FIRST MID ILLINOIS BANCSHARES INC
Form 10-K
March 04, 2016

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, 2015
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.)
1421 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:
Common stock, par value $4.00 per share
(Title of class)

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

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 whether the Registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes [X] No [ ]

Indicate by check mark 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 amendments to this Form Yes [X]

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 [ ]	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 $107,610,277. 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 4, 2016, 8,456,302 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 2016 Annual Meeting of Shareholders to be held on April 27, 2016	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. doing business as First Mid Insurance Group (“First Mid Insurance”). 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
- Peoples State Bank of Mansfield on May 1, 2006

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 (2000); de novo branches in Champaign, Illinois and Maryville, Illinois (2002), a de novo branch in Highland, Illinois (2005) de novo branches in Decatur, Illinois and Champaign, Illinois (2009), and a de novo branch in Decatur, Illinois (2013).

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

On September 10, 2010, First Mid Bank acquired 10 Illinois branches (the “Branches”) from First Bank, a Missouri state chartered bank, located in Bartonville, Bloomington, Galesburg, Knoxville, Peoria and Quincy, Illinois.

On August 14, 2015 First Mid Bank acquired 12 Illinois branch offices (the "ONB Branches") of Old National Bank in Southern Illinois, a national banking association having its principal office in Evansville, Indiana, located in Lawrenceville, Mt Carmel, Mt Vernon, Carmi, De Soto, Murphysboro, Marion, Harrisburg, Carterville and Carbondale, Illinois.

On December 1, 2015 FIrst Mid Insurance acquired Illiana Insurance Agency, LTD ("Illiana"), an insurance agency based in Philo, Illinois.

Employees

The Company, MIDS, First Mid Insurance and First Mid Bank, collectively, employed 513 people on a full-time equivalent basis as of December 31, 2015. 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 experience, 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 First Mid Insurance. Of these, the community banking line contributes approximately 91% 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, health, life 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

Mission Statement. The Company's mission statement is to fulfill the financial needs of our communities with exceptional personal service, professionalism and integrity, and deliver meaningful value and results for customers and shareholders.
Achieve 2020. Achieve 2020 is a strategic plan that was developed in 2015. This multi-year strategic plan has broad-based initiatives designed to ensure the Company performs at a level with the highest performing community banks in the Midwest and to increase value for its shareholders, customers and employees in the future. The strategic plan was developed by executive management of the Company, modified and adopted by the Board of Directors and communicated to employees. The Achieve 2020 plan was not undertaken as a result of any weaknesses or deficiencies identified during the Company's control assessments but rather as part of the Company's effort to continually assess and improve. Achieve 2020 is comprised of broad strategies that impact growth, customers, employees, and operations and infrastructure, shareholders and risk management. Following is a description of these strategies.
Growth Strategy. The Company believes that growth of revenues and its customer base is vital to the goal of increasing the value of its shareholders' investment. The Company strives to create shareholder value by maintaining a strong balance sheet and increasing profits. 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 strategic 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 attempt to match products and services with the particular financial needs of individual customers and prospective customers. Many senior officers of the organization are required to attend monthly 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 and measured between the business lines and is facilitated by an on-line application.

Within the community banking line, the Company has focused on growing business operating and real estate loans. Total commercial real estate loans have increased from $321 million at December 31, 2011 to $409 million at December 31, 2015. Approximately 62% of the Company's total revenues were derived from lending activities in the fiscal year ended December 31, 2015. The Company has also focused on growing its 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, and investment services for individuals and

employee benefit services for businesses. The insurance brokerage line has focused on increasing property and casualty and group medical insurance for businesses and personal lines insurance to individuals.

Growth through 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 building shareholder value. Most past acquisitions have been cash-based transactions. The Company would also consider a stock-based acquisition if the strategic and financial metrics were compelling.

Customer Strategy. The Company uses its market and customer knowledge to build relationships that provide high-value customer experiences that continually improve customer satisfaction and loyalty.

Employee Strategy. The Company strives for employee engagement at all levels of the organization. The judgments, experiences and capabilities of these employees are used to create an environment where meeting the needs of our customer, communities and stockholders is always a priority.

Strategy for Operations & Infrastructure. Operationally, the Company centralizes most administrative and operational tasks within its home office 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 practicable, and allows for better management of risk inherent in the business. The Company also utilizes technology where practicable in daily banking activities to reduce the potential for human error. While the Company does not employ every new technology that is introduced, it attempts to be competitive with other banking organizations with respect to operational and customer technology.

Shareholder Strategy. The Company strives to provide a competitive dividend as well as the opportunity for stock price appreciation.

Risk Management Strategy. The Company maintains a comprehensive risk management framework. The Company has initiated an Enterprise Risk Management ("ERM") process whereby management assesses the relevant risks inherent in the business, determines internal controls and procedures are in place to address the various risks, develops a structure for monitoring and reporting risk indicators and trends over time, and incorporates action plans to manage risk positions. The ERM process was not undertaken as a result of any weaknesses or deficiencies identified during the Company's control assessments but rather is part of the Company's effort to continually assess and improve by taking a more holistic approach to risk management. The Company's Chief Risk Management Officer is responsible for facilitating the ERM process. The Company utilizes a comprehensive set of operational policies and procedures that have been developed over time. These policies are continually reviewed by management, the Chief Risk Management Officer, and the Board of Directors. The Company's internal audit function completes procedures to ensure compliance with these policies. While there are several risks that pertain to the business of banking, three risks that are inherent with most banking companies are credit risk, interest rate risk, and liquidity risk.

In the business of banking, credit risk is an important risk as losses from uncollectible loans can diminish capital, earnings and shareholder value. In order to address this risk, the lending function of First Mid Bank receives significant oversight 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 $4 million and up to $15 million. The full Board of Directors must approve all underwriting decisions in excess of $15 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 $1.4 million (0.15% of total loans) over the past five years. Nonperforming loans were $4.0 million (0.31% of total loans) at December 31, 2015. 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 banking business. The Company's Asset Liability Management Committee, consisting of experienced individuals, from various departments, 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 for evaluating these risks. 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 2015, the Company's net interest margin decreased to 3.27% from 3.43% in 2014 primarily due to the additional cash received from the ONB acquisition that increased lower yielding interest-bearing balances at banks.

Markets and Competition

The Company has active competition in all areas in which First Mid Bank 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, on-line services and pricing of services, including interest rates paid on deposits, interest rates charged on loans, and fees charged for fiduciary and other banking services.

During 2015, First Mid Bank operated facilities in the Illinois counties of Adams, Champaign, Christian, Coles, Cumberland, Dewitt, Douglas, Effingham, Jackson, Jefferson, Knox, Lawrence, Macon, Madison, Moultrie, Peoria, Piatt, Saline, Wabash, White and Williamson. Each facility primarily serves the community in which it is located. First Mid Bank served thirty-three different communities with forty-six separate locations in 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.

Rights Agreement

On January 21, 2015, the Company entered into an Amendment No. 1 to the Rights Agreement (the "Rights Agreement"), dated as of September 22, 2009, by and between the Company and Computershare Trust Company, N.A., as rights agent. This amendment accelerated the expiration of the Company's common stock purchase rights (the “Rights”) from 5:00 p.m., Mattoon, Illinois time, on September 22, 2019, to 5:00 p.m., Mattoon, Illinois time, on January 21, 2015, and had the effect of terminating the Rights Agreement on that date. At the time of the termination of the Rights Agreement, all of the Rights distributed to holders of the Company's common stock pursuant to the Rights Agreement expired.

Branch Purchase and Assumption

On January 30, 2015, First Mid Bank, a wholly-owned subsidiary of the Company, entered into a Purchase and Assumption Agreement (the “Purchase Agreement”) with Old National Bank, a national banking association having its principal office in Evansville, Indiana, pursuant to which First Mid Bank purchased certain assets and assume certain liabilities of 12 branch offices of Old National Bank in Southern Illinois (the “ONB Branches”). Pursuant to the terms of the Purchase Agreement, First Mid Bank agreed to assume certain deposit liabilities and to acquire certain loans, as well as cash, real property, furniture, and other fixed operating assets associated with the ONB Branches. The book value of loan and deposit balances assumed was approximately $156 million and $453 million, respectively. First Mid Bank also agreed to assume certain leases, and entered into certain subleases, relating to the ONB Branches. The completion of the Purchase was subject to regulatory approval required by the Office of the Comptroller of the Currency and normal customary closing conditions, including First Mid Bank, in conjunction with the Company, obtaining financing in connection with the acquisition. Following satisfaction of these conditions, First Mid Bank and Old National Bank closed the acquisition on August 14, 2015.

Capital Raise

On June 18, 2015, the Company entered into a securities purchase agreement with a limited number of institutional investors to sell, and accepted from certain other accredited investors, including certain directors of the Company, subscriptions for, an aggregate total of 1,392,859 newly issued shares of the Company's common stock at a purchase price of $21.00 per share, for an aggregate gross purchase price of approximately $29,250,039 (the "Offering"). The Offering closed on June 19, 2015. The Company used the net proceeds of the Offering to provide capital support for the purchase of the ONB Branches and for general corporate purposes.

Acquisition of Illiana

On December 1, 2015, First Mid Insurance Group, a wholly-owned subsidiary of the Company, acquired substantially all of the assets of Illiana, a health plan and life insurance and annuities business.

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 repealed 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 amended the definitions of "broker" and "dealer" under the Securities Exchange Act of 1934, as amended, 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. The GLB Act also amended 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.

Dodd-Frank Wall Street Reform and Consumer Protection Act

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Dodd-Frank Act") was signed into law on July 21, 2010. Generally, the Act is effective the day after it was signed into law, but different effective dates apply to specific sections of the law. The Company will continue to evaluate the affects of these changes. Uncertainty remains as to the ultimate impact of the Act, which could have a material adverse impact either on the financial services industry as a whole, or on the Company's business, results of operations and financial condition. The Act, among other things:

- Resulted in the Federal Reserve issuing rules limiting debit-card interchange fees.

- After a three-year phase-in period which began January 1, 2013, existing trust preferred securities for holding companies with consolidated assets greater than $15 billion and all new issuances of trust preferred securities are removed as a permitted component of a holding company's Tier 1 capital. Trust preferred securities outstanding as of May 19, 2010 that were issued by bank holding companies with total consolidated assets of less than $15 billion, such as First Mid, will continue to count as Tier 1 capital.

- Provides for an increase in the FDIC assessment for depository institutions with assets of $10 billion or more, increases in the minimum reserve ratio for the deposit insurance fund from 1.15% to 1.35% (however, the FDIC is to offset the effect of this increase for holding companies with total consolidated assets of less than $10 billion, such as First Mid) and changes in the basis for determining FDIC premiums from deposits to assets.

- Creates a new Consumer Financial Protection Bureau that will have rulemaking authority for a wide range of consumer protection laws that would apply to all banks and certain non-bank financial institutions and would have broad powers to supervise and enforce consumer protection laws.

- Provides for new disclosure and other requirements relating to executive compensation and corporate governance.

- Changes standards for Federal preemption of state laws related to federally chartered institutions and their subsidiaries.

- Provides mortgage reform provisions including (i) a customer's ability to repay, (ii) restricting variable-rate lending by requiring the ability to repay to be determined for variable-rate loans by requiring lenders to evaluate using the maximum rate that will apply during the first five years of a variable-rate loan term, and (iii) making more loans subject to provisions for higher cost loans and new disclosures.

- Creates a financial stability oversight council that will recommend to the Federal Reserve increasingly strict rules for capital, leverage, liquidity, risk management and other requirements as companies grow in size and complexity.

- Permanently increases the deposit insurance coverage to $250 thousand and allows depository institutions to pay interest on checking accounts.

- Requires publicly-traded bank holding companies with assets of $10 billion or more to establish a risk committee responsible for enterprise-wide risk management practices.

- Limits and regulates, under the provisions of the Act know as the Volker Rule, a financial institution's ability to engage in proprietary trading or to own or invest in certain private equity and hedge funds.

Basel III

In September 2010, the Basel Committee on Banking Supervision proposed higher global minimum capital standards, including a minimum Tier 1 common capital ratio and additional capital and liquidity requirements. On July 2, 2013, the Federal Reserve Board approved a final rule to implement these reforms and changes required by the Dodd-Frank Act. This final rule was subsequently adopted by the OCC and the FDIC.

As included in the proposed rule of June 2012, the final rule included new risk-based capital and leverage ratios, which are being phased in from 2015 to 2019, and refined the definition of what constitutes “capital” for purposes of calculating those ratios. The new minimum capital level requirements applicable to the Company and First Mid Bank beginning in 2015 were: (i) a new common equity Tier 1 capital ratio of 4.5%; (ii) a Tier 1 capital ratio of 6%; (iii) a total capital ratio of 8%; and (iv) a Tier 1 leverage ratio of 4%. The rule also established a “capital conservation buffer” of 2.5% above the new regulatory minimum capital requirements, which must consist entirely of common equity Tier 1 capital and will result in the following minimum ratios: (i) a common equity Tier 1 capital ratio of 7.0%, (ii) a Tier 1 capital ratio of 8.5%, and (iii) a total capital ratio of 10.5%. The new capital conservation buffer requirement will be phased in beginning in January 2016 at 0.625% of risk weighted assets and will increase by that amount each year until fully implemented in January 2019. An institution will be subject to limitations on paying dividends, engaging in share repurchases and paying discretionary bonuses if its capital level falls below the buffer amount.

The final rule also made three changes to the proposed rule of June 2012 that impacted the Company. First, the proposed rule required banking organizations to include accumulated other comprehensive income ("AOCI") in common equity tier 1 capital. AOCI includes accumulated unrealized gains and losses on certain assets and liabilities that have not been included in net income. Under existing general risk-based capital rules, most components of AOCI are not included in a banking organization's regulatory capital calculations. The final rule allowed community banking organizations to make a one-time election not to include these additional components of AOCI in regulatory capital and instead use the existing treatment under the general risk-based capital rules that excludes most AOCI components from regulatory capital. The Company has made this election

Second, the proposed rule modified the risk-weight framework applicable to residential mortgage exposures to require banking organizations to divide residential mortgage exposure into two categories in order to determine the applicable risk weight. The final rule, however, retained the existing treatment for residential mortgage exposures under the general risk-based capital rules.

Third, the proposed rule required banking organizations with total consolidated assets of less than $15 billion as of December 31, 2009, such as the Company, to phase out over ten years any trust preferred securities and cumulative perpetual preferred securities from its Tier 1 capital regulatory capital. The final rule, however, permanently grandfathers into Tier 1 capital of depository institution holding companies with total consolidated assets of less than $15 billion as of December 31, 2009 any trust preferred securities or cumulative perpetual preferred stock issued before May 19, 2010.

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 4%. For purposes of these capital standards, Tier 1 capital consists primarily of permanent stockholders' equity, which includes the Series C Preferred Stock issued by the Company in 2011, 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.

As of December 31, 2015, 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 14.25%, a Tier 1 risk-based ratio of 13.23% and a leverage ratio of 9.20%.

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 Securities Exchange Act of 1934, as amended, 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 Dodd-Frank Act expands the authority of banks to engage in interstate branching. The Dodd-Frank Act allows a state or national bank to open a de novo branch in another state if the law of the state where the branch is to be located would permit a state bank chartered by that state to open the branch.

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 July 21, 2010, The Dodd-Frank Act permanently raised the standard maximum deposit insurance amount from $100,000 to $250,000. On November 9, 2010, the FDIC issued a final rule to implement Section 343 of the Dodd-Frank Act, which provides unlimited deposit insurance coverage for "noninterest-bearing transaction accounts" from December 31, 2010 through December 31, 2012. Also, the FDIC will no longer charge a separate assessment for the insurance of these accounts under the Dodd-Frank Act.

On February 27, 2009, the FDIC adopted a final rule 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 which imposes rates based on an institution's risk to the deposit insurance fund. The

rates increased the range of annual risk based assessment rates from 5 to 7 basis points to 7 to 24 basis points. The final rules both increase base assessment rates and incorporate additional assessments for excess reliance on brokered deposits and FHLB advances. This new assessment took effect April 1, 2009. The Company expensed $809,000, $717,000 and $743,000 for this assessment during 2015, 2014 and 2013, respectively. The increase in this assessment was primarily due to an increase in quarterly average assets.

In addition to its insurance assessment, each insured bank was subject 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 $95,000, $87,000 and $89,000 during 2015, 2014 and 2013, respectively, for this assessment.

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, 2015, 2014, and 2013 First Mid Bank paid supervisory fees to the OCC totaling $352,000, $342,000, and $333,000, respectively.

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 4%, 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, 2015, 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 13.75%, a Tier 1 risk-based ratio of 12.73% and a leverage ratio of 8.83%.

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, 2015. As of December 31, 2015, approximately $35.2 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% of the bank’s capital and surplus and, with all affiliates together, to an aggregate of 20% 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
Joseph R. Dively (56)	Chairman of the Board of Directors, President and Chief Executive Officer
Michael L. Taylor (47)	Senior Executive Vice President and Chief Financial Officer
John W. Hedges (67)	Senior Executive Vice President
Laurel G. Allenbaugh (55)	Executive Vice President
Eric S. McRae (50)	Executive Vice President
Bradley L. Beesley (44)	Executive Vice President
Christopher L. Slabach (53)	Senior Vice President
Clay M. Dean (41)	Senior Vice President
Amanda D. Lewis (36)	Senior Vice President

Joseph R. Dively, age 56, is the Chairman of the Board of Directors, President and Chief Executive Officer of the Company since January 1, 2014 and the President of First Mid Bank since May 2011. Prior to assuming these positions in the Company, he was the Senior Executive Vice President of the Company beginning in May 2011. He was with Consolidated Communications Holdings, Inc. in Mattoon, Illinois from 2003 to May 2011.

Michael L. Taylor, age 47, has been Senior Executive Vice President since 2014 and Chief Financial Officer of the Company since 2000. He served as Executive Vice President from from 2007 to 2014 and as Vice President from 2000 to 2007. He was with AMCORE Bank in Rockford, Illinois from 1996 to 2000.

John W. Hedges, age 67, has been Senior Executive Vice President of the Company and Senior Executive Vice President and Chief Credit Officer of First Mid Bank since May 2011. He served as President of First Mid Bank from September 1999 to May 2011. He was with National City Bank in Decatur, Illinois from 1976 to 1999.

Laurel G. Allenbaugh, age 55, has been Executive Vice President of the Company and Executive Vice President, Chief Operations & IT Officer of First Mid Bank 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.

Eric S. McRae, age 50, has been Executive Vice President of the Company and Executive Vice President, Senior Lender of First Mid Bank since December 2008. He served as President of the Decatur region from 2001 to December 2008.

Bradley L. Beesley, age 44, has been Executive Vice President of the Company and Chief Trust & Wealth Management Officer of First Mid Bank since March 2015. He served as Senior Vice President from May 2007 to March 2015.

Christopher L. Slabach, age 53, has been Senior Vice President of the Company since 2007 and Senior Vice President, Chief Risk Officer of First Mid Bank since 2008. He served as Vice President, Audit of the Company from 1998 to 2007.

Clay M. Dean, age 41, has been Senior Vice President of the Company since 2010 and Senior Vice President and Chief Insurance Services Officer of the First Mid Bank and Chief Executive Officer of First Mid Insurance since

September 2014. He served as Senior Vice President, Chief Deposit Services Officer of First Mid Bank from November 2012 to September 2014 and as Senior Vice President, Director of Treasury Management of First Mid Bank from 2010 to 2012.

Amanda D. Lewis, age 36, has been Senior Vice President of the Company and Senior Vice President, Chief Deposit Services Officer of First Mid Bank since September 2014. She served as Vice President, Director of Marketing from 2001 until September 2014.

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 again 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, 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. Although the housing, capital and credit markets have materially improved since the declines beginning in 2007, future declines could adversely affect the Company's business.

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.

Decline in 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 institutions are interrelated as a result of clearing, counterparty or other relationships. The Company has exposure to different 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 institutions or the financial services industry in general, led to market-wide liquidity problems in recent year 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. As seen starting in the middle of 2007, significant turmoil and volatility in worldwide financial markets can result 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. These types of situations 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. 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 $848 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, 2015. A listing of these industries is contained in under "Item 7. 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.

Deterioration in the real estate market could lead to 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. Increases in commercial and consumer delinquency levels or 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 and capital. 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 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."

A failure in or breach of the company's operational or security systems, or those of it's third party service providers, including as a result of cyber-attacks, could disrupt the company's business, result in unintentional disclosure or misuse of confidential or proprietary information, damage the company's reputation, increase our costs and cause losses. As a financial institution, the company's operations rely heavily on the secure processing, storage and transmission of confidential and other information on it's computer systems and networks. Any failure, interruption or breach in security or operational integrity of these systems could result in failures or disruptions in the company's online banking system, customer relationship management, general ledger, deposit and loan servicing and other systems. The security and integrity of these systems could be threatened by a variety of interruptions or information security breaches, including those caused by computer hacking, cyber-attacks, electronic fraudulent activity or attempted theft of financial assets. Management cannot assert that any such failures, interruption or security breaches will not occur, or if they do occur that they will be adequately addressed. While certain protective policies and procedures are in place, the nature and sophistication of the threats continue to evolve. The Company may be required to expend significant additional resources in the future to modify and enhance these protective measures.

Additionally, the company faces the risk of operational disruption, failure, termination or capacity constraints of any of the third parties that facilitate its business activities, including exchanges, clearing agents, clearing houses or other financial intermediaries. Such parties could also be the source of an attack on, or breach of, its operational systems. Any failures, interruptions or security breaches in the company's information systems could damage its reputation, result in a loss of customer business, result in a violation of privacy or other laws, or expose us to civil litigation, regulatory fines or losses not covered by insurance.

If the Company’s stock price declines from levels at December 31, 2015, 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, 2015. 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 C Preferred Stock impacts net income available to common stockholders and earnings per share. As long as shares of the Series C Preferred Stock is outstanding, no dividends may be paid on the Company’s common stock unless all dividends on the Series C Preferred Stock have been paid in full. The dividends declared on the Series C Preferred Stock reduce the net income available to common stockholders and earnings per share.

Holders of Series C Preferred Stock have rights that are senior to those of common stockholders. The Series C Preferred Stock is senior to the shares of common stock and holders of the Series C Preferred Stock have certain rights and preferences that are senior to holders of common stock. The Series C Preferred Stock will rank senior to the common stock and all other equity securities designated as ranking junior to the Series C Preferred Stock. So long as any shares of the Series C 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 C Preferred Stock for all prior dividend periods. The Series C 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.

If the Company is unable to make favorable acquisitions or successfully integrate our acquisitions, the Company’s growth could be impacted. In the past several years, the Company has completed acquisitions of banks, bank branches and other businesses. We may continue to make such acquisitions in the future. When the Company evaluates acquisition opportunities, the Company evaluates whether the target institution has a culture similar to the Company, experienced management and the potential to improve the financial performance of the Company. If the Company fails to successfully identify, complete and integrate favorable acquisitions, the Company could experience slower growth. Acquiring other banks, bank branches or businesses involves various risks commonly associated with acquisitions, including, among other things: potential exposure to unknown or contingent liabilities or asset quality issues of the target institution, difficulty and expense of integrating the operations and personnel of the target institution, potential disruption to the Company (including diversion of management’s time and attention), difficulty in estimating the value of the target institution, and potential changes in banking or tax laws or regulations that may affect the target institution.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

The Company's headquarters is located at 1421 Charleston Avenue, Mattoon Illinois . This location is also used by the loan and deposit operations departments of First Mid Bank. In addition, the Company owns a facility located at 1500 Wabash Avenue, Mattoon, Illinois, which it is currently leasing to a non-affiliated third party.

The main office of First Mid Bank is located at 1515 Charleston Avenue, Mattoon, Illinois and is owned by First Mid Bank. First Mid Bank also owns a building located at 1520 Charleston Avenue, which is used by First Mid Insurance, MIDS or its data processing and by First Mid Bank for back room operations. First Mid Bank also conducts business through numerous facilities, owned and leased, located in twenty-three counties throughout Illinois. Of the forty-five other banking offices operated by First Mid Bank, twenty-four are owned and twenty-one are leased from non-affiliated third parties.

None of the properties owned by the Corporation are subject to any major encumbrances. The Company believes these facilities are suitable and adequate to operate its banking and related business. The net investment of the Company and subsidiaries in real estate and equipment at December 31, 2015 was $31.3 million.

ITEM 3. LEGAL PROCEEDINGS

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

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 566 shareholders of record as of December 31, 2015 and is included for quotation on the NASDAQ Stock Market, LLC.

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
2015		
4th	$26.50	$21.05
3rd	22.50	21.00
2nd	21.97	19.35
1st	21.10	17.51
2014		
4th	$22.00	$16.90
3rd	22.00	19.05
2nd	23.80	19.05
1st	23.50	21.00

The Board of Directors of the Company declared cash dividends semi-annually during the two years ended December 31, 2015 and 2014. 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
10/27/2015	12/07/2015	$0.29
04/29/2015	06/08/2015	0.30
10/28/2014	12/08/2014	0.29
04/30/2014	06/06/2014	0.26

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 16 – “Dividend Restrictions” herein.

The following table summarizes share repurchase activity for the fourth quarter of 2015:

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, 2015 – October 31, 2015	—	—	—	$7,198,000
November 1, 2015 – November 30, 2015	—	—	—	7,198,000
December 1, 2015 – December 31, 2015	1,101	$22.54	1,101	7,173,000
Total	1,101	$22.54	1,101	$7,173,000

Since August 5, 1998, the Board of Directors has approved repurchase programs pursuant to which the Company may repurchase a total of approximately $76.7 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.
- On February 22, 2011, repurchases of $5 million of additional shares of the Company’s common stock.
- On November 13, 2012 repurchases of $5 million of additional shares of the Company’s common stock.
- On November 19, 2013, repurchases of $5 million additional shares of the Company's common stock.
- On October 28, 2014, repurchases of $5 million 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).

	2015	2014	2013	2012	2011
Summary of Operations					
Interest income	$59,251	$54,734	$53,459	$55,767	$56,772
Interest expense	3,499	3,252	3,535	6,157	8,504
Net interest income	55,752	51,482	49,924	49,610	48,268
Provision for loan losses	1,318	629	2,193	2,647	3,101
Other income	20,544	18,369	19,341	18,310	15,787
Other expense	49,248	44,507	43,504	42,838	43,053
Income before income taxes	25,730	24,715	23,568	22,435	17,901
Income tax expense	9,218	9,254	8,846	8,410	6,529
Net income	16,512	15,461	14,722	14,025	11,372
Dividends on preferred shares	2,200	4,152	4,417	4,252	3,576
Net income available to common stockholders	$14,312	$11,309	$10,305	$9,773	$7,796
Per Common Share Data					
Basic earnings per share	$1.84	$1.88	$1.74	$1.62	$1.29
Diluted earnings per share	1.81	1.85	1.73	1.62	1.29
Dividends declared per share	0.59	0.55	0.46	0.42	0.40
Book value per common share	21.01	19.55	16.54	17.53	16.18
Tangible Book Value per common share	15.09	15.63	11.75	12.68	11.24
Capital Ratios					
Total capital to risk-weighted assets	14.25 %	15.60 %	15.58 %	15.65 %	14.48 %
Tier 1 capital to risk-weighted assets	13.23 %	14.42 %	14.37 %	14.51 %	13.37 %
Common equity tier 1 ratio	9.92 %	10.32 %	7.78 %	7.54 %	7.00 %
Tier 1 capital to average assets	9.20 %	10.52 %	10.12 %	9.66 %	8.99 %
Financial Ratios					
Net interest margin	3.27 %	3.43 %	3.38 %	3.44 %	3.45 %
Return on average assets	0.91 %	0.97 %	0.94 %	0.91 %	0.76 %
Return on average common equity	8.97 %	10.34 %	10.11 %	9.53 %	8.36 %
Dividend on common shares payout ratio	32.07 %	29.26 %	26.44 %	25.93 %	31.01 %
Average equity to average assets	10.34 %	9.94 %	9.81 %	9.76 %	8.88 %
Allowance for loan losses as a percent of total loans	1.14 %	1.29 %	1.35 %	1.29 %	1.29 %
Year End Balances					
Total assets	$2,114,499	$1,607,103	$1,605,498	$1,578,032	$1,500,956
Net loans, including loans held for sale	1,267,313	1,048,724	969,555	899,289	848,954
Total deposits	1,732,568	1,272,077	1,287,616	1,274,065	1,170,734
Total equity	205,009	164,916	149,381	156,687	140,967
Average Balances					
Total assets	$1,807,998	$1,593,227	$1,568,638	$1,543,453	$1,502,794
Net loans, including loans held for sale	1,112,413	1,008,980	912,452	855,335	796,520
Total deposits	1,455,047	1,293,621	1,283,599	1,236,598	1,212,206
Total equity	186,898	158,364	153,922	150,578	133,444

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 years ended December 31, 2015, 2014 and 2013. 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 may contain certain forward-looking statements, 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 1955. 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 could differ materially from the results indicated by these statements because the realization of those results is subject to many risks and uncertainties, including those described in Item 1A. "Risk Factors" and other sections of the Company's Annual Report on Form 10-K and the Company's other filings with the SEC, and 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, the Company's success in raising capital, demand for loan products, deposit flows, competition, demand for financial services in the Company's market area and accounting principles, policies and guidelines. 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, 2015, 2014 and 2013

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 $16.5 million, $15.5 million, and $14.7 million and diluted earnings per share were $1.81, $1.85, and $1.73 for the years ended December 31, 2015, 2014 and 2013, respectively. The increase in net income in 2015 was primarily the result of an increase in net interest income due to growth in loan balances and sustained low funding costs, a reduction in provision for loan losses given lower non-performing assets and net charge-offs, while the decrease in earnings per share was due to the increase in common shares following the capital raise completed in the second quarter of 2015. The following table shows the Company's annualized performance ratios for the years ended December 31, 2015, 2014 and 2013:

	2015		2014		2013	
Return on average assets	0.91	%	0.97	%	0.94	%
Return on average common equity	8.97	%	10.34	%	10.11	%
Average common equity to average assets	10.34	%	9.94	%	9.81	%

Total assets at December 31, 2015, 2014 and 2013 were $2.11 billion, $1.61 billion, and $1.61 billion, respectively. Net loan balances increased to $1.27 billion at December 31, 2015, from $1.05 billion at December 31, 2014, from $970 million at December 31, 2013. Of the increase in 2015, $152 million was due to loans acquired in the Old National Bank purchase, In addition, $48.7 million or 22% was due to increases in commercial and industrial loans and $20.7 million or 9% was due to increases in loans secured by real estate. Of the increase in 2014, $55.4 million or 32.9% was due to increases in commercial and industrial loans and $19.8 million or 2.7% was due to increases in loans secured by real estate. Of the increase in 2013, $61.4 million or 86% was due to increases in loans secured by real estate.

Total deposit balances increased to $1.73 billion at December 31, 2015 from $1.27 billion at December 31, 2014 and from $1.29 billion at December 31, 2013. The increase in 2015 was primarily the result of the acquisition of the ONB Branches during third quarter of 2015 that included $454 million in deposits . The decline in 2014 was due to declines in non-interest bearing deposits and higher rate CDs that matured and were not replaced offset by an increase in interest bearing deposits.

Net interest margin, defined as net interest income divided by average interest-earning assets, was 3.27% for 2015, 3.43% for 2014 and 3.38% for 2013. The decrease during 2015 was primarily due to the decline in earning asset yields from the higher amount of interest bearing deposits or short-term liquidity from the acquisition and declines in loan yields. The increase during 2014 was primarily due to the growth in loan balances.

Net interest income increased to $55.8 million in 2015 from $51.5 million in 2014 and $49.9 million in 2013. 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 increased to $20.5 million in 2015 compared to $18.4 million in 2014 and $19.3 million in 2013. ATM revenue increased by $761,000 or 19.4%, and service charge income increased $417,000 or 7.9% primarily due to increased transactions following the Old National Bank Branch acquisition, Mortgage banking income increased $158,000 or 26.5% as refinance activity and new purchase activity has increased due to lower mortgage rates. Additionally, trust, brokerage & insurance commissions increased $762,000 or 12%. The primary reason for the decrease of $.9 million or 5% from 2013 to 2014 was less gains on sales of securities and a decline in mortgage banking income as refinance and new purchase activity has slowed, offset by increases in revenue from brokerage and insurance commissions and deposit account service charges.

Non-interest expenses increased $4,741,000, to $49.2 million in 2015 compared to $44.5 million in 2014, and $43.5 million in 2013. The increase during 2015 was primarily due to expenses incurred of $1.4 million to acquire the twelve ONB Branches and expenses for the operation of the branches from acquisition in August through year-end. In addition, salaries & benefits expense increased $1.6 million or 6.3%, and occupancy & equipment expense increased $796,000 or 9.5%. The increase during 2014 of 2.3% was primarily due to an increase in salary and benefits expense as a result of higher officer salary and insurance costs.

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

	2015 vs 2014	2014 vs 2013
Net interest income	$4,270	$1,558
Provision for loan losses	(689)	1,564
Other income, including securities transactions	2,175	(972)
Other expenses	(4,741)	(1,003)
Income taxes	36	(408)
Increase in net income	$1,051	$739

Credit quality is an area of importance to the Company. Year-end total nonperforming loans were $4.0 million at December 31, 2015 compared to $4.5 million at December 31, 2014, and $6.5 million at December 31, 2013. The decrease in 2015 and 2014 was the result of loans that paid off or became current during the year and loans transferred to other real estate owned. Other real estate owned balances totaled $477,000 at December 31, 2014 compared to $263,000 at December 31, 2014, and $568,000 at December 31, 2013. The increase in 2015 was due to more properties being transferred in than sold during the year. The Company's provision for loan losses was $1.3 million for 2015, compared to $629,000 for 2014, and $2.2 million for 2013. At December 31, 2015, loans secured by both commercial and residential real estate comprised 66%, 70%, and 74% of the loan portfolio for 2015, 2014, and 2013, respectively.

The Company also held an investment in one trust preferred security with a fair value of $1.9 million and unrealized losses of $1.2 million compared to a fair value of $364,000 and unrealized losses of $2.9 million at December 31, 2014. During 2015 and 2014 the Company did not record any additional impairment charges for these securities. 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, 2015, 2014, and 2013 was 13.23%, 14.42%, and 14.37%, respectively. The Company's total capital to risk weighted assets ratio at December 31, 2015, 2014, and 2013 was 14.25%, 15.60% ,and 15.58%, respectively. The primary reason for the decrease in these ratios was completion of the acquisition of twelve ONB Branches which increased risk-weighted assets by approximately $227 million offset by completion of private placement capital raise completed during the second quarter of 2015 which resulted in an increase in common stockholder's equity of approximately

$29.3 million. The increase in these ratios during 2014 was primarily the result of an increase in retained earnings from current year net income and slightly lower preferred dividends due to the conversion of Series B Preferred Stock. The decline in these ratios during 2013 was primarily due to a decrease in retained earning resulting from a greater amount of preferred dividends paid following the issuance of additional Series C Preferred Stock in 2012. (See "Preferred Stock" in Note 1 to consolidated financial statements for more detailed information.)

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, 2015, 2014 and 2013 were $298.3 million, $242.8 million, and $244.2 million, respectively. See Note 17 – "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 is 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 2015 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, is reflected on the balance sheets. 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 11 – "Disclosures of Fair Values of Financial Instruments."

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, 2015			Year Ended December 31, 2014			Year Ended December 31, 2013		
	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate
ASSETS									
Interest-bearing deposits	$78,605	$199	0.25 %	$32,379	$83	0.26 %	$13,633	$33	0.24 %
Federal funds sold	493	—	0.10 %	495	1	0.10 %	6,923	6	0.09 %
Certificates of deposit investments	5,118	44	0.86 %	—	—	— %	2,554	14	0.55 %
Investment securities									
Taxable	400,423	7,741	1.93 %	374,285	7,499	2.00 %	466,031	9,153	1.96 %
Tax-exempt (1)	88,194	2,807	3.18 %	69,614	2,352	3.38 %	61,127	2,069	3.38 %
Loans (2) (3)	1,126,479	48,460	4.30 %	1,022,605	44,799	4.38 %	924,900	42,184	4.56 %
Total earning assets	1,699,312	59,251	3.49 %	1,499,378	54,734	3.65 %	1,475,168	53,459	3.62 %
Cash and due from banks	39,296			34,782			30,397		
Premises and equipment	28,883			27,892			29,089		
Other assets	54,573			44,800			46,432		
Allowance for loan losses	(14,066)			(13,625)			(12,448)		
Total assets	$1,807,998			$1,593,227			$1,568,638		
LIABILITIES AND STOCKHOLDERS' EQUITY									
Deposits:									
Demand deposits, interest-bearing	$669,442	722	0.11 %	$559,168	689	0.12 %	$544,157	795	0.15 %
Savings deposits	298,594	398	0.13 %	281,185	375	0.13 %	294,615	452	0.15 %
Time deposits	219,836	1,162	0.53 %	229,763	1,287	0.56 %	207,454	1,456	0.70 %
Securities sold under agreements to repurchase	113,748	62	0.05 %	97,478	47	0.05 %	87,468	46	0.05 %
FHLB advances	23,164	616	2.66 %	14,575	339	2.33 %	13,258	254	1.91 %
Federal funds purchased	142	—	— %	16	—	0.52 %	1,463	9	0.62 %
Subordinated debentures	20,620	526	2.55 %	20,620	514	2.49 %	20,620	523	2.54 %
Other debt	471	13	2.66 %	101	1	1.22 %	—	—	— %
Total interest-bearing liabilities	1,346,017	3,499	0.26 %	1,202,906	3,252	0.27 %	1,169,035	3,535	0.30 %
Demand deposits	267,175			223,505			237,373		
Other liabilities	7,908			8,452			8,308		
Stockholders' equity	186,898			158,364			153,922		
Total liabilities & equity	$1,807,998			$1,593,227			$1,568,638		
Net interest income		$55,752			$51,482			$49,924	

Net interest spread	3.23	%	3.38	%	3.32	%
Impact of non-interest bearing funds	0.04	%	0.05	%	0.06	%
Net yield on interest-earning assets	3.27	%	3.43	%	3.38	%

(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):

	2015 Compared to 2014 Increase – (Decrease)			2014 Compared to 2013 Increase – (Decrease)		
	Total Change	Volume (1)	Rate (1)	Total Change	Volume (1)	Rate (1)
Earning Assets:						
Interest-bearing deposits	$116	$119	$(3)	$50	$47	$3
Federal funds sold	(1)	(1)	—	(5)	(6)	1
Certificates of deposit investments	44	44	—	(14)	(7)	(7)
Investment securities:						
Taxable	242	510	(268)	(1,654)	(1,836)	182
Tax-exempt (2)	455	598	(143)	283	287	(4)
Loans (3)	3,661	4,490	(829)	2,615	4,328	(1,713)
Total interest income	4,517	5,760	(1,243)	1,275	2,813	(1,538)
Interest-Bearing Liabilities:						
Deposits:						
Demand deposits, interest-bearing	33	102	(69)	(106)	27	(133)
Savings deposits	23	23	—	(77)	(19)	(58)
Time deposits	(125)	(56)	(69)	(169)	144	(313)
Securities sold under agreements to repurchase	15	15	—	1	1	—
FHLB advances	277	223	54	85	26	59
Federal funds purchased	—	—	—	(9)	(8)	(1)
Subordinated debentures	12	—	12	(9)	—	(9)
Other debt	12	10	2	1	(326)	327
Total interest expense	247	317	(70)	(283)	(155)	(128)
Net interest income	$4,270	$5,443	$(1,173)	$1,558	$2,968	$(1,410)

(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 increased $4.3 million or 8.3% in 2015 compared to an increase of $1.6 million or 3.1% in 2014. Net interest income increased primarily due to assets added in the acquisition of twelve ONB Branches and the growth in average earning assets. The net interest margin decreased primarily due to the decline in earning asset yield from the higher amount of interest bearing deposits or short-term liquidity from the acquisition and declines in loan and investment yields. The increase in 2014 is primarily due to growth in average earning assets and an increase in net interest margin. The net interest margin increased due to the shift in balances of investment securities to higher-yielding loans, an increase in yield on investments and the reduction in deposit costs.

In 2015 average earning assets increased by $199.9 million, or 13.3%, and average interest-bearing liabilities increased by $143.1 million or 11.9%. In 2014, average earning assets increased by $24.2 million or 1.6% and average

interest-bearing liabilities increased $33.9 million or 2.9% compared with 2013. Changes in average balances are shown below:

- Average interest-bearing deposits held by the Company increased $46.2 million or 142.8% in 2015 compared to 2014. In 2014, average interest-bearing deposits held by the Company increased $18.7 million or 137.5% compared to 2013.

- Average federal funds sold decreased $2,000 or 0.4% in 2015 compared to 2014. In 2014, average federal funds sold decreased $6.4 million or 92.8% compared to 2013.

- Average certificates of deposit investments increased $5.1 million or 100.0% in 2015 compared to 2014. In 2014, average certificates of deposit investments decreased $2.6 million or 100.0% compared to 2013.

- Average loans increased by $103.9 million or 10.2% in 2015 compared to 2014. In 2014, average loans increased by $97.7 million or 10.6% compared to 2013.

- Average securities increased by $44.7 million or 10.1% in 2015 compared to 2014. In 2014, average securities decreased by $83.3 million or 15.8% compared to 2013.

- Average deposits increased by $117.8 million or 11.0% in 2015 compared to 2014. In 2014, average deposits increased by $23.9 million or 2.3% compared to 2013.

- Average securities sold under agreements to repurchase increased by $16.3 million or 16.7% in 2015 compared to 2014. In 2014, average securities sold under agreements to repurchase increased by $10.0 million or 11.4% compared to 2013.

- Average borrowings and other debt increased by $9.1 million or 25.7% in 2015 compared to 2014. In 2014, average borrowings and other debt decreased by $29,000 or 0.1% compared to 2013.

- The federal funds rate remained at a range of .25% to .30% at December 31, 2015, 2014 and 2013.

- Net interest margin decreased to 3.27% compared to 3.43% in 2014 and 3.38% in 2013. Asset yields decreased by 16 basis points in 2015, and interest-bearing liabilities decreased by 1 basis point.

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 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 35% (referred to as the tax equivalent adjustment). The tax equivalent basis adjustments to net interest income for 2015, 2014 and 2013 were $1,674,000, $1,435,000, and $1,316,000, respectively. The net yield on interest-earning assets on a tax equivalent basis was 3.37% in 2015, 3.53% in 2014 and 3.47% in 2013.

Provision for Loan Losses

The provision for loan losses in 2015 was $1,318,000 compared to $629,000 in 2014 and $2,193,000 in 2013. Nonperforming loans decreased to $4,013,000 at December 31, 2015 from $4,540,000 at December 31, 2014 and $6,469,000 at December 31, 2013. The increase in provision expense in 2015 was the result of an increase in net charge offs and an increase in loan balances. Net charge-offs were $424,000 during 2015, $196,000 during 2014 and $720,000 during 2013. 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	
	2015	2014	2013	2015	2014
Trust	$3,746	$3,571	$3,565	$175	$6
Brokerage	1,315	1,039	833	276	206
Insurance commissions	2,107	1,796	1,638	311	158

Service charges	5,681	5,264	4,865	417	399
Securities gains	452	715	2,293	(263)	(1,578)
Mortgage banking	754	596	935	158	(339)
ATM / debit card revenue	4,676	3,915	3,772	761	143
Other	1,813	1,473	1,440	340	33
Total other income	$20,544	$18,369	$19,341	$2,175	$(972)

Total non-interest income increased to $20.5 million in 2015 compared to $18.4 million in 2014 and $19.3 million in 2013. The primary reasons for the more significant year-to-year changes in other income components are as follows:

- Trust revenues increased $175,000 or 4.9% in 2015 to $3,746,000 from $3,571,000 in 2014 and $3,565,000 in 2013. The increases during 2015 and 2014 were primarily due to increases in market value related fees. Trust assets were $794.0 million at December 31, 2015 compared to $757.3 million at December 31, 2014 and $722.9 million at December 31, 2013.

- Revenue from brokerage increased $276,000 or 26.6% to $1,315,000 in 2015 from $1,039,000 in 2014 and $833,000 in 2013 due to an increase in the number of brokerage accounts from new business development efforts.

- Insurance commissions increased $311,000 or 17.3% to $2,107,000 in 2015 from $1,796,000 in 2014 compared to $1,638,000 in 2013. The increase from 2014 to 2015 was due to an increase in contingency income received from carriers based on claims experience and an increase in commission and fee income received. The increase from 2013 to 2014 was due to an increase in contingency income received from carriers based on claims experience.

- Fees from service charges increased $417,000 or 7.9% to $5,681,000 in 2015 from $5,264,000 in 2014 and $4,865,000 in 2013. The increase from 2014 to 2015 was primarily due to additional income from the ONB branches acquired in the third quarter of 2015. The increase from 2013 to 2014 was primarily due to an increase in overdraft fees and transaction service charges.

- Net securities gains in 2015 were $452,000 down $263,000 or (36.8)% from $715,000 in 2014 and $2,293,000 in 2013. The decline in 2015 was due to market conditions and balance sheet position. The decline in security gains from 2013 to 2014 was primarily due to the sale of two trust preferred securities that resulted in net security gains of $1.4 million.

- Mortgage banking income increased $158,000 or 26.5% to $754,000 in 2015 from $596,000 in 2014 and $935,000 in 2013. The increase during 2015 was due to a increase in the volume of loans originated and sold by First Mid Bank. Loans sold balances are as follows:

  $57 million (representing 457 loans) in 2015
  $44 million (representing 368 loans) in 2014
  $65 million (representing 552 loans) in 2013

First Mid Bank generally releases the servicing rights on loans sold into the secondary market.

- Revenue from ATMs and debit cards increased $761,000 or 19.4% to $4,676,000 in 2015 from $3,915,000 in 2014 compared to $3,772,000 in 2013. The increase from 2014 to 2015 was due to the ONB Branches acquired during the third quarter of 2015 and an increase in electronic transactions and incentives received from VISA. The increase from 2013 to 2014 was primarily due to in increase in electronic transactions and incentives received from VISA.

- Other income increased $340,000 or 23.1% in 2015 to $1,813,000 from $1,473,000 in 2014 compared to $1,440,000 in 2013. The increase from 2014 to 2015 was due to income from the ONB branches acquired during the third quarter of 2015 and an increase in merchant card processing fees. The increase from 2013 to 2014 was primarily due to an increase in merchant card processing fees.

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	
	2015	2014	2013	2015	2014
Salaries and benefits	$26,337	$24,771	$24,128	$1,566	$643
Occupancy and equipment	9,143	8,347	8,223	796	124
Other real estate owned, net	19	23	163	(4)	(140)
FDIC insurance assessment expense	904	804	832	100	(28)
Amortization of other intangibles	891	643	674	248	(31)
Stationery and supplies	681	646	603	35	43
Legal and professional fees	2,474	2,333	2,070	141	263
Marketing and promotion	1,092	1,015	1,221	77	(206)
Other	7,707	5,925	5,590	1,782	335
Total other expense	$49,248	$44,507	$43,504	$4,741	$1,003

Total non-interest expense increased to $49.2 million in 2015 from $44.5 million in 2014 and $43.5 million in 2013. 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, increased $1,566,000 or 6.3% to $26.3 million from $24.8 million in 2014, and $24.1 million in 2013. The increase was due to the addition of 84 employees with the acquisition of twelve ONB branches and merit increases for continuing employees during the first quarter of 2015. The increase in 2014 was primarily due to merit increases for continuing employees during the first quarter of 2014 offset by a decrease in the number of employees. There were 513 full-time equivalent employees at December 31, 2015, compared to 400 at December 31, 2014, and 406 at December 31, 2013.

- Occupancy and equipment expense increased $796,000 or 9.5% to $9.1 million in 2015 from $8.3 million in 2014, compared to $8.2 million in 2013. The increase in 2015 was primarily due to increases in rent and depreciation expenses related to the acquisition of twelve ONB Branches. The increase in 2014 was primarily due to increases in maintenance and repair expense for equipment and software and buildings owned by the company offset by less depreciation expense on software that was fully amortized during 2014.

- Net other real estate owned expense decreased $4,000 or 17.4% to $19,000 from $23,000 in 2014, and $163,000 in 2013. The decrease in 2015 was primarily due to less losses on properties sold during 2015 compared to properties sold in 2014. The decrease during 2014 were primarily due to the decline in the outstanding balance of other real estate owned.

- FDIC insurance expense increased $100,000 or 12.4% to $904,000 from $804,000 in 2014, and $832,000 in 2013. The increase in 2015 was primarily due to an increase in average assets due to the acquisition of twelve ONB Branches. The decrease in 2014 was primarily due to lower assessment rates as a result of improved asset quality offset by an increase in average assets compared to the previous year.

- Amortization of other intangibles expense increased $248,000 or 38.6% to $891,000 from $643,000 in 2014, compared to $674,000 in 2013. The increase in 2015 was due to the acquisition of twelve ONB Branches. The decrease in intangible amortization expense in 2014 was due to less amortization expense for core deposit intangibles.

- Other operating expenses increased $1,782,000 or 30.1% to $7,707,000 from $5,925,000 in 2014, compared to $5,590,000 in 2013. The increase in 2015 was primarily due to expenses incurred to acquire of twelve ONB Branches during the third quarter of 2015. The increase in 2014 was primarily due to filing and listing fees paid to NASDAQ during 2014 that was not paid during 2013 and increases in various other expenses in 2014.

- On a net basis, all other categories of operating expenses increased $253,000 or 6.3% to $4,247,000 from $3,994,000 in 2014, compared to $3,894,000 in 2013. The increase in 2015 was primarily due to an increase in legal and professional fees, marketing and promotion, and stationary and supplies due to the acquisition of twelve ONB Branches. The increase in 2014 was primarily due to an increase in legal and professional fees offset by a decrease in marketing and promotion.

Income Taxes

Income tax expense amounted to $9,218,000 in 2015 compared to $9,254,000 in 2014, and $8,846,000 in 2013. Effective tax rates were 35.8% for 2015, 37.4% for 2014, and 37.5% for 2013. The decline in effective tax rate for 2015 was primarily due to a reduction in the Company's state tax rate, from 9.5% to 7.75% beginning January 1, 2015.

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Analysis of Balance Sheets

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 amortized cost of the available-for-sale and held-to-maturity securities for the last three years (dollars in thousands):

	December 31,								
	2015			2014			2013		
	Amortized Cost	Weighted Average Yield		Amortized Cost	Weighted Average Yield		Amortized Cost	Weighted Average Yield	
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$175,576	1.70	%	$154,874	1.72	%	$197,805	1.56	%
Obligations of states and political subdivisions	107,164	3.22	%	75,589	3.33	%	65,304	3.43	%
Mortgage-backed securities: GSE residential	312,132	2.52	%	193,814	2.48	%	229,661	2.60	%
Trust preferred securities	3,130	1.41	%	3,300	1.14	%	3,652	1.14	%
Other securities	4,035	1.38	%	4,036	1.20	%	6,035	1.17	%
Total securities	$602,037	2.39	%	$431,613	2.33	%	$502,457	2.27	%

At December 31, 2015, the Company's investment portfolio increased by $170.4 million from December 31, 2014 primarily due to purchases of obligation of U.S. government corporations and agencies securities and mortgaged-backed securities as the company deploys the excess cash received in the acquisition of the ONB Branches. 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. During the third quarter of 2014, management evaluated its available-for-sale portfolio and transferred obligations of U.S. government corporations & agencies securities with a fair value of $53.6 million from available-for-sale to held-to-maturity to reduce price volatility. Management determined it has both the intent and ability to hold these securities to maturity. Transfers of investment securities into the held-to-maturity category from available-for-sale are made at fair value on the date of transfer. There were no gains or losses recognized as a result of this transfer. The related $1.4 million of unrealized holding loss that was included in the transfer is retained in the carrying value of the held-to-maturity securities and in other comprehensive income net of deferred taxes. These amounts are being amortized into net interest income over the remaining life of the related securities as a yield adjustment, resulting in no impact on future net income.

The table below presents the credit ratings as of December 31, 2015 for certain investment securities (in thousands):

			Average Credit Rating of Fair Value at December 31, 2015 (1)					
	Amortized Cost	Estimated Fair Value	AAA	AA +/-	A +/-	BBB +/-	< BBB -	Not rated
Available-for-sale:								
U.S. Treasury securities and obligations of U.S. government corporations and	$90,368	$90,141	$—	$90,141	$—	$—	$—	$—

agencies								
Obligations of state and political subdivisions	107,164	110,717	3,066	75,996	30,827	—	—	828
Mortgage-backed securities (2)	312,132	312,054	—	—	—	—	—	312,054
Trust preferred securities	3,130	1,906	—	—	—	—	1,906	—
Other securities	4,035	4,030	—	—	2,000	1,966	—	64
Total investments	$516,829	$518,848	$3,066	$166,137	$32,827	$1,966	$1,906	$312,946
Held-to-maturity:								
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$85,208	$85,737	$—	$80,737	$—	$—	$—	$5,000

(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 consist of one trust preferred pooled security issued by FTN Financial Securities Corp. (“FTN”). The following table contains information regarding this security as of December 31, 2015:

Deal name	PreTSL XXVIII	
Class	Mezzanine C-1	
Book value	$3,130,000	
Fair value	$1,906,000	
Unrealized gains/(losses)	$(1,224,000	)
Other-than-temporary impairment recorded in earnings	$1,111,000	
Lowest credit rating assigned	CCC	
Number of performing banks	35	
Number of issuers in default	8	
Number of issuers in deferral	1	
Original collateral	$360,850,000	
Actual defaults & deferrals as a % of original collateral	13.7	%
Remaining collateral	$340,712,000	
Actual defaults & deferrals as a % of remaining collateral	14.5	%
Expected defaults & deferrals as a % of remaining collateral	40.2	%
Performing collateral	$291,212,000	
Estimated incremental defaults	$67,084,000	
Current balance of class	$34,694,000	
Subordination	$198,241,000	
Excess subordination	$10,797,000	
Excess subordination as a % of remaining performing collateral	12.0	%
Discount rate (1)	1.62%-4.29%	
Expected defaults & deferrals as a % of remaining collateral (2)	2% / .36	
Recovery assumption (3)	10	%
Prepayment assumption (4)	1	%

(1) The discount rate for floating rate bonds is a compound interest formula based on the LIBOR forward curve for each payment date
(2) 2% annually for 2 years and 36 basis points annually thereafter
(3) With 2 year lag
(4) Additional assumptions regarding prepayments:
Banks with more than $15 billion in total assets as of 12/31/2009:
(a) For fixed rate TruPS, all securities will be called in one year
(b) For floating rate TruPS, (1) all securities with spreads greater than 250 bps will be called in one year (2) all securities with spreads between 150 bps and 250 bps will be called at a rate of 5% annually (3) all securities with spreads less than 150 bps will be called at a rate of 1% annually
Banks with less than $15 billion in total assets as of 12/31/2009:
(a) For fixed rate TruPS, (1) all securities with coupons greater than 8% that were issued by healthy banks with the capacity to prepay will be called in one year (2) All remaining fixed rate securities will be called at a rate of 1% annually
(b) For floating rate TruPs, all securities will be called at a rate of 1% annually

The trust preferred pooled security is a Collateralized Debt Obligations ("CDOs") backed by a pool of debt securities issued by financial institutions. The collateral consists of trust-preferred securities and subordinated debt securities issued by banks, bank holding companies and insurance companies. Performing collateral is the amount of remaining collateral less the balances of collateral in deferral or default. Subordination is the amount of performing collateral in excess of the current balance of a specified class and all classes senior to the specified class. Excess subordination is the amount that the performing collateral balance exceeds the current outstanding balance of the specific class, plus all senior classes. It is a static measure of credit enhancement, but does not incorporate all of the structural elements of the security deal. This amount can also be impacted by future defaults and deferrals, deferring balances that cure or redemptions of securities by issuers. A negative excess subordination indicates that the current performing collateral of the security would be insufficient to pay the current principal balance of the class notes after all of the senior classes' notes were paid. However, the performing collateral balance excludes the collateral of issuers currently deferring their interest payments. Because these issuers are expected to resume payment in the future (within five years of the first deferred interest period), a negative excess subordination does not necessarily mean a class note holder will not receive a greater than projected or even full payment of cash flow at maturity.

During the year ended December 31, 2015 the Company received all of the contractual interest payments for its trust preferred security. During 2014 and 2013, the Company was receiving "payment in kind" ("PIK") in lieu of cash interest on its trust preferred security investment as and to the extent described below. The Company's use of "PIK" does not indicate that additional securities have been issued in satisfaction of any outstanding obligation; rather, it indicates that a coverage test of a class or tranche directly senior to the class in question failed and interest received on the PIK note was being capitalized, which means the principal balance was being increased. Once the coverage test is met, capitalized interest is paid in cash and current cash interest payments resume.

The Company's trust preferred security investment allows, under the terms of the issue, for issuers to defer interest for up to five consecutive years. After five years, if not cured, the security is considered to be in default and the trustee may demand payment in full of principal and accrued interest. Issuers are also considered to be in default in the event of the failure of the issuer or a subsidiary. The structuring of the trust preferred security provides for a waterfall approach to absorbing losses whereby lower classes or tranches are initially impacted and more senior tranches are only impacted after lower tranches can no longer absorb losses. Likewise, the waterfall approach also applies to principal and interest payments received, as senior tranches have priority over lower tranches in the receipt of payments. Both deferred and defaulted issuers are considered non-performing, and the trustee calculates, on a quarterly or semi-annual basis, certain coverage tests prior to the payment of cash interest to owners of the various tranches of the securities. The coverage tests are compared to an over-collateralization target that states the balance of performing collateral as a percentage of the tranche balance plus the balance of all senior tranches. The tests must show that performing collateral is sufficient to meet requirements for the senior tranches, both in terms of cash flow and collateral value, before cash interest can be paid to subordinate tranches. As a result of the cash flow waterfall provisions within the structure of these securities, when a senior tranche fails its coverage test, all of the cash flows that would have been paid to lower tranches are paid to the senior tranche and recorded as a reduction of the senior tranches' principal. This principal reduction in the senior tranche continues until the coverage test of the senior tranche is passed or the principal of the tranche is paid in full. For so long as the cash flows are being diverted to the senior tranches, the amount of interest due and payable to the subordinate tranches is capitalized and recorded as an increase in the principal value of the tranche. The Company's trust preferred security investment is in the mezzanine branch or class which are subordinate to the more senior tranches of the issues. During 2013, the Company received it's full interest payments.

The impact of payment of PIK to subordinate tranches is to strengthen the position of the senior tranches by reducing the senior tranches' principal balances relative to available collateral and cash flow. The impact to the subordinate tranches is to increase principal balances, decrease cash flow, and increase credit risk to the tranches receiving the PIK. The risk to holders of a security of a tranche in PIK status is that the total cash flow will not be sufficient to

repay all principal and capitalized interest related to the investment.

During the fourth quarter of 2010, after analysis of the expected future cash flows and the timing of resumed interest payments, the Company determined that placing its trust preferred security on non-accrual status was the most prudent course of action. The Company stopped all accrual of interest and ceased to capitalize any PIK to the principal balance of the securities. The Company intends to keep its remaining trust preferred security on non-accrual status until the scheduled interest payments resume on a regular basis and the full payment of the securities is ensured. The PIK status of these securities, among other factors, indicates potential other-than-temporary impairment ("OTTI") and accordingly, the Company performed further detailed analysis of the investments' cash flows and the credit conditions of the underlying issuers. This analysis incorporates, among other things, the waterfall provisions and any resulting PIK status of the securities to determine if cash flow will be sufficient to pay all principal and interest due to the investment tranche held by the Company.

See discussion below and Note 4 – Investment Securities in the notes to the financial statements for more detail regarding this analysis. Based on this analysis, the Company believes the amortized costs recorded for its trust preferred securities investments accurately reflects the position of these securities at December 31, 2015 and 2014.

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 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 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 in the notes to the financial statements for a discussion of the Company’s evaluation and, when applicable, charges for OTTI.

Loans

The loan portfolio (net of unearned interest) is the largest category of the Company’s earning assets. The following table summarizes the composition of the loan portfolio, including loans held for sale, for the last five years (in thousands):

	2015	% Outstanding Loans		2014	2013	2012	2011
Construction and land development	$39,209	3.1	%	$21,627	$25,321	$31,341	$23,136
Farm loans	122,474	9.6	%	110,193	109,405	86,271	72,585
1-4 Family residential properties	231,571	18.1	%	181,921	184,761	186,498	181,849
Multifamily residential properties	45,740	3.6	%	53,129	50,174	44,863	19,846
Commercial real estate	409,172	31.9	%	379,604	356,999	316,322	321,001

Loans secured by real estate	848,166	66.3	%	746,474	726,660	665,295	618,417
Agricultural loans	75,886	5.9	%	68,298	64,128	61,014	63,257
Commercial and industrial loans	305,060	23.7	%	223,780	168,353	160,299	150,716
Consumer loans	41,579	3.2	%	15,118	14,579	16,264	16,271
All other loans	11,198	0.9	%	8,736	9,084	8,193	11,413
Total loans	$1,281,889	100.0	%	$1,062,406	$982,804	$911,065	$860,074

Loan balances increased by $219.5 million or 20.7% from December 31, 2014 to December 31, 2015 primarily due to loans added in the acquisition of twelve ONB Branches and increases in originations of loans secured by real estate and commercial and industrial loans. Loan balances increased by $79.6 million or 8.1% from December 31, 2013 to December 31, 2014 primarily due to originations of loans commercial and industrial loans. The balances of loans sold into the secondary market were $57.1 million in 2015 compared to $44.0 million in 2014. The balance of real estate loans held for sale, included in the balances shown above, amounted to $968,000 and $1,958,000 as of December 31, 2015 and 2014, 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, 2015 and 2014 (dollars in thousands):

	December 31, 2015			December 31, 2014		
	Principal balance	% Outstanding Loans		Principal balance	% Outstanding Loans	
Central region	$401,150	31.3	%	$368,484	34.7	%
Sullivan region	161,921	12.6	%	153,731	14.5	%
Decatur region	287,788	22.5	%	256,241	24.1	%
Peoria region	172,203	13.4	%	166,056	15.6	%
Highland region	114,378	8.9	%	117,894	11.1	%
Southern region	144,449	11.3	%	—	—	%
Total all regions	$1,281,889	100.0	%	$1,062,406	100.0	%

Loans are geographically dispersed among these regions located in central and southwestern Illinois. While these regions have experienced some economic stress during 2015 and 2014, 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 some 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, 2015 and 2014, the Company did have industry loan concentrations in excess of 25% of total risk-based capital in the following industries (dollars in thousands):

	December 31, 2015			December 31, 2014		
	Principal balance	% Outstanding Loans		Principal balance	% Outstanding Loans	
Other grain farming	$161,495	12.60	%	$155,136	14.60	%
All Other General Merchandise Stores	39,864	3.11	%	46,169	4.35	%
Lessors of non-residential buildings	109,070	8.51	%	96,508	9.08	%
Lessors of residential buildings & dwellings	67,513	5.27	%	65,781	6.19	%
Hotels and motels	62,881	4.91	%	56,546	5.32	%

Balances of all other grain merchandise stores were not considered a concentration during 2015, but is shown here for comparative purposes. 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, 2015, 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	$34,264	$4,077	$868	$39,209
Farm loans	6,452	53,094	62,928	122,474
1-4 Family residential properties	21,531	78,887	131,153	231,571
Multifamily residential properties	1,372	18,266	26,102	45,740
Commercial real estate	43,196	238,296	127,680	409,172
Loans secured by real estate	106,815	392,620	348,731	848,166
Agricultural loans	56,702	18,225	959	75,886
Commercial and industrial loans	130,591	119,409	55,060	305,060
Consumer loans	3,299	27,444	10,836	41,579
All other loans	1,398	3,971	5,829	11,198
Total loans	$298,805	$561,669	$421,415	$1,281,889

(1) Based upon remaining contractual maturity.
(2) Includes demand loans, past due loans and overdrafts.

As of December 31, 2015, loans with maturities over one year consisted of approximately $841.9 million in fixed rate loans and approximately $141.2 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 Nonperforming Other 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 “troubled debt restructurings”. 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 against 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,									
	2015		2014		2013		2012		2011	
Nonaccrual loans	$3,412		$4,105		$6,121		$7,573		$6,723	
Restructured loans which are performing in accordance with revised terms	601		435		348		20		717	
Total nonperforming loans	4,013		4,540		6,469		7,593		7,440	
Repossessed assets	477		263		568		1,229		4,606	
Total nonperforming loans and repossessed assets	$4,490		$4,803		$7,037		$8,822		$12,046	
Nonperforming loans to loans, before allowance for loan losses	0.31	%	0.43	%	0.66	%	0.83	%	0.87	%
Nonperforming loans and repossessed assets to loans, before allowance for loan losses	0.35	%	0.45	%	0.72	%	0.98	%	1.40	%

The $693,000 decrease in nonaccrual loans during 2015 resulted from the net of $2.3 million of loans put on nonaccrual status, offset by $397,000 of loans transferred to other real estate owned, $85,000 of loans charged off and $2.5 million of loans becoming current or paid-off. The following table summarizes the composition of nonaccrual loans (in thousands):

	December 31, 2015			December 31, 2014		
	Balance	% of Total		Balance	% of Total	
Construction and land development	$142	4.2	%	$785	19.1	%
Farm loans	454	13.3	%	29	0.7	%
1-4 Family residential properties	975	28.5	%	878	21.4	%
Multifamily residential properties	317	9.3	%	—	—	%
Commercial real estate	269	7.9	%	2,074	50.5	%
Loans secured by real estate	2,157	63.2	%	3,766	91.7	%
Agricultural loans	79	2.3	%	—	—	%
Commercial and industrial loans	928	27.2	%	332	8.1	%
Consumer loans	248	7.3	%	7	0.2	%
Total loans	$3,412	100.0	%	$4,105	100.0	%

Interest income that would have been reported if nonaccrual and restructured loans had been performing totaled $48,000, $71,000 and $45,000 for the years ended December 31, 2015, 2014 and 2013, respectively.

The $215,000 increase in repossessed assets during 2015 resulted from the net of $470,000 of additional assets repossessed, $234,000 of repossessed assets sold and $21,000 of further write-downs of repossessed assets to current market value. The following table summarizes the composition of repossessed assets (in thousands):

	December 31, 2015			December 31, 2014		
	Balance	% of Total		Balance	% of Total	
Construction and land development	$186	38.9	%	$201	76.4	%
1-4 family residential properties	—	—	%	62	23.6	%
Commercial real estate	291	60.9	%	—	—	%
Total real estate	477	99.8	%	263	100.0	%
Consumer Loans	1	0.2	%	—	—	%
Total repossessed collateral	$478	100.0	%	$263	100.0	%

Repossessed assets sold during 2015 resulted in net losses of $21,000, of which $14,000 was related to real estate asset sales and $7,000 was related to other repossessed assets sales. Repossessed assets sold during 2014 resulted in net losses of $33,000, of which $33,000 were related to real estate asset sales and $0 was related to other repossessed assets 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 probable losses existing 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 three-year loss migration analysis as one of several components in assessing the probability of inherent future losses. Given the continued weakened economic conditions, management also increased its allocation to various loan categories for economic factors during 2015 and 2014. 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 uncertainty regarding grain prices, drought conditions 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, 2015, the Company's loan portfolio included $198.4 million of loans to borrowers whose businesses are directly related to agriculture. Of this amount, $161.5 million was concentrated in other grain farming. Total loans to borrowers whose businesses are directly related to agriculture increased $19.9 million from $178.5 million at December 31, 2014 while loans concentrated in other grain farming increased $6.4 million from $155.1 million at December 31, 2014.

While the Company adheres to sound underwriting practices, including collateralization of loans, any extended period of low commodity prices, drought conditions, 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 $62.9 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 $109.1 million of loans to lessors of non-residential buildings and $67.5 million of loans to lessors of residential buildings and dwellings.

The structure of the Company's loan approval process is based on progressively larger lending authorities granted to individual loan officers, loan committees, and ultimately the Board of Directors. Outstanding balances to one borrower or affiliated borrowers are limited by federal regulation; however, limits well below the regulatory thresholds are generally observed. The vast majority of the Company's loans are to businesses located in the geographic market areas served by the Company's branch bank system. Additionally, a significant portion of the collateral securing the loans in the portfolio is located within the Company's primary geographic footprint. In general, the Company adheres to loan underwriting standards consistent with industry guidelines for all loan segments.

The Company minimizes credit risk by adhering to sound underwriting and credit review policies. Management and the Board of Directors of the Company review these policies at least annually. 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. On a quarterly basis, the Board of Directors and management review the status of problem loans and determine a best estimate of the allowance. In addition to internal policies and controls, regulatory authorities periodically review asset quality and the overall adequacy of the allowance for loan losses.

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):

	2015	2014	2013	2012	2011
Average loans outstanding, net of unearned income	$1,126,479	$1,022,605	$924,900	$866,912	$807,463
Allowance-beginning of period	13,682	13,249	11,776	11,120	10,393
Charge-offs:					
Real estate-mortgage	131	185	479	1,423	2,625
Commercial, financial & agricultural	222	41	426	699	881
Installment	285	63	35	79	92
Other	268	248	188	170	162
Total charge-offs	906	537	1,128	2,371	3,760
Recoveries:					
Real estate-mortgage	186	110	36	137	1,171
Commercial, financial & agricultural	120	78	232	85	97
Installment	24	26	30	67	28
Other	152	127	110	91	90
Total recoveries	482	341	408	380	1,386
Net charge-offs	424	196	720	1,991	2,374
Provision for loan losses	1,318	629	2,193	2,647	3,101
Allowance-end of period	$14,576	$13,682	$13,249	$11,776	$11,120
Ratio of annualized net charge-offs to average loans	0.04 %	0.03 %	0.08 %	0.23 %	0.29 %
Ratio of allowance for loan losses to loans outstanding (less unearned interest at end of period)	1.14 %	1.29 %	1.35 %	1.29 %	1.29 %
Ratio of allowance for loan losses to nonperforming loans	363.0 %	301.4 %	204.8 %	155.1 %	149.5 %

The ratio of the allowance for loan losses to nonperforming loans is 363.0% as of December 31, 2015 compared to 301.4% as of December 31, 2014. The increase in this ratio is primarily due to the decline in nonperforming loans during 2015. Management believes that the overall estimate of the allowance for loan losses appropriately accounts for probable losses attributable to current exposures.

During 2015, the Company had net charge-offs of $424,000 compared to $196,000 in 2014. During 2015, the Company's significant charge-offs included $49,000 on one commercial real estate loan, $149,000 on one commercial loan, and $251,000 on one consumer loan. During 2014, the Company's significant charge-offs included $110,000 on four commercial real estate loans to 3 borrowers and $34,000 on one consumer loan.

At December 31, 2015, the allowance for loan losses amounted to $14.6 million or 1.14% of total loans. At December 31, 2014, the allowance for loan losses amounted to $13.7 million or 1.29% of total loans. The decline in the ratio from December 31, 2014 to December 31, 2015 is due to the increase in loan balances that were recorded at fair value from the ONB acquisition.

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, 2015			December 31, 2014			December 31, 2013		
	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	$994	18.1	%	$790	17.4	%	$771	19.1	%
Commercial / Commercial real estate	11,379	63.0	%	10,914	64.4	%	10,646	61.8	%
Agricultural / Agricultural real estate	1,337	15.5	%	1,360	16.8	%	533	17.6	%
Consumer	642	3.4	%	386	1.4	%	377	1.5	%
Total allocated	14,352	100.0	%	13,450	100.0	%	12,327	100.0	%
Unallocated	224	NA		232	N/A		922	N/A	
Allowance at end of year	$14,576	100.0	%	$13,682	100.0	%	$13,249	100.0	%

	December 31, 2012			December 31, 2011		
	Allowance for loan losses	% of loans to total loans		Allowance for loan losses	% of loans to total loans	
Residential real estate	$726	19.7	%	$636	21.5	%
Commercial / Commercial real estate	9,301	62.5	%	8,791	58.8	%
Agricultural / Agricultural real estate	558	16.0	%	546	15.2	%
Consumer	403	1.8	%	378	4.5	%
Total allocated	10,988	100.0	%	10,351	100.0	%
Unallocated	788	N/A		769	N/A	
Allowance at end of year	$11,776	100.0	%	$11,120	100.0	%

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 for 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.

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 the the years ended December 31, 2015, 2014 and 2013 (dollars in thousands):

	2015			2014			2013		
	Average Balance	Weighted Average Rate		Average Balance	Weighted Average Rate		Average Balance	Weighted Average Rate	
Demand deposits:									
Non-interest-bearing	$267,175	—	%	$223,505	—	%	$237,373	—	%
Interest-bearing	669,442	0.11	%	559,168	0.12	%	544,157	0.15	%
Savings	298,594	0.13	%	281,185	0.13	%	294,615	0.15	%
Time deposits	219,836	0.53	%	229,763	0.56	%	207,454	0.70	%
Total average deposits	$1,455,047	0.16	%	$1,293,621	0.18	%	$1,283,599	0.21	%

The following table sets forth the high and low month-end balances for the years ended December 31, 2015, 2014 and 2013 (in thousands):

	2015	2014	2013
High month-end balances of total deposits	$1,741,079	$1,305,825	$1,310,169
Low month-end balances of total deposits	1,266,199	1,265,058	1,263,941

In 2015, the average balance of deposits increased by $161.4 million from 2014. The increase was primarily the result of deposit balances acquired in the acquisition of twelve ONB Branches. Average non-interest bearing deposits increased $43.7 million, other interest-bearing deposits increased by $110.2 million, savings accounts increased by $17.4 million, offset by a decrease of $9.9 million in time deposits. In 2014, the average balance of deposits increased by $10.0 million from 2013. The increase was primarily attributable to an increase in time deposits offset by declines in non-interest bearing and savings account balances. Average non-interest bearing deposits decreased by $13.9 million, savings accounts decreased by $13.4 million, average balances of other interest-bearing deposits increased $15 million and time deposits increased by $22.3 million.

Balances of time deposits of $100,000 or more include time deposits maintained for public fund entities and consumer time deposits. The following table sets forth the maturity of time deposits of $100,000 or more (in thousands):

	December 31,		
	2015	2014	2013
3 months or less	$30,108	$35,604	$17,946
Over 3 through 6 months	10,714	15,270	12,625
Over 6 through 12 months	23,091	21,710	38,084
Over 12 months	24,942	25,861	28,060
Total	$88,855	$98,445	$96,715

The balance of time deposits of $100,000 or more decreased $9.6 million from December 31, 2014 to December 31, 2015. The balance of time deposits of $100,000 or more increased $1.7 million from December 31, 2013 to December 31, 2014. The decrease in 2015 was a result of time deposits that were not renewed and brokered CDs that were not

replaced. The increase in 2014 was primarily due to an increase in public funds invested in CDs offset by declines in other CDs.

In 2015 the Company maintained account relationships with various public entities throughout its market areas. Ninety four public entities had total balances of $122.3 million in various checking accounts and time deposits as of December 31, 2015. These balances are subject to change depending upon the cash flow needs of the public entity.

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, loans (short-term or long-term debt) that the Company has outstanding and junior subordinated debentures. Information relating to securities sold under agreements to repurchase and other borrowings as December 31, 2015, 2014 and 2013 is presented below (dollars in thousands):

	2015	2014	2013
At December 31:			
Securities sold under agreements to repurchase	$128,842	$121,869	$119,187
Federal Home Loan Bank advances:			
Fixed term – due in one year or less	5,000	—	10,000
Fixed term – due after one year	15,000	20,000	10,000
Junior subordinated debentures	20,620	20,620	20,620
Total	$169,462	$162,489	$159,807
Average interest rate at end of period	0.77 %	0.54 %	0.47 %
Maximum outstanding at any month-end:			
Securities sold under agreements to repurchase	$128,842	$121,869	$119,187
Federal funds purchased	—	—	5
Federal Home Loan Bank advances:			
FHLB-overnite	—	—	11,000
Fixed term – due in one year or less	10,000	10,000	10,000
Fixed term – due after one year	20,000	20,000	10,000
Debt:			
Debt due in one year or less	2,000	—	—
Junior subordinated debentures	20,620	20,620	20,620
Averages for the period (YTD):			
Securities sold under agreements to repurchase	$113,748	$97,478	$87,468
Federal funds purchased	142	16	1,463
Federal Home Loan Bank advances:			
FHLB-overnite	—	—	2,915
Fixed term – due in one year or less	5,479	1,520	3,589
Fixed term – due after one year	17,685	13,055	6,754
Debt:			
Loans due in one year or less	471	101	—
Junior subordinated debentures	20,620	20,620	20,620
Total	$158,145	$132,790	$122,809
Average interest rate during the period	0.36 %	0.30 %	0.68 %

Securities sold under agreements to repurchase increased $6.9 million during 2015 primarily due to agreements added with the acquisition of the twelve ONB Branches. FHLB advances represent borrowings by First Mid Bank to economically fund loan demand.

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At December 31, 2015 the advances totaling $20.0 million were as follows:

- $5 million advance with a 10-year maturity, at 4.58%, due July 14, 2016, one year lockout, callable quarterly
- $5 million advance with a 6-year maturity, at 2.30% due August 24, 2020
- $5 million advance with a 7-year maturity, at 2.55% due October 1, 2021
- $5 million advance with a 8-year maturity, at 2.4%, due January 9, 2023

At December 31, 2015 and 2014, there was no outstanding loan balance on a revolving credit agreement with The Northern Trust Company. This loan was renewed on April 17, 2015 for one year as a revolving credit agreement with a maximum available balance of $15 million. The interest rate is floating at 2.25% over the federal funds rate (2.5% at December 31, 2015). The loan is unsecured and subject to a borrowing agreement containing requirements for the Company and First Mid Bank, including requirements for operating and capital ratios. The Company and its subsidiary bank were in compliance with the existing covenants at December 31, 2015 and 2014.

On February 27, 2004, the Company completed the issuance and sale of $10 million of floating rate trust preferred securities through First Mid-Illinois Statutory Trust I ("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 Trust I, 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 (3.17% and 3.08% at December 31, 2015 and 2014, respectively), reset quarterly, and are callable at par, at the option of the Company, quarterly. 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 First Mid-Illinois Statutory Trust II ("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, bore interest at a fixed rate of 6.98% paid quarterly until June 15, 2011 and then converted to floating rate (LIBOR plus 160 basis points) after June 15, 2011 (2.11% and 1.84% at December 31, 2015 and 2014, respectively). The net proceeds to the Company were used for general corporate purposes, including the Company's acquisition of Mansfield Bancorp, Inc. in 2006.

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, 2010, 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 March 31, 2012. The application of the revised quantitative limits did not and is not expected to have a significant impact on its calculation of Tier 1 capital for regulatory purposes or its classification as well-capitalized. The Dodd-Frank Act, signed into law July 21, 2010, removes trust preferred securities as a permitted component of a holding company's Tier 1 capital after a three-year phase-in period beginning January 1, 2013 for larger holding companies. For holding companies with less than $15 billion in consolidated assets, existing issues of trust preferred securities are grandfathered and not subject to this new restriction. New issuances of trust preferred securities, however would not count as Tier 1 regulatory capital.

In addition to requirements of the Dodd-Frank Act discussed above, the act also required the federal banking agencies to adopt rules that prohibit banks and their affiliates from engaging in proprietary trading and investing in and sponsoring certain unregistered investment companies (defined as hedge funds and private equity funds). This rule is generally referred to as the "Volcker Rule." On December 10, 2013, the federal banking agencies issued final rules to implement the prohibitions required by the Volcker Rule. Following the publication of the final rule, and in reaction to concerns in the banking industry regarding the adverse impact the final rule's treatment of certain collateralized debt instruments has on community banks, the federal banking agencies approved a final rule to permit banking entities to retain interests in certain collateralized debt obligations backed primarily by trust preferred securities. Under the final rule, the agencies permit the retention of an interest in or sponsorship of covered funds by banking entities under $15 billion in assets if (1) the collateralized debt obligation was established and issued prior to May 19, 2010, (2) the banking entity reasonably believes that the offering proceeds received by the collateralized debt obligation were invested primarily in qualifying trust preferred collateral, and (3) the banking entity's interests in the collateralized debt obligation was acquired on or prior to December 10, 2013. Although the Volcker Rule impacts many large banking entities, the Company does not currently anticipate that the Volcker Rule will have a material effect on the operations of the Company or First Mid Bank.

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 interest-bearing assets differ significantly from the maturity or repricing characteristics of interest-bearing 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 GAP for selected maturity periods at December 31, 2015 (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	$73,214	$—	$—	$—	$—	$—	$73,214	$73,214
Certificates of deposit investments	25,000	—	—	—	—	—	25,000	25,056
Taxable investment securities	64	10,968	32,205	52,993	58,320	338,789	493,339	493,868
Nontaxable investment securities	455	945	301	2,566	1,255	105,195	110,717	110,717
Loans	584,274	244,117	170,906	103,736	95,803	83,053	1,281,889	1,280,670
Total	$683,007	$256,030	$203,412	$159,295	$155,378	$527,037	$1,984,159	$1,983,525
Interest-bearing liabilities:								
Savings and NOW accounts	$199,030	$43,721	$45,471	$64,722	$66,740	$396,990	$816,674	$816,674
Money market accounts	293,706	3,031	3,115	4,041	4,125	21,802	329,820	329,820
Other time deposits	174,257	32,141	19,096	8,033	8,717	1,194	243,438	243,333
Short-term borrowings/debt	128,842	—	—	—	—	—	128,842	128,843

Long-term borrowings/debt	25,620	—	—	—	5,000	10,000	40,620	33,629
Total	$821,455	$78,893	$67,682	$76,796	$84,582	$429,986	$1,559,394	$1,552,299
Rate sensitive assets – rate sensitive liabilities	$(138,448)	$177,137	$135,730	$82,499	$70,796	$97,051	$424,765	
Cumulative GAP	$(138,448)	$38,689	$174,419	$256,918	$327,714	$424,765		
Cumulative amounts as % of total Rate sensitive assets	-7.0%	8.9%	6.8%	4.2%	3.6%	4.9%		
Cumulative Ratio	-7.0%	1.9%	8.8%	12.9%	16.5%	21.4%		

The static GAP analysis shows that at December 31, 2015, the Company was liability sensitive, on a cumulative basis, through the twelve-month time horizon. This indicates that future increases in interest rates could have an adverse effect on net interest income.

There are several ways the Company measures and manages the exposure to interest rate sensitivity, including static GAP analysis. 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. The Company is currently experiencing downward pressure on asset yields resulting from the extended period of historically low interest rates and heightened competition for loans. A continuation of this environment could result in a decline in interest income and the net interest margin.

Capital Resources

At December 31, 2015, the Company’s stockholders' equity had increased $40.1 million, or 24.3%, to $205,009,000 from $164,916,000 as of December 31, 2014. The increase resulted primarily from the private placement capital raise completed during the second quarter of 2015 which resulted in additional common equity of $29.3 million. During 2015, net income contributed $16,512,000 to equity before the payment of dividends to stockholders. The change in market value of available-for-sale investment securities increased stockholders' equity by $1,296,000, net of tax. Additional purchases of treasury stock $53,246 shares (at an average cost of $20.01 per share) decreased stockholders’ equity by approximately $1,066,000.

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 Preferred Stock. Additionally, during 2011 and 2012, the Company sold to certain accredited investors including directors, executive officers, and certain major customers and holders of the Company’s common stock, $27,500,000, in the aggregate, of a newly authorized series of its preferred stock designated as Series C Preferred Stock. During 2014, the Company converted the Series B Preferred Stock to approximately 1,139,195 shares of common stock in accordance with the terms of the offering.

Stock Plans

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 710-10, for purposes of the First Mid-Illinois Bancshares, Inc. Deferred Compensation Plan (“DCP”). At December 31, 2015, the Company classified the cost basis of its common stock issued and held in trust in connection with the DCP of approximately $3,566,000 as treasury stock. The Company also classified the cost basis of its related deferred compensation obligation of approximately $3,566,000 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:

- 6,153 common shares during 2015
- 13,724 common shares during 2014, and
- 12,700 common shares during 2013

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:

- 11,885 common shares during 2015
- 8,971 common shares during 2014, and
- 9,747 common shares during 2013

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 $4,556,000 in common stock dividends paid during 2015, $1,069,000 or 23.5% was reinvested into shares of common stock of the Company through the DRIP. Of the $2,489,000 in preferred stock dividends paid during 2015, $198,000 or 8.0% was reinvested into shares of common stock through the DRIP. Events that resulted in common shares being reinvested in the DRIP:

- During 2015, 50,003 common shares were issued from common stock dividends and 9,714 common shares were issued from preferred stock dividends.
- During 2014, 43,969 common shares were issued from common stock dividends and 17,339 common shares were issued from preferred stock dividends.
- During 2013, 31,035 common shares were issued from common stock dividends and 15,885 common shares were issued from preferred 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.

On September 27, 2011, the Board of Directors passed a resolution authorizing and approving the Executive Long-Term Incentive Plan ("LTIP"). The LTIP was implemented to provide methodology for granting Stock Awards and Stock Unit Awards under the SI Plan to select senior executives of the Company or any subsidiary.

A maximum of 300,000 shares of common stock may be issued under the SI Plan. As of December 31, 2015, the Company had awarded 59,500 shares as stock options under the SI Plan. There were no shares awarded as stock options during 2015 or 2014. During 2015, the Company awarded 18,002 shares as stock unit awards. During 2014 the Company awarded 19,377 shares as 50% Stock Awards and 50% Stock Unit Awards under the SI Plan. This SI Plan is more fully described in Note 13 - Stock Incentive Plan.

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 $76.7 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.
- On February 22, 2011, repurchases of $5 million of additional shares of the Company's common stock.
- On November 13, 2012, repurchases of $5 million of additional shares of the Company's common stock.
- On November 19, 2013, repurchases of $5 million additional shares of the Company's common stock.
- On October 24, 2014, repurchases of $5 million additional shares of the Company's common stock.

During 2015, the Company repurchased 53,246 (0.63% of common shares) at a total price of $1,066,000. During 2014, the Company repurchased 82,680 (1.2% of common shares) at a total price of $1,763,000. As of December 31, 2015, approximately $7.2 million remains available for purchase under the repurchase programs. Treasury stock is further affected by activity in the DCP.

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Capital Ratios

Minimum regulatory requirements are 8% for the Total Risk-based capital ratio, 6% for the Tier 1 Risk-based capital ratio, 4.5% for the Common Equity Tier 1 capital ratio, and 4% for the Tier 1 Leverage ratio. The Company and First Mid Bank have capital ratios above the minimum regulatory capital requirements and, as of December 31, 2015, 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, 2015 follows:

	Total Risk-based Capital Ratio		Tier One Risk-based Capital Ratio		Common Equity Tier 1 Capital Ratio		Tier One Leverage Ratio (Capital to Average Assets)	
First Mid-Illinois Bancshares, Inc. (Consolidated)	14.25	%	13.23	%	9.92	%	9.20	%
First Mid-Illinois Bank & Trust, N.A.	13.75	%	12.73	%	12.73	%	8.83	%

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 of cash include overnight federal fund lines, Federal Home Loan Bank advances, the ability to borrow at the Federal Reserve Bank of Chicago, and the Company's operating line of credit with The Northern Trust Company. Details for these sources include:

- First Mid Bank has $35 million available in overnight federal fund lines, including $10 million from U.S. Bank, N.A., $10 million from Wells Fargo Bank, N.A. and $15 million from The Northern Trust Company. Availability of the funds is subject to First Mid Bank meeting minimum regulatory capital requirements for total capital to risk-weighted assets and Tier 1 capital to total average assets. As of December 31, 2015, First Mid Bank met these regulatory requirements.

- First Mid Bank can borrow from the Federal Home Loan Bank as a source of liquidity. Availability of the funds is subject to the pledging of collateral to the Federal Home Loan Bank. Collateral that can be pledged includes one-to-four family residential real estate loans and securities. At December 31, 2015, the excess collateral at the FHLB would support approximately $123.5 million of additional advances.

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

- In addition, as of December 31, 2015, the Company had a revolving credit agreement in the amount of $15 million with The Northern Trust Company with an outstanding balance of zero and $15 million in available funds. This loan was renewed on April 17, 2015 for one year as a revolving credit agreement. The interest rate 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, including requirements for operating and capital ratios. The Company and its subsidiary bank were in compliance with the existing covenants at December 31, 2015 and 2014.

Management continues to monitor 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 provisions on U.S. Treasury and government agency securities; and
- operating activities, including scheduled debt repayments and dividends to stockholders.

The following table summarizes significant contractual obligations and other commitments at December 31, 2015 (in thousands):

	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Time deposits	$243,438	$167,359	$53,116	$21,665	$1,298
Debt	20,620	—	—	—	20,620
Other borrowings	148,842	133,842	15,000	—	—
Operating leases	48,308	2,594	5,001	4,028	36,685
Supplemental retirement	715	100	200	123	292
	$461,923	$303,895	$73,317	$25,816	$58,895

For the year ended December 31, 2015, net cash of $22.0 million was provided from operating activities, $10.4 million was provided from investing activities, and $31.7 million was provided from financing activities. In total cash and cash equivalents increased by $64.1 million since year-end 2014.

For the year ended December 31, 2014, net cash of $17.8 million was provided from operating activities, $10.0 million was used in investing activities, and $21.1 million was used in financing activities. In total cash and cash equivalents increased by $13.4 million since year-end 2013.

For the year ended December 31, 2013, net cash of $24.7 million was provided from operating activities, $67.1 million was used in investing activities, and $24.9 million was provided from financing activities. In total cash and cash equivalents increased by $1.0 million since year-end 2012.

For the years ended December 31, 2015 and 2014, the Company also had $10 million of floating rate trust preferred securities outstanding through each of Trust I and Trust II. See Note 9 – “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

Accounting Standards Update 2014-09, Revenue from Contracts with Customers (Topic 606): Revenue from Contracts with Customers ("ASU 2014-09"). In May 2014, FASB issued ASU 2014-09 which creates a new topic in the FASB Accounting Standards Codification(R) ("ASC"), Topic 606. In addition to superseding and replacing nearly all existing U.S. GAAP revenue recognition guidance, including industry-specific guidance, ASU 2014-09 establishes a new control-based revenue recognition model, changes the basis for deciding when revenue is recognized over time or at a point in time, provides new and more detailed guidance on specific topics and expands and improves disclosures about revenue. In addition, ASU 2014-09 adds a new Subtopic to the ASC, Other Assets and Deferred Costs: Contracts with Customers ("ASC 340-40"), to provide guidance on costs related to obtaining a contract with a customer and costs incurred in fulfilling a contract with a customer that are not in the scope of another ASC Topic. The new guidance does not apply to certain contracts within the scope of other ASC Topics, such as lease contracts, insurance contracts, financing arrangements, financial instruments, guarantee other than product or service warranties, and non-monetary exchanges between entities in the same line of business to facilitate sales to customers. The amendments are effective for annual periods and interim periods within those annual periods beginning after December 15, 2016. The adoption of this guidance is not expected to have a material impact on the Company’s financial statements.

Accounting Standards Update 2014-11, Transfers and Servicing (Topic 860): Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures ("ASU 2014-11"). In June 2014, FASB issued ASU 2014-11 which changes the accounting for repurchase-to-maturity transactions and repurchase financing arrangements to secured borrowing accounting. ASU 2014-11 also requires enhanced disclosures about repurchase agreements and other similar

transactions. The accounting changes in this update are effective for the first interim or annual period beginning after December 31, 2014. The disclosure for transactions accounted for as a sale is effective for the first interim or annual period beginning on or after December 15, 2014; the disclosure for transactions accounted for as secured borrowings is required to be presented for annual periods after December 15, 2014, and interim periods after March 15, 2015. Early application is not permitted. The adoption of this amendment did not have a material effect on the Company's financial statements.

Accounting Standards Update 2016-01, Financial Instruments (Topic 825): Recognition and Measurement of Financial Assets and Financial Liabilities ("ASU 2016-01"). In January 2016, FASB issued ASU 2016-01 which amends prior guidance to require an entity to measure its equity investments (except those accounted for under the equity method of accounting) to be measured at fair value with changes in fair value recognized in net income. An entity may choose to measure equity investments that do not have readily determinable fair values at cost minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or similar investment of same issuer. The new guidance simplifies the impairment assessment of equity investments without readily determinable fair values, requires public entities to use the exit price notion when measuring fair value of financial instruments for disclosure purposes, requires an entity to present separately in other comprehensive income the portion of the total change in fair value of a liability resulting from changes in the instrument-specific credit risk when the entity has selected fair value option for financial instruments and requires separate presentation of financial assets and liabilities by measurement category and form of financial asset. The new guidance will be effective for reporting periods after January 1, 2018 and is not expected to have a significant impact on the Company's financial statements.

Accounting Standards Update 2016-02, Leases (Topic 842)("ASU 2016-02"). On February 25, 2016, FASB issued ASU 2016-02 which creates Topic 842, Leases and supersedes Topic 840, Leases. ASU 2016-02 is intended to improve financial reporting about leasing transactions, by increasing transparency and comparability among organizations. Under the new guidance, a lessee will be required to all leases with lease terms of more than 12 months on their balance sheet as lease liabilities with a corresponding right-of-use asset. ASU 2016-02 maintains the dual model for lease accounting, requiring leases to be classified as either operating or finance, with lease classification determined in a manner similar to existing lease guidance. The new guidance will be effective for public companies for fiscal years beginning on or after December 15, 2018, and for private companies for fiscal years beginning on or after December 15, 2019. Early adoption is permitted for all entities. Managerment is evaluating the impact ASU 2016-02 will have on the Company's financial statements.

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, 2015, 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, 2015	Net Interest Income				Return On Average Equity	
Prime rate is 3.25%	($000)		(%)		2015=8.80%	
Prime rate increase of:						
200 basis points to 5.25%	$(1,825	)	(4.2	)%	0.85	%
100 basis points to 4.25%	(916	)	(2.1	)%	0.42	%
Prime rate decrease of:						
100 basis points to 2.25%	(2,861	)	(6.5	)%	(1.3	)%
200 basis points to 1.25%	(5,402	)	(12.3	)%	(2.6	)%

The following table shows the same analysis performed as of December 31, 2014:

	Increase (Decrease) In					
December 31, 2014	Net Interest Income				Return On Average Equity	
Prime rate is 3.25%	($000)		(%)		2014=9.67%	
Prime rate increase of:						
200 basis points to 5.25%	$(2,399	)	(6.9	)%	(1.28	)%
100 basis points to 4.25%	(1,271	)	(3.6	)%	(0.68	)%
Prime rate decrease of:						
100 basis points to 2.25%	(1,237	)	(3.6	)%	(0.66	)%
200 basis points to 1.25%	(2,582	)	(7.4	)%	(1.38	)%

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 income 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 EVE. 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, 2015 and 2014 (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	Economic Value of Equity	
	Interest Rates (basis points)	Amount of Change ($000)	Percent of Change
December 31, 2015	+200 bp	$(17,340)	(5.5)%
	+100 bp	(6,789)	(2.1)%
	-200 bp	(71,013)	(22.4)%
	-100 bp	(29,468)	(9.3)%
December 31, 2014	+200 bp	(18,519)	(7.6)%
	+100 bp	(8,764)	(3.6)%
	-200 bp	(40,167)	(16.5)%
	-100 bp	(13,453)	(5.5)%

As indicated above, at December 31, 2015, in the event of a sudden and sustained increase in prevailing market interest rates, First Mid Bank's EVE would be expected to decrease if rates increased 100 or 200 basis points. 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, 2015, 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. At December 31, 2015, First Mid Bank slightly exceeded policy guidelines for a decrease in interest rates of 200 basis points. The general level of interest rates are at historically low levels and the bank is monitoring its position and the likelihood of further rate decreases.

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.

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ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Consolidated Balance Sheets

December 31, 2015 and 2014

(In thousands, except share data)	2015	2014
Assets		
Cash and due from banks:		
Non-interest bearing	$42,570	$40,716
Interest bearing	72,722	10,520
Federal funds sold	492	494
Cash and cash equivalents	115,784	51,730
Certificates of deposit investments	25,000	—
Investment securities:		
Available-for-sale, at fair value	518,848	377,856
Held-to-maturity, at amortized cost (estimated fair value of $85,737 at December 31, 2015 and $53,937 at December 31, 2014)	85,208	53,650
Loans held for sale	968	1,958
Loans	1,280,921	1,060,448
Less allowance for loan losses	(14,576)	(13,682)
Net loans	1,266,345	1,046,766
Interest receivable	8,085	6,828
Other real estate owned	477	263
Premises and equipment, net	31,340	27,352
Goodwill, net	41,007	25,753
Intangible assets, net	8,997	1,844
Other assets	12,440	13,103
Total assets	$2,114,499	$1,607,103
Liabilities and Stockholders' Equity		
Deposits:		
Non-interest bearing	$342,636	$222,116
Interest bearing	1,389,932	1,049,961
Total deposits	1,732,568	1,272,077
Repurchase agreements with customers	128,842	121,869
Interest payable	356	285
Other borrowings	20,000	20,000
Junior subordinated debentures	20,620	20,620
Dividends payable	550	530
Other liabilities	6,554	6,806
Total liabilities	1,909,490	1,442,187
Stockholders' Equity:		
Convertible preferred stock, no par value; authorized 1,000,000 shares; issued 5,500 shares in 2015 and 2014	27,400	27,400
Common stock, $4 par value; authorized 18,000,000 shares; issued 9,003,710 shares in 2015 and 7,529,815 shares in 2014	38,015	32,119
Additional paid-in capital	79,626	55,607
Retained earnings	71,712	61,956
Deferred compensation	3,245	3,329
Accumulated other comprehensive income (loss)	723	(875)
Less treasury stock at cost, 549,743 shares in 2015 and 496,497 shares in 2014	(15,712)	(14,620)

Total stockholders’ equity	205,009	164,916
Total liabilities and stockholders’ equity	$2,114,499	$1,607,103

See accompanying notes to consolidated financial statements.

Consolidated Statements of Income
For the years ended December 31, 2015, 2014 and 2013

(In thousands, except per share data)	2015	2014	2013
Interest income:			
Interest and fees on loans	$48,460	$44,799	$42,184
Interest on investment securities:			
Taxable	7,741	7,499	9,153
Exempt from federal income tax	2,807	2,352	2,069
Interest on certificates of deposit investments	44	—	14
Interest on federal funds sold	—	1	6
Interest on deposits with other financial institutions	199	83	33
Total interest income	59,251	54,734	53,459
Interest expense:			
Interest on deposits	2,282	2,351	2,703
Interest on securities sold under agreements to repurchase	62	47	46
Interest on FHLB borrowings	616	339	254
Interest on other borrowings	13	1	9
Interest on subordinated debentures	526	514	523
Total interest expense	3,499	3,252	3,535
Net interest income	55,752	51,482	49,924
Provision for loan losses	1,318	629	2,193
Net interest income after provision for loan losses	54,434	50,853	47,731
Other income:			
Trust revenues	3,746	3,571	3,565
Brokerage commissions	1,315	1,039	833
Insurance commissions	2,107	1,796	1,638
Service charges	5,681	5,264	4,865
Securities gains, net	452	715	2,293
Mortgage banking revenue, net	754	596	935
ATM / debit card revenue	4,676	3,915	3,772
Other income	1,813	1,473	1,440
Total other income	20,544	18,369	19,341
Other expense:			
Salaries and employee benefits	26,337	24,771	24,128
Net occupancy and equipment expense	9,143	8,347	8,223
Net other real estate owned expense	19	23	163
FDIC insurance expense	904	804	832
Amortization of intangible assets	891	643	674
Stationery and supplies	681	646	603
Legal and professional	2,474	2,333	2,070
Marketing and donations	1,092	1,015	1,221
Other expense	7,707	5,925	5,590
Total other expense	49,248	44,507	43,504
Income before income taxes	25,730	24,715	23,568
Income taxes	9,218	9,254	8,846
Net income	16,512	15,461	14,722
Dividends on preferred shares	2,200	4,152	4,417