.7 yrs	
Average risk-free interest rate	1.3	%	3.4	%

The total compensation cost recognized in the income statement for 2009 was $53,000 with a related tax benefit of $2,000. The total compensation cost recognized in the income statement for 2008 was $58,000 with a related tax benefit of $1,000. The total compensation cost recognized in the income statement for 2007 was $61,000 with a related tax benefit of $3,000.

A summary of option activity under the SI Plan and the 1997 Stock Incentive Plan as of December 31, 2009, 2008 and 2007, and changes during the years then ended is presented below:

	2009			
			Weighted-Average	
		Weighted-Average	Remaining	Aggregate
			Contractual	Intrinsic
	Shares	Exercise Price	Term	Value
Outstanding, beginning of year	352,425	$ 19.73		
Granted	-	-		
Exercised	(37,267)	10.42		
Forfeited or expired	(26,125)	24.08		