OLD NATIONAL BANCORP /IN/
Form 10-K
February 26, 2013
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

Annual Report Pursuant to Section 13 or 15(d)

Of the Securities Exchange Act of 1934

For the fiscal year ended December 31, 2012

Commission File Number 1-15817

OLD NATIONAL BANCORP

(Exact name of the Registrant as specified in its charter)

INDIANA	**35-1539838**
(State or other jurisdiction of	**(I.R.S. Employer**

incorporation or organization)	**Identification No.)**
One Main Street	
Evansville, Indiana	**47708**
(Address of principal executive offices)	**(Zip Code)**

(812) 464-1294

(Registrant s telephone number, including area code)

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

Title of Each Class	Name of each exchange on which registered
Common Stock, No Par Value	**New York Stock Exchange**
Preferred Stock Purchase Rights	

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 ¨ No x

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (s232.405 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 (s229.405 of this chapter) is not contained herein, and will not be contained, to the best of the Registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ¨

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

Large accelerated filer x	Accelerated filer ¨
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes ¨ No x

The aggregate market value of the Registrant s voting common stock held by non-affiliates on June 30, 2012, was $1,102,329,460 (based on the closing price on that date of $12.01). In calculating the market value of securities held by non-affiliates of the Registrant, the Registrant has treated as securities held by affiliates as of June 30, 2012, voting stock owned of record by its directors and principal executive officers, and voting stock held by the Registrant s trust department in a fiduciary capacity for benefit of its directors and principal executive officers. This calculation does not reflect a determination that persons are affiliates for any other purposes.

The number of shares outstanding of the Registrant s common stock, as of January 31, 2013, was 101,184,000.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the Annual Meeting of Shareholders to be held May 9, 2013, are incorporated by reference into Part III of this Form 10-K.

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FORWARD-LOOKING STATEMENTS

In this report, we have made various statements regarding current expectations or forecasts of future events, which speak only as of the date the statements are made. These statements are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements are also made from time-to-time in press releases and in oral statements made by the officers of Old National Bancorp (Old National, or the Company). Forward-looking statements are identified by the words expect, may, could, intend, project, believe , anticipate and similar expressions. Forward-looking statements also include, but are not limited to, statements regarding estimated cost savings, plans and objectives for future operations, the Company s business and growth strategies, including future acquisitions of banks, regulatory developments, and expectations about performance as well as economic and market conditions and trends.

Such forward-looking statements are based on assumptions and estimates, which although believed to be reasonable, may turn out to be incorrect. Therefore, undue reliance should not be placed upon these estimates and statements. We can not assure that any of these statements, estimates, or beliefs will be realized and actual results may differ from those contemplated in these forward-looking statements. We undertake no obligation to publicly update any forward-looking statements, whether as a result of new information, future events, or otherwise. You are advised to consult further disclosures we may make on related subjects in our filings with the SEC. In addition to other factors discussed in this report, some of the important factors that could cause actual results to differ materially from those discussed in the forward-looking statements include the following:

- economic, market, operational, liquidity, credit and interest rate risks associated with our business;
- economic conditions generally and in the financial services industry;
- expected cost savings in connection with the consolidation of recent acquisitions may not be fully realized or realized within the expected time frames, and deposit attrition, customer loss and revenue loss following completed acquisitions may be greater than expected;
- unexpected difficulties and losses related to FDIC-assisted acquisitions, including those resulting from our loss-sharing arrangements with the FDIC;
- increased competition in the financial services industry either nationally or regionally, resulting in, among other things, credit quality deterioration;
- our ability to achieve loan and deposit growth;
- volatility and direction of market interest rates;
- governmental legislation and regulation, including changes in accounting regulation or standards;
- our ability to execute our business plan;

a weakening of the economy which could materially impact credit quality trends and the ability to generate loans;

changes in the securities markets; and

changes in fiscal, monetary and tax policies.

Investors should consider these risks, uncertainties and other factors in addition to risk factors included in our other filings with the SEC.

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PART I

ITEM 1. BUSINESS

GENERAL

Old National is a financial holding company incorporated in the State of Indiana and maintains its principal executive office in Evansville, Indiana. We, through our wholly owned banking subsidiary, provide a wide range of services, including commercial and consumer loan and depository services, investment and brokerage services, lease financing and other traditional banking services. Through our non-bank affiliates, we provide services to supplement the banking business including fiduciary and wealth management services, insurance and other financial services. As of December 31, 2012, we employed 2,684 full-time equivalent associates.

COMPANY PROFILE

Old National Bank, our wholly owned banking subsidiary (Old National Bank), was founded in 1834 and is the oldest company in Evansville, Indiana. In 1982, Old National was formed; in 2001 we became a financial holding company and we are currently the largest financial holding company headquartered in the state of Indiana. Also in 2001, we completed the consolidation of 21 bank charters enabling us to operate under a common name with consistent product offerings throughout the financial center locations, consolidating back-office operations and allowing us to provide more convenient service to clients. We provide financial services primarily in Indiana, eastern and southeastern Illinois, and central and western Kentucky.

OPERATING SEGMENTS

We operate in two segments: community banking and treasury. Substantially all of our revenues are derived from customers located in, and substantially all of our assets are located in, the United States. A description of each segment follows.

Community Banking Segment

The community banking segment operates through Old National Bank, and has traditionally been the most significant contributor to our revenue and earnings. The primary goal of the community banking segment is to provide products and services that address clients needs and help clients reach their financial goals by offering a broad array of quality services. Our financial centers focus on convenience factors such as location, space for private consultations and quick client access to routine transactions.

As of December 31, 2012, Old National Bank operated 180 banking financial centers located primarily in Indiana, Illinois, and Kentucky. The community banking segment primarily consists of lending and depository activities along with merchant cash management, internet banking and other services relating to the general banking business. In addition, the community banking segment includes Indiana Old National Insurance Company (IONIC), which reinsures credit life insurance. IONIC also provides property and casualty insurance for Old National and reinsures most of the coverage with non-affiliated carriers.

Lending Activities

We earn interest income on loans as well as fee income from the origination of loans. Lending activities include loans to individuals which primarily consist of home equity lines of credit, residential real estate loans and consumer loans, and loans to commercial clients, which include commercial loans, commercial real estate loans, letters of credit and lease financing. Residential real estate loans are either kept in our loan portfolio or sold to secondary investors, with gains or losses from the sales being recognized.

Depository Activities

We strive to serve individuals and commercial clients by providing depository services that fit their needs at competitive rates. We pay interest on the interest-bearing deposits and receive service fee revenue on various accounts. Deposit accounts include products such as noninterest-bearing demand, negotiable order of withdrawal (NOW), savings and money market, and time deposits. Debit and ATM cards provide clients with access to their accounts 24 hours a day at any ATM location. We also provide 24-hour telephone access and online banking as well as other electronic banking services.

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Investment and Brokerage Services

We, through a registered third party broker-dealer, provide clients with convenient and professional investment services and a variety of brokerage products. This line of business offers a full array of investment options and investment advice to its clients.

Treasury Segment

Treasury manages investments, wholesale funding, interest rate risk, liquidity and leverage for Old National. Treasury also provides capital markets products, including interest rate derivatives, foreign exchange and industrial revenue bond financing for our commercial clients.

Other

The following lines of business are included in the other column for all periods reported:

Wealth Management

Fiduciary and trust services targeted at high net worth individuals are offered through an affiliate trust company under the business name of Old National Trust Company.

Insurance Agency Services

Through our insurance agency subsidiaries, we offer full-service insurance brokerage services including commercial property and casualty, surety, loss control services, employee benefits consulting and administration, and personal insurance. These subsidiaries are insurance agencies that offer products that are issued and underwritten by various insurance companies not affiliated with us.

Purchased Credit Impaired Loans

For internal reporting, purchased credit impaired loans and the associated FDIC indemnification asset reside in the special assets department and are included in the Other segment.

Additional information about our business segments is included in Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations, and Note 23 to the consolidated financial statements.

MARKET AREA

We own the largest Indiana-based bank and one of the largest independent insurance agencies headquartered in Indiana. Operating from a home base in Evansville, Indiana, we have continued to grow our footprint in Indiana and Kentucky with continued expansion in the attractive Louisville, Indianapolis and Lafayette markets. In February 2007, we expanded into Northern Indiana by acquiring St. Joseph Capital Corporation, which had banking offices in Mishawaka and Elkhart, Indiana. In March 2009, we completed the acquisition of the Indiana retail branch banking network of Citizens Financial Group, which consisted of 65 branches and a training facility. The branches are located primarily in the Indianapolis area. On January 1, 2011, we closed on our acquisition of Monroe Bancorp, strengthening our presence in Bloomington, Indiana and the central and south central Indiana markets. On July 29, 2011, we acquired the banking operations of Integra Bank N.A. in an FDIC-assisted transaction. Integra Bank was a full service community bank headquartered in Evansville, Indiana that operated 52 branch locations, primarily in southwest Indiana, southeastern Illinois and western Kentucky. On September 15, 2012, we closed on our acquisition of Indiana Community Bancorp, strengthening our presence in Columbus, Indiana and the south central Indiana market.

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The following table reflects the market locations where we have a significant share of the deposit market. The market share data is by metropolitan statistical area. The Evansville, Indiana data includes branches in Henderson, Kentucky. The data includes deposit information for Indiana Community Bancorp, which was acquired on September 15, 2012.

Old National Deposit Market Share and Number of Branch Locations

Deposits as of June 30, 2012

Market Location	Number of Branches	Deposit Market Share Rank
Evansville, Indiana	20	1
Bloomington, Indiana	9	1
Central City, Kentucky	4	1
Danville, Illinois	2	1
North Vernon, Indiana	1	1
Vincennes, Indiana	4	2
Washington, Indiana	3	2
Columbus, Indiana	7	2
Jasper, Indiana	7	2
Terre Haute, Indiana	6	2
Seymour, Indiana	3	2
Carbondale, Illinois	4	3
Madison, Indiana	1	3

Source: FDIC

ACQUISITION AND DIVESTITURE STRATEGY

Since the formation of Old National in 1982, we have acquired more than 40 financial institutions and financial services companies. Future acquisitions and divestitures will be driven by a disciplined financial process and will be consistent with the existing focus on community banking, client relationships and consistent quality earnings. Targeted geographic markets for acquisitions include mid-size markets within or near our existing franchise with average to above average growth rates.

As with previous acquisitions, the consideration paid by us will be in the form of cash, debt or Old National stock. The amount and structure of such consideration is based on reasonable growth and cost savings assumptions and a thorough analysis of the impact on both long- and short-term financial results.

On January 1, 2011, we acquired Monroe Bancorp in an all stock transaction. Monroe Bancorp was headquartered in Bloomington, Indiana and had 15 banking centers. Pursuant to the merger agreement, the shareholders of Monroe Bancorp received approximately 7.6 million shares of Old National Bancorp stock valued at approximately $90.1 million. On January 1, 2011, unaudited financial statements of Monroe Bancorp showed assets of $808.1 million, which included $509.6 million of loans, $166.4 million of securities and $711.5 million of deposits. The acquisition strengthens our deposit market share in the Bloomington, Indiana market and improved our deposit market share rank to first place in 2011.

On June 1, 2011, Old National Bancorp s wholly owned trust subsidiary, American National Trust and Investment Management Company d/b/a Old National Trust Company (ONTC), acquired the trust business of Integra Bank, N.A. As of the closing, the trust business had approximately $328 million in assets under management. Old National paid Integra $1.3 million in an all cash transaction.

On July 29, 2011, Old National acquired the banking operations of Integra Bank N.A. (Integra) in an FDIC- assisted transaction. Integra was a full service community bank headquartered in Evansville, Indiana that operated 52 branch locations. As part of the purchase and assumption agreement, the Company and the FDIC entered into loss sharing agreements (each, a loss sharing agreement and collectively, the loss sharing agreements), whereby the FDIC will cover a substantial portion of any future losses on loans (and related unfunded commitments), other real estate owned (OREO) and up to 90 days of certain accrued interest on loans. The acquired loans and OREO subject to the loss sharing agreements are referred to collectively as covered assets. Under the terms of the loss sharing agreements, the FDIC will reimburse Old National for 80% of losses up to $275.0 million, losses in excess of $275.0 million up to $467.2 million at 0% reimbursement, and 80% of losses in excess of $467.2 million. As of December 31, 2012, we do not expect losses to exceed $275.0 million. Old National will reimburse the FDIC for its share of recoveries with respect to losses for which the FDIC has reimbursed the Bank under the loss sharing agreements. The loss sharing provisions of the agreements for commercial and single family residential mortgage loans are in effect for five and ten years, respectively, from the July 29, 2011 acquisition date and the loss recovery provisions for such loans are in effect for eight years and ten years, respectively, from the acquisition date.

On September 15, 2012, Old National acquired Indiana Community Bancorp in an all stock transaction. Indiana Community Bancorp was headquartered in Columbus, Indiana and had 17 full-service banking centers serving the South Central Indiana area. Pursuant to the merger agreement, the shareholders of Indiana Community Bancorp received approximately 6.6 million shares of Old National Bancorp common stock valued at approximately $88.5 million. Old National assumed assets with a fair value of approximately $906.3 million, including $497.4 million of loans and $784.6 million of deposits. The acquisition strengthened our deposit market share in Columbus, Indiana and south central Indiana market.

COMPETITION

The banking industry and related financial service providers operate in a highly competitive market. Old National competes with financial service providers such as local, regional and national banking institutions, savings and loan associations, credit unions, finance companies, investment brokers, and mortgage banking companies. In addition, Old National s non-bank services face competition with asset managers and advisory services, money market and mutual fund companies and insurance agencies.

SUPERVISION AND REGULATION

Old National is subject to extensive regulation under federal and state laws. The regulatory framework is intended primarily for the protection of depositors, federal deposit insurance funds and the banking system as a whole and not for the protection of shareholders and creditors.

Significant elements of the laws and regulations applicable to Old National and its subsidiaries are described below. The description is qualified in its entirety by reference to the full text of the statutes, regulations and policies that are described. Also, such statutes, regulations and policies are continually under review by Congress and state legislatures and federal and state regulatory agencies. A change in statutes, regulations or regulatory policies applicable to Old National and its subsidiaries could have a material effect on the business of the Company.

The Dodd-Frank Act

On July 21, 2010, financial regulatory reform legislation entitled the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) was signed into law. The Dodd-Frank Act implements far-reaching changes across the financial regulatory landscape, including provisions that, among other things, will:

- Centralize responsibility for consumer financial protection by creating a new agency, the Consumer Financial Protection Bureau, responsible for implementing, examining and enforcing compliance with federal consumer financial laws.
- Restrict the preemption of state law by federal law and disallow subsidiaries and affiliates of national banks, such as Old National Bank, from availing themselves of such preemption.
- Apply the same leverage and risk-based capital requirements that apply to insured depository institutions to most bank holding companies.

Require the Office of the Comptroller of the Currency to seek to make its capital requirements for national banks, such as Old National Bank, countercyclical so that capital requirements increase in times of economic expansion and decrease in times of economic contraction.

Require financial holding companies to be well capitalized and well managed. Bank holding companies and banks must also be both well capitalized and well managed in order to acquire banks located outside their home state.

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Change the assessment base for federal deposit insurance from the amount of insured deposits to consolidated assets less tangible capital, eliminate the ceiling on the size of the Deposit Insurance Fund (DIF) and increase the floor on the size of the DIF.

Impose comprehensive regulation of the over-the-counter derivatives market, which would include certain provisions that would effectively prohibit insured depository institutions from conducting certain derivatives businesses in the institution itself.

Require large, publicly traded bank holding companies to create a risk committee responsible for the oversight of enterprise risk management.

Implement corporate governance revisions, including with regard to executive compensation and proxy access by shareholders, that apply to all public companies, not just financial institutions.

Make permanent the $250,000 limit for federal deposit insurance and increase the cash limit of Securities Investor Protection Corporation protection from $100,000 to $250,000.

Repeal the federal prohibitions on the payment of interest on demand deposits, thereby permitting depository institutions to pay interest on business transaction accounts as well as other accounts.

Amend the Electronic Fund Transfer Act (EFTA) to, among other things, give the Federal Reserve the authority to establish rules regarding interchange fees charged for electronic debit transactions by payment card issuers having assets over $10 billion and to enforce a new statutory requirement that such fees be reasonable and proportional to the actual cost of a transaction to the issuer.

The Dodd-Frank Act also creates a new Bureau of Consumer Financial Protection (the CFPB) that is responsible for administering federal consumer financial protection laws. The CFPB, which began operations on July 21, 2011, is an independent bureau within the FRB and has broad rule-making, supervisory and examination authority to set and enforce rules in the consumer protection area over financial institutions that have assets of $10.0 billion or more. The Dodd-Frank Act also gives the CFPB expanded data collecting powers for fair lending purposes for both small business and mortgage loans, as well as expanded authority to prevent unfair, deceptive and abusive practices. The consumer complaint function will also be consolidated into the CFPB.

Many aspects of the Dodd-Frank Act are subject to rulemaking and will take effect over several years, making it difficult to anticipate the overall financial impact on Old National, its customers or the financial industry more generally. However, several provisions of the Dodd-Frank Act have been implemented. In addition to the establishment of the CFPB, the FRB final rule implementing the Dodd-Frank Act s Durbin Amendment, which limits debit card interchange fees, was issued on July 21, 2011 for transactions occurring after September 30, 2011. The final rule established a cap on the fees banks with more than $10 billion in assets can charge merchants for debit card transactions. The fee was set at $0.21 per transaction plus an additional 5 bps of the transaction amount and $0.01 to cover fraud losses. The FRB repealed Regulation Q as mandated by the Dodd-Frank Act on July 21, 2011. Regulation Q was implemented as part of the Glass-Steagall Act in the 1930 s and provided a prohibition against the payment of interest on demand deposits.

While the total impact of the fully implemented Dodd-Frank Act on Old National is not currently known, the impact is expected to be substantial and may have an adverse impact on its financial performance and growth opportunities. Provisions in the legislation that affect the payment of interest on demand deposits and interchange fees are likely to increase the costs associated with deposits as well as place limitations on certain revenues those deposits may generate. Provisions in the legislation that revoke the Tier 1 capital treatment of trust preferred securities and otherwise require revisions to the capital requirements of Old National and Old National Bank could require Old National and Old National Bank to seek other sources of capital in the future.

Other Regulatory Agencies and Requirements

Old National is registered as a bank holding company and has elected to be a financial holding company. It is subject to the supervision of, and regulation by, the Board of Governors of the Federal Reserve System (Federal Reserve) under the Bank Holding Company Act of 1956, as amended (BHC Act). The Federal Reserve has issued regulations under the BHC Act requiring a bank holding company to serve as a source of financial and managerial strength to its subsidiary banks. It is the policy of the Federal Reserve that, pursuant to this requirement, a bank holding company should stand ready to use its resources to provide adequate capital funds to its subsidiary banks during periods of financial stress or adversity.

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The BHC Act requires the prior approval of the Federal Reserve to acquire more than a 5% voting interest of any bank or bank holding company. Additionally, the BHC Act restricts Old National s non-banking activities to those which are determined by the Federal Reserve to be closely related to banking and a proper incident thereto.

On October 26, 2001, the USA Patriot Act of 2001 was signed into law. Enacted in response to the terrorist attacks in New York, Pennsylvania and Washington, D.C. on September 11, 2001, the Patriot Act is intended to strengthen U.S. law enforcement s and the intelligence community s ability to work cohesively to combat terrorism on a variety of fronts. The Patriot Act contains sweeping anti-money laundering and financial transparency laws and the statute and regulations promulgated under it impose a number of significant obligations on entities subject to its provisions, including: (a) due diligence requirements for financial institutions that administer, maintain, or manage private bank accounts or correspondent accounts for non-U.S. persons; (b) standards for verifying customer identification at account opening; (c) rules to promote cooperation among financial institutions, regulators and law enforcement entities in identifying parties that may be involved in terrorism or money laundering; (d) reports by non-financial trades and businesses filed with the U.S. Treasury Department s (the Treasury Department or the Treasury) Financial Crimes Enforcement Network for transactions exceeding $10,000; and (e) filing of suspicious activities reports by brokers and dealers if they believe a customer may be violating U.S. laws and regulations.

Under the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA), a bank holding company is required to guarantee the compliance of any insured depository institution subsidiary that may become undercapitalized (as defined in FDICIA) with the terms of any capital restoration plan filed by such subsidiary with its appropriate federal bank regulatory agency.

Bank holding companies are required to comply with the Federal Reserve s risk-based capital guidelines. The Federal Deposit Insurance Corporation (FDIC) and the Office of the Comptroller of the Currency (OCC) have adopted risk-based capital ratio guidelines to which depository institutions under their respective supervision are subject. The guidelines establish a systematic analytical framework that makes regulatory capital requirements more sensitive to differences in risk profiles among banking organizations. Risk-based capital ratios are determined by allocating assets and specified off-balance sheet commitments to four risk-weighted categories, with higher levels of capital being required for the categories perceived as representing greater risk. Old National s banking affiliate, Old National Bank, met all risk-based capital requirements of the FDIC and OCC as of December 31, 2012. For Old National s regulatory capital ratios and regulatory requirements as of December 31, 2012, see Note 21 to the consolidated financial statements.

In December 2010 and January 2011, the Basel Committee on Banking Supervision published the final texts of reforms on capital and liquidity generally referred to as Basel III. Although Basel III is intended to be implemented by participating countries for large, internationally active banks, its provisions are likely to be considered by United States banking regulators in developing new regulations applicable to other banks in the United States, including Old National Bank.

For banks in the United States, among the most significant provisions of Basel III concerning capital are the following:

A minimum ratio of common equity to risk-weighted assets reaching 4.5%, plus an additional 2.5% as a capital conservation buffer, by 2019 after a phase-in period.

A minimum ratio of Tier 1 capital to risk-weighted assets reaching 6.0% by 2019 after a phase-in period.

A minimum ratio of total capital to risk-weighted assets, plus the additional 2.5% capital conservation buffer, reaching 10.5% by 2019 after a phase -in period.

An additional countercyclical capital buffer to be imposed by applicable national banking regulators periodically at their discretion, with advance notice.

Restrictions on capital distributions and discretionary bonuses applicable when capital ratios fall within the buffer zone.

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Deduction from common equity of deferred tax assets that depend on future profitability to be realized.

Increased capital requirements for counterparty credit risk relating to OTC derivatives, repos and securities financing activities.

For capital instruments issued on or after January 13, 2013 (other than common equity), a loss-absorbency requirement such that the instrument must be written off or converted to common equity if a trigger event occurs, either pursuant to applicable law or at the direction of the banking regulator. A trigger event is an event under which the banking entity would become nonviable without the write-off or conversion, or without an injection of capital from the public sector. The issuer must maintain authorization to issue the requisite shares of common equity if conversion were required.

The Basel III provisions on liquidity include complex criteria establishing a liquidity coverage ratio (LCR) and a net stable funding ratio (NSFR). The purpose of the LCR is to ensure that a bank maintains adequate unencumbered, high quality liquid assets to meet its liquidity needs for 30 days under a severe liquidity stress scenario. The purpose of the NSFR is to promote more medium and long-term funding of assets and activities, using a one-year horizon. Although Basel III is described as a final text, it is subject to the resolution of certain issues and to further guidance and modification, as well as to adoption by United States banking regulators.

When fully phased in on January 1, 2019, Basel III requires banks to maintain the following new standards and introduces a new capital measure Common Equity Tier 1 , or CET1 . Basel III increases the CET1 to risk-weighted assets to 4.5%, and introduces a capital conservation buffer of an additional 2.5% of common equity to risk-weighted assets, raising the target CET1 to risk-weighted assets ratio to 7%. It requires banks to maintain a minimum ratio of Tier 1 capital to risk weighted assets of at least 6.0%, plus the capital conservation buffer effectively resulting in Tier 1 capital ratio of 8.5%. Basel III increases the minimum total capital ratio to 8.0% plus the capital conservation buffer, increasing the minimum total capital ratio to 10.5%. Basel III also introduces a non-risk adjusted tier 1 leverage ratio of 3%, based on a measure of total exposure rather than total assets, and new liquidity.

On June 7, 2012, the federal bank regulatory agencies issued a series of proposed rules that would revise their risk-based and leverage capital requirements and their method for calculating risk-weighted assets to make them consistent with Basel III and certain provisions of the Dodd-Frank Act. The proposed rules would apply to all depository institutions, top-tier bank holding companies with total consolidated assets of $500 million or more, and top-tier savings and loan holding companies (banking organizations). Among other things, the proposed rules establish a new Common Equity Tier 1 minimum capital requirement of 4.5% and a higher minimum Tier 1 capital requirement of 6.0%. The proposed rules would also increase the required capital for certain categories of assets, including higher-risk residential mortgages, higher-risk construction real estate loans and certain exposures related to securitizations.

Additionally, the U.S. implementation of Basel III contemplates that, for banking organizations with less than $15 billion in assets, the ability to treat trust preferred securities as Tier 1 capital would be phased out over a ten-year period. The proposed rules also required unrealized gains and losses on certain securities holdings to be included for purposes of calculating regulatory capital requirements. The proposed rules limit a banking organization s capital distributions and certain discretionary bonus payments if the banking organization does not hold a capital conservation buffer consisting of a specified amount of Common Equity Tier 1 capital in addition to the amount necessary to meet its minimum risk-based capital requirements.

The Basel III implementation proposal provides for a number of deductions from and adjustments to CET1. These include, for example, the requirement that mortgage servicing rights, deferred tax assets dependent upon future taxable income and significant investments in non-consolidated financial entities be deducted from CET1 to the extent that any one such category exceeds 10% of CET1 or all such categories in the aggregate exceed 15% of CET1. Under current capital standards, the effects of accumulated other comprehensive income items included in capital are excluded for the purposes of determining regulatory capital ratios. Under the Basel III Proposal, the effects of certain accumulated other comprehensive items are not excluded, which could result in significant variations in the level of capital depending upon the impact of interest rate fluctuations on the fair value of the Corporation s securities portfolio. The Basel III Proposal also requires the phase-out of certain hybrid securities, such as trust preferred securities, as Tier 1 capital of bank holding companies in equal installments between 2013 and 2016. Trust preferred securities no longer included in Tier 1 capital may nonetheless be included as a component of Tier 2 capital.

Implementation of the deductions and other adjustments to CET1 will begin on January 1, 2014 and will be phased-in over a five-year period (20% per year). The implementation of the capital conservation buffer will begin on January 1, 2016 at the 0.625% level and be phased in over a four-year period (increasing by that amount on each subsequent January 1, until it reaches 2.5% on January 1, 2019).

The Basel III implementation proposal would also revise the prompt corrective action regulations described below by (i) introducing a CET1 ratio requirement at each level (other than critically undercapitalized), with the required CET1 ratio being 6.5% for well-capitalized status; (ii) increasing the minimum Tier 1 capital ratio requirement for each category, with the minimum Tier 1 capital ratio for well-capitalized status being 8% (as compared to the current 6%); and (iii) eliminating the current provision that provides that a bank with a composite supervisory rating of 1 may have a 3% leverage ratio and still be adequately capitalized. The Basel III proposal does not change the total risk-based capital requirement for any category.

Management believes that, as of December 31, 2012, Old National and Old National Bank would meet all capital adequacy requirements under the proposed rules on a fully phased-in basis if such requirements were currently effective. There can be no guarantee that the rule proposals will be adopted in their current form, what changes may be made before adoption, or when ultimate adoption will occur. Requirements to maintain higher levels of capital or to maintain higher levels of liquid assets could adversely impact the Corporation s net income and return on equity.

Old National Bank is subject to the provisions of the National Bank Act, is supervised, regulated and examined by the OCC, and is subject to the rules and regulations of the OCC, Federal Reserve and the FDIC. A substantial portion of Old National s cash revenue is derived from dividends paid to it by Old National Bank. These dividends are subject to various legal and regulatory restrictions as summarized in Note 21 to the consolidated financial statements.

Both federal and state law extensively regulate various aspects of the banking business, such as reserve requirements, truth-in-lending and truth-in-savings disclosures, equal credit opportunity, fair credit reporting, trading in securities and other aspects of banking operations. Branching by Old National Bank is subject to the jurisdiction and requires notice to or the prior approval of the OCC.

Old National and Old National Bank are subject to the Federal Reserve Act, which restricts financial transactions between banks and affiliated companies. The statute limits credit transactions between banks, affiliated companies and its executive officers and its affiliates. The statute prescribes terms and conditions for bank affiliate transactions deemed to be consistent with safe and sound banking practices, and restricts the types of collateral security permitted in connection with a bank s extension of credit to an affiliate. Additionally, all transactions with an affiliate must be on terms substantially the same or at least as favorable to the institution as those prevailing at the time for comparable transactions with nonaffiliated parties.

FDICIA accomplished a number of sweeping changes in the regulation of depository institutions, including Old National Bank. FDICIA requires, among other things, federal bank regulatory authorities to take prompt corrective action with respect to banks which do not meet minimum capital requirements.

Under current prompt corrective action regulations, a bank will be (i) well capitalized if the institution has a total risk-based capital ratio of 10.0% or greater, a Tier 1 risk-based capital ratio of 6.0% or greater, and a leverage ratio of 5.0% or greater, and is not subject to any order or written directive by any such regulatory authority to meet and maintain a specific capital level for any capital measure; (ii) adequately capitalized if the institution has a total risk-based capital ratio of 8.0% or greater, a Tier 1 risk-based capital ratio of 4.0% or greater, and a leverage ratio of 4.0% or greater and is not well capitalized ; (iii) undercapitalized if the institution has a total risk-based capital ratio that is less than 8.0%, a Tier 1 risk-based capital ratio of less than 4.0% or a leverage ratio of less than 4.0%; (iv) significantly undercapitalized if the institution has a total risk-based capital ratio of less than 6.0%, a Tier 1 risk-based capital ratio of less than 3.0% or a leverage ratio of less than 3.0%; and (v) critically undercapitalized if the institution s tangible equity is equal to or less than 2.0% of average quarterly tangible assets. An institution may be downgraded to, or deemed to be in, a capital category that is lower than indicated by its capital ratios if it is determined to be in an unsafe or unsound condition or if it receives an unsatisfactory examination rating with respect to certain matters. A bank s capital category is determined solely for the purpose of applying prompt corrective action regulations, and the capital category may not constitute an accurate representation of the bank s overall financial condition or prospects for other purposes.

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FDICIA generally prohibits a depository institution from making any capital distributions (including payment of a dividend) or paying any management fee to its parent holding company if the depository institution would thereafter be undercapitalized. Undercapitalized institutions are subject to growth limitations and are required to submit a capital restoration plan. The agencies may not accept such a plan without determining, among other things, that the plan is based on realistic assumptions and is likely to succeed in restoring the depository institution s capital. In addition, for a capital restoration plan to be acceptable, the depository institution s parent holding company must guarantee that the institution will comply with such capital restoration plan. The bank holding company must also provide appropriate assurances of performance. The aggregate liability of the parent holding company is limited to the lesser of (i) an amount equal to 5.0% of the depository institution s total assets at the time it became undercapitalized and (ii) the amount which is necessary (or would have been necessary) to bring the institution into compliance with all capital standards applicable with respect to such institution as of the time it fails to comply with the plan. If a depository institution fails to submit an acceptable plan, it is treated as if it is significantly undercapitalized.

Significantly undercapitalized depository institutions may be subject to a number of requirements and restrictions, including orders to sell sufficient voting stock to become adequately capitalized, requirements to reduce total assets, and cessation of receipt of deposits from correspondent banks. Critically undercapitalized institutions are subject to the appointment of a receiver or conservator.

Management believes that, as of December 31, 2012, Old National Bank was well capitalized based on the aforementioned ratios.

FDICIA further directed each federal banking agency to prescribe standards for depository institutions and depository institution holding companies relating to internal controls, information systems, internal audit systems, loan documentation, credit underwriting, interest rate exposure, asset growth, management compensation, a maximum ratio of classified assets to capital, minimum earnings sufficient to absorb losses, a minimum ratio of market value to book value of publicly traded shares and such other standards as the agency deems appropriate.

The Gramm-Leach-Bliley Act (GLBA) permits bank holding companies which have elected to become financial holding companies to engage in a substantially broader range of non-banking activities, including securities, investment advice and insurance activities, than is permissible for bank holding companies that have not elected to become financial holding companies. Old National has elected to be a financial holding company. As a result, Old National may underwrite and sell securities and insurance. It may acquire, or be acquired by, brokerage firms and insurance underwriters.

GLBA established new requirements for financial institutions to provide enhanced privacy protections to customers. In June of 2000, the Federal banking agencies jointly adopted a final regulation providing for the implementation of these protections. Financial institutions are required to provide notice to consumers which details its privacy policies and practices, describes under what conditions a financial institution may disclose nonpublic personal information about consumers to nonaffiliated third parties and provides an opt-out method which enables consumers to prevent the financial institution from disclosing customer information to nonaffiliated third parties. Financial institutions were required to be in compliance with the final regulation by July 1, 2001, and Old National was in compliance at such date and continues to be in compliance.

A major focus of governmental policy on financial institutions in recent years has been aimed at combating money laundering and terrorist financing. The USA PATRIOT Act of 2001 (the USA Patriot Act) substantially broadened the scope of United States anti-money laundering laws and regulations by imposing significant new compliance and due diligence obligations, creating new crimes and penalties and expanding the extra-territorial jurisdiction of the United States. Failure of a financial institution to maintain and implement adequate programs to combat money laundering and terrorist financing, or to comply with all of the relevant laws or regulations, could have serious legal and reputational consequences for the institution, including causing applicable bank regulatory authorities not to approve merger or acquisition transactions when regulatory approval is required or to prohibit such transactions even if approval is not required.

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We are currently subject to a consent order with the OCC relating to our Bank Secrecy Act/Anti-Money Laundering Program. See Risk Factors A failure by Old National Bank to satisfy the terms and conditions of the Consent Order it consented and agreed to with the Office of the Comptroller of the Currency may subject it to monetary penalties and impact future regulatory approvals.

In October 2008, the Emergency Economic Stabilization Act of 2008 (EESA) was enacted. The EESA authorized the Treasury Department to purchase from financial institutions and their holding companies up to $700 billion in mortgage loans, mortgage-related securities and certain other financial instruments, including debt and equity securities issued by financial institutions and their holding companies in a troubled asset relief program (TARP). The purpose of TARP was to restore confidence and stability to the U.S. banking system and to encourage financial institutions to increase their lending to customers and to each other. The Treasury Department allocated $350 billion towards the TARP Capital Purchase Program (CPP). Under the CPP, Treasury purchased debt or equity securities from participating institutions. The TARP also included direct purchases or guarantees of troubled assets of financial institutions. Participants in the CPP are subject to executive compensation limits and are encouraged to expand their lending and mortgage loan modifications. Old National participated in CPP, but on March 31, 2009, Old National repurchased all of the $100 million in preferred, non-voting stock that was sold to the Treasury Department as part of the CPP. In May 2009, Old National repurchased the warrants for up to 813,000 shares of the Company s common stock issued by the Company to the Treasury Department on December 12, 2008 for $1.2 million. This repurchase was the final phase required of Old National to end its participation in the CPP.

EESA also increased FDIC deposit insurance on most accounts from $100,000 to $250,000. The Dodd-Frank Act made permanent the $250,000 deposit insurance limit for insured deposits.

Following a systemic risk determination, the FDIC established a Temporary Liquidity Guarantee Program (TLGP) on October 14, 2008. The TLGP includes the Transaction Account Guarantee Program (TAGP), which provided unlimited deposit insurance coverage through December 31, 2009 for noninterest-bearing transaction accounts (typically business checking accounts) and certain funds swept into noninterest-bearing savings accounts. Institutions participating in the TAGP pay a 10 basis points fee (annualized) on the balance of each covered account in excess of $250,000, while the extra deposit insurance is in place. The TAGP was extended through December 31, 2010. The enactment of the Dodd-Frank Act provided unlimited federal deposit insurance until December 31, 2012 for noninterest bearing demand transaction accounts at all insured depository institutions.

On February 17, 2009, the American Recovery and Reinvestment Act of 2009 (ARRA) was signed into law by President Obama. ARRA includes a wide variety of programs intended to stimulate the economy and provide for extensive infrastructure, energy, health, and education needs. In addition, ARRA imposes certain new executive compensation and corporate expenditure limits on all current and future TARP recipients, including Old National, until the institution has repaid the Treasury, which is now permitted under ARRA without penalty and without the need to raise new capital, subject to the Treasury s consultation with the recipient s appropriate regulatory agency. Old National has been a TARP recipient, but has exercised its right to repay Treasury and is no longer subject to the compensation and corporate expenditure limits imposed by ARRA on TARP recipients.

In addition to the matters discussed above, Old National Bank is subject to additional regulation of its activities, including a variety of consumer protection regulations affecting its lending, deposit and collection activities and regulations affecting secondary mortgage market activities. The earnings of financial institutions are also affected by general economic conditions and prevailing interest rates, both domestic and foreign, and by the monetary and fiscal policies of the United States government and its various agencies, particularly the Federal Reserve.

Additional legislative and administrative actions affecting the banking industry may be considered by Congress, state legislatures and various regulatory agencies, including those referred to above. It cannot be predicted with certainty whether such legislative or administrative action will be enacted or the extent to which the banking industry in general, or Old National and Old National Bank in particular, would be affected.

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AVAILABLE INFORMATION

All reports filed electronically by Old National with the Securities and Exchange Commission (SEC), including the annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy and information statements, other information and amendments to those reports filed or furnished (if applicable), are accessible at no cost on Old National s web site at www.oldnational.com as soon as reasonably practicable after electronically submitting such materials to the SEC. The SEC maintains an Internet site that contains reports, proxy and information statements and other information regarding issuers that file electronically with the SEC, and Old National s filings are accessible on the SEC s web site at www.sec.gov. The public may read and copy any materials filed by Old National with the SEC at the SEC s Public Reference Room at 100 F Street, N.E, Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330.

ITEM 1A. RISK FACTORS

Old National s business could be harmed by any of the risks noted below. In analyzing whether to make or to continue an investment in Old National, investors should consider, among other factors, the following:

Risks Related to Old National s Business

A failure by Old National Bank to satisfy the conditions and obligations of the Consent Order it consented and agreed to with the Office of the Comptroller of the Currency (OCC) may subject it to monetary penalties and impact future regulatory approvals.

Old National Bank is subject to certain conditions and obligations of a Consent Order (the Order) it consented and agreed to with the OCC, Old National Bank s federal banking regulator, relating to Old National Bank s Bank Secrecy Act/Anti-Money Laundering Program. Among other things, the Order requires the ongoing implementation of a system of internal controls, independent testing and training programs designed to ensure full compliance with the Bank Secrecy Act (BSA) and to review account and transaction activity to determine whether suspicious activity was timely identified and reported by Old National Bank. The OCC did not identify any systemic undetected criminal activity or money laundering and the Order does not call for the payment of a civil monetary penalty. While the Order is in effect, it may impact Old National s ability to obtain regulatory approval for merger and acquisition activity. While Old National Bank is implementing or has implemented corrective action for each deficiency and expects to satisfy all of the requirements of the Order in a timely fashion, material failure to comply with the Order could result in enforcement actions by the OCC, including the imposition of operating and expansion restrictions and monetary penalties.

Economic conditions have affected and could continue to adversely affect our revenues and profits.

From December 2007 through June 2009, the U.S. economy was in recession. Business activity across a wide range of industries and regions in the U.S. was greatly reduced. Although economic conditions have begun to slowly improve, certain sectors, such as real estate, remain weak and unemployment remains high. Local governments and many businesses are still facing serious difficulties due to lower consumer spending and the lack of liquidity in the credit markets.

Market conditions also led to the failure or merger of several prominent financial institutions and numerous regional and community-based financial institutions. These failures, as well as projected future failures, have had a significant negative impact on the capitalization level of the deposit insurance fund of the FDIC, which, in turn, has led to a significant increase in deposit insurance premiums paid by financial institutions.

Old National s financial performance generally, and in particular the ability of borrowers to pay interest on and repay principal of outstanding loans and the value of collateral securing those loans, as well as demand for loans and other products and services that Old National offers, is highly dependent upon the business environment in the markets where Old National operates and in the United States as a whole. A favorable business environment is generally characterized by, among other factors, economic growth, efficient capital markets, low inflation, low unemployment, high business and investor confidence, and strong business earnings. Unfavorable or uncertain economic and market conditions can be caused by declines in economic growth, business activity or investor or business confidence; limitations on the availability or increases in the cost of credit and capital; increases in inflation or interest rates; high unemployment, natural disasters, terrorist acts or a combination of these or other factors.

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The business environment has been adverse for many households and businesses in the United States and worldwide. While economic conditions in the United States and worldwide have begun to improve, there can be no assurance that this improvement will continue. Such conditions could adversely affect the credit quality of Old National s loans, results of operations and financial condition.

In response to economic and market conditions, from time to time we have undertaken initiatives to reduce our cost structure where appropriate. These initiatives, as well as any future workforce and facilities reductions, may not be sufficient to meet current and future changes in economic and market conditions and allow us to achieve profitability. In addition, costs actually incurred in connection with our restructuring actions may be higher than our estimates of such costs and/or may not lead to the anticipated cost savings. Unless and until the economy, loan demand, credit quality and consumer confidence improve, it is unlikely that revenues will increase significantly, and may be reduced further.

If Old National s actual loan losses exceed Old National s allowance for loan losses, Old National s net income will decrease.

Old National makes various assumptions and judgments about the collectibility of Old National s loan portfolio, including the creditworthiness of Old National s borrowers and the value of the real estate and other assets serving as collateral for the repayment of Old National s loans. Despite Old National s underwriting and monitoring practices, the effect of the declining economy could negatively impact the ability of Old National s borrowers to repay loans in a timely manner and could also negatively impact collateral values. As a result, Old National may experience significant loan losses that could have a material adverse effect on Old National s operating results. Since Old National must use assumptions regarding individual loans and the economy, Old National s current allowance for loan losses may not be sufficient to cover actual loan losses. Old National s assumptions may not anticipate the severity or duration of the current credit cycle and Old National may need to significantly increase Old National s provision for losses on loans if one or more of Old National s larger loans or credit relationships becomes delinquent or if Old National expands its commercial real estate and commercial lending. In addition, federal and state regulators periodically review Old National s allowance for loan losses and may require Old National to increase the provision for loan losses or recognize loan charge-offs. Material additions to Old National s allowance would materially decrease Old National s net income. There can be no assurance that Old National s monitoring procedures and policies will reduce certain lending risks or that Old National s allowance for loan losses will be adequate to cover actual losses.

Old National s loan portfolio includes loans with a higher risk of loss.

Old National Bank originates commercial real estate loans, commercial loans, agricultural real estate loans, agricultural loans, consumer loans, and residential real estate loans primarily within Old National s market areas. Commercial real estate, commercial, consumer, and agricultural loans may expose a lender to greater credit risk than loans secured by residential real estate because the collateral securing these loans may not be sold as easily as residential real estate. These loans also have greater credit risk than residential real estate for the following reasons:

Commercial Real Estate Loans. Repayment is dependent upon income being generated in amounts sufficient to cover operating expenses and debt service.

Commercial Loans. Repayment is dependent upon the successful operation of the borrower s business.

Consumer Loans. Consumer loans (such as personal lines of credit) are collateralized, if at all, with assets that may not provide an adequate source of payment of the loan due to depreciation, damage, or loss.

Agricultural Loans. Repayment is dependent upon the successful operation of the business, which is greatly dependent on many things outside the control of either Old National Bank or the borrowers. These factors include weather, commodity prices, and interest rates.

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We face risks with respect to expansion.

We have acquired, and may continue to acquire, other financial institutions or parts of those institutions in the future, and we may engage in de novo branch expansion. We may also consider and enter into new lines of business or offer new products or services.

We may incur substantial costs to expand, and we can give no assurance such expansion will result in the levels of profits we seek. There can be no assurance that integration efforts for any mergers or acquisitions will be successful. Also, we may issue equity securities in connection with acquisitions, which could cause ownership and economic dilution to our current shareholders. There is no assurance that, following any mergers or acquisitions, our integration efforts will be successful or that, after giving effect to the acquisition, we will achieve profits comparable to, or better than, our historical experience.

Acquisitions and mergers involve a number of expenses and risks, including:

- the time and costs associated with identifying potential new markets, as well as acquisition and merger targets;
- the estimates and judgments used to evaluate credit, operations, management and market risks with respect to the target institution may not be accurate;
- the time and costs of evaluating new markets, hiring experienced local management and opening new offices, and the time lags between these activities and the generation of sufficient assets and deposits to support the costs of the expansion;
- our ability to finance an acquisition and possible dilution to our existing shareholders;
- the diversion of our management s attention to the negotiation of a transaction, and the integration of the operations and personnel of the combined businesses;
- entry into new markets where we lack experience;
- the introduction of new products and services into our business;
- the incurrence and possible impairment of goodwill associated with an acquisition and possible adverse short-term effects on our results of operations; and
- the risk of loss of key employees and customers.

In the current economic environment, we anticipate that in addition to opportunities to acquire other banks in privately negotiated transactions, we may also have opportunities to bid to acquire the assets and liabilities of failed banks in FDIC-assisted transactions. These acquisitions involve risks similar to acquiring existing banks. Because FDIC-assisted acquisitions are structured in a manner that would not allow us the time normally associated with due diligence investigations prior to committing to purchase the target bank or preparing for integrations of an acquired bank, we may face additional risks in FDIC-assisted transactions. These risks include, among other things:

- loss of customers of the failed bank;

strain on management resources related to collection and management of problem loans;

problems related to integration of personnel and operating systems;

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the ultimate collectibility of claims with the FDIC under the shared loss agreement are dependent upon the performance of the underlying covered assets, the passage of time and our ability to service loans in accordance with the shared loss agreement; and

losses may exceed our estimates and move us into a tranche where we have 0% coverage under our loss sharing agreements with the FDIC.

***Our growth or future losses may require us to raise additional capital in the future, but that capital may not be available when it is needed or the cost of that capital may be very high*.**

We are required by regulatory authorities to maintain adequate levels of capital to support our operations. We anticipate that our capital resources will satisfy our capital requirements for the foreseeable future. We may at some point need to raise additional capital to support continued growth or losses, both internally and through acquisitions. Any capital we obtain may result in the dilution of the interests of existing holders of our common stock.

Our ability to raise additional capital, if needed, will depend on conditions in the capital markets at that time (which are outside our control) and on our financial condition and performance. Accordingly, we cannot make assurances of our ability to raise additional capital if needed, or if the terms will be acceptable to us. If we cannot raise additional capital when needed, our ability to further expand our operations through internal growth and acquisitions could be materially impaired and our financial condition and liquidity could be materially and negatively affected.

Our wholesale funding sources may prove insufficient to replace deposits or support our future growth.

As a part of our liquidity management, we use a number of funding sources in addition to core deposit growth and repayments and maturities of loans and investments. These sources include brokered certificates of deposit, repurchase agreements, and federal funds purchased. Negative operating results or changes in industry conditions could lead to an inability to replace these additional funding sources at maturity. Our financial flexibility could be constrained if we are unable to maintain our access to funding or if adequate financing is not available to accommodate future growth at acceptable interest rates. Finally, if we are required to rely more heavily on more expensive funding sources to support future growth, our revenues may not increase proportionately to cover our costs. In this case, our results of operations and financial condition would be negatively affected.

Our Accounting Estimates and Risk Management Processes Rely On Analytical and Forecasting Models

The processes that we use to estimate probable loan losses and to measure the fair value of financial instruments, as well as the processes used to estimate the effects of changing interest rates and other market measures on our financial condition and results of operations, depend upon the use of analytical and forecasting models. These models reflect assumptions that may not be accurate, particularly in times of market stress or other unforeseen circumstances. Even if these assumptions are adequate, the models may prove to be inadequate or inaccurate because of other flaws in their design or their implementation. If our models for determining interest rate risk and asset-liability management are inadequate, we may incur increased or unexpected losses upon changes in market interest rates or other market measures. If our models for determining probable loan losses are inadequate, the allowance for loan losses may not be sufficient to support future charge-offs. If our models to measure the fair value of financial instruments are inadequate, the fair value of such financial instruments may fluctuate unexpectedly or may not accurately reflect what we could realize upon sale or settlement of such financial instruments. Any such failure in our analytical or forecasting models could have a material adverse effect on our business, financial condition and results of operations.

The Repeal Of Federal Prohibitions On Payment Of Interest On Demand Deposits Could Increase Our Interest Expense

All federal prohibitions on the ability of financial institutions to pay interest on demand deposit accounts were repealed as part of the Dodd-Frank Act beginning on July 21, 2011. As a result, some financial institutions have commenced offering interest on demand deposits to compete for customers. We cannot predict what interest rates other institutions may offer as market interest rates begin to increase. Our interest expense will increase and our net interest margin will decrease if we begin offering interest on demand deposits to attract additional customers or maintain current customers, which could have a material adverse effect on our business, financial condition and results of operations.

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If Old National forecloses on collateral property, Old National may be subject to the increased costs associated with the ownership of real property, resulting in reduced revenues.

Old National may have to foreclose on collateral property to protect Old National s investment and may thereafter own and operate such property, in which case Old National will be exposed to the risks inherent in the ownership of real estate. The amount that Old National, as a mortgagee, may realize after a default is dependent upon factors outside of Old National s control, including, but not limited to: (i) general or local economic conditions; (ii) neighborhood values; (iii) interest rates; (iv) real estate tax rates; (v) operating expenses of the mortgaged properties; (vi) environmental remediation liabilities; (vii) ability to obtain and maintain adequate occupancy of the properties; (viii) zoning laws; (ix) governmental rules, regulations and fiscal policies; and (x) acts of God. Certain expenditures associated with the ownership of real estate, principally real estate taxes, insurance, and maintenance costs, may adversely affect the income from the real estate. Therefore, the cost of operating real property may exceed the income earned from such property, and Old National may have to advance funds in order to protect Old National s investment, or Old National may be required to dispose of the real property at a loss. The foregoing expenditures and costs could adversely affect Old National s ability to generate revenues, resulting in reduced levels of profitability.

Old National operates in an extremely competitive market, and Old National s business will suffer if Old National is unable to compete effectively.

In Old National s market area, the Company encounters significant competition from other commercial banks, savings and loan associations, credit unions, mortgage banking firms, consumer finance companies securities brokerage firms, insurance companies, money market mutual funds and other financial intermediaries. The Company s competitors may have substantially greater resources and lending limits than Old National does and may offer services that Old National does not or cannot provide. Old National s profitability depends upon Old National s continued ability to compete successfully in Old National s market area.

The loss of key members of Old National s senior management team could adversely affect Old National s business.

Old National believes that Old National s success depends largely on the efforts and abilities of Old National s senior management. Their experience and industry contacts significantly benefit Old National. The competition for qualified personnel in the financial services industry is intense, and the loss of any of Old National s key personnel or an inability to continue to attract, retain and motivate key personnel could adversely affect Old National s business.

A breach of information security or compliance breach by one of our agents or vendors could negatively affect Old National s reputation and business.

Old National relies upon a variety of computing platforms and networks over the internet for the purposes of data processing, communication and information exchange. Despite the safeguards instituted by Old National, such systems are susceptible to a breach of security. In addition, Old National relies on the services of a variety of third-party vendors to meet Old National s data processing and communication needs. The occurrence of any failures, interruptions or security breaches of Old National s information systems or our vendors information systems could damage our reputation, result in a loss of customer business, and expose us to civil litigation and possible financial loss. Such costs and/or losses could materially affect Old National s earnings.

Fiduciary Activity Risk Factor

Old National Is Subject To Claims and Litigation Pertaining To Fiduciary Responsibility

From time to time, customers make claims and take legal action pertaining to Old National s performance of its fiduciary responsibilities. If such claims and legal actions are not resolved in a manner favorable to Old National they may result in significant financial liability and/or adversely affect the market perception of Old National and its products and services as well as impact customer demand for those products and services. Any financial liability or reputational damage could have a material adverse effect on the Old National s business, which, in turn, could have a material adverse effect on the Old National s financial condition and results of operations.

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Risks Related to the Banking Industry

Old National operates in a highly regulated environment, and changes in laws and regulations to which Old National is subject may adversely affect Old National s results of operations.

Old National operates in a highly regulated environment and is subject to extensive regulation, supervision and examination by the Office of Comptroller of the Currency (OCC), the Federal Deposit Insurance Corporation (FDIC), the Board of Governors of the Federal Reserve System (the Federal Reserve) and the State of Indiana. Such regulation and supervision of the activities in which an institution may engage is primarily intended for the protection of the depositors and federal deposit insurance funds. In addition, the Treasury has certain supervisory and oversight duties and responsibilities under EESA and the CPP. See Business Supervision and Regulation herein. Applicable laws and regulations may change, and such changes may adversely affect Old National s business. The Dodd-Frank Act, enacted in July 2010, instituted major changes to the banking and financial institutions regulatory regimes in light of the recent performance of and government intervention in the financial services sector. Many aspects of the Dodd-Frank Act are subject to rulemaking and will take effect over several years, making it difficult to anticipate the overall financial impact on Old National. Provisions in the legislation that affect the payment of interest on demand deposits and interchange fees are likely to increase the costs associated with deposits as well as place limitation on certain revenues those deposits may generate. Provisions in the legislation that revoke the Tier 1 capital treatment of trust preferred securities and otherwise require revisions to the capital requirements of Old National and Old National Bank could require Old National and Old National Bank to seek other sources of capital in the future. In addition, certain provisions in the legislation that do not currently apply to Old National may become effective if Old National grows and its consolidated assets increase to over ten billion.

Regulatory authorities also have extensive discretion in connection with their supervisory and enforcement activities, including but not limited to the imposition of restrictions on the operation of an institution, the classification of assets by the institution, the adequacy of an institution s Bank Secrecy Act/Anti Money Laundering program management, and the adequacy of an institution s allowance for loan losses. Any change in such regulation and oversight, whether in the form of restrictions on activities, regulatory policy, regulations, or legislation, including but not limited to changes in the regulations governing institutions, could have a material impact on Old National and its operations.

Changes in economic or political conditions could adversely affect Old National s earnings, as the ability of Old National s borrowers to repay loans, and the value of the collateral securing such loans, decline.

Old National s success depends, to a certain extent, upon economic or political conditions, local and national, as well as governmental monetary policies. Conditions such as recession, unemployment, changes in interest rates, inflation, money supply and other factors beyond Old National s control may adversely affect its asset quality, deposit levels and loan demand and, therefore, Old National s earnings. Because Old National has a significant amount of commercial real estate loans, decreases in real estate values could adversely affect the value of property used as collateral. Adverse changes in the economy may also have a negative effect on the ability of Old National s borrowers to make timely repayments of their loans, which would have an adverse impact on Old National s earnings. In addition, substantially all of Old National s loans are to individuals and businesses in Old National s market area. Consequently, any economic decline in Old National s primary market areas, which include Indiana, Kentucky and Illinois, could have an adverse impact on Old National s earnings.

Changes in interest rates could adversely affect Old National s results of operations and financial condition.

Old National s earnings depend substantially on Old National s interest rate spread, which is the difference between (i) the rates Old National earns on loans, securities and other earning assets and (ii) the interest rates Old National pays on deposits and other borrowings. These rates are highly sensitive to many factors beyond Old National s control, including general economic conditions and the policies of various governmental and regulatory authorities. If market interest rates rise, Old National will have competitive pressures to increase the rates that Old National pays on deposits, which could result in a decrease of Old National s net interest income. If market interest rates decline, Old National could experience fixed rate loan prepayments and higher investment portfolio cash flows, resulting in a lower yield on earnings assets.

Our Internal Operations are Subject to a Number of Risks.

Old National s internal operations are subject to certain risks, including but not limited to, data processing system failures and errors, customer or employee fraud and catastrophic failures resulting from terrorist acts or natural disasters. Operational risk resulting from inadequate or failed internal processes, people, and systems includes the risk of fraud by employees or persons outside of our company, the execution of unauthorized transactions by employees, errors relating to transaction processing and systems, and breaches of the internal control system and compliance requirements. This risk of loss also includes potential legal actions that could arise as a result of the operational deficiency or as a result of noncompliance with applicable regulatory standards.

The banking industry is undergoing technological innovation at a fast pace. To keep up with its competition, Old National needs to stay abreast of innovations and evaluate those technologies that will enable it to compete on a cost-effective basis. The cost of such technology, including personnel, can be high in both absolute and relative terms. There can be no assurance, given the fast pace of change and innovation, that Old National s technology, either purchased or developed internally, will meet or continue to meet the needs of Old National.

Our earnings could be adversely impacted by incidences of fraud and compliance failures that are not within our direct control.

Financial institutions are inherently exposed to fraud risk. A fraud can be perpetrated by a customer of the Bank, an employee, a vendor, or members of the general public. We are most subject to fraud and compliance risk in connection with the origination of loans, ACH transactions, ATM transactions and checking transactions. Our largest fraud risk, associated with the origination of loans, includes the intentional misstatement of information in property appraisals or other underwriting documentation provided to us by third parties. Compliance risk is the risk that loans are not originated in compliance with applicable laws and regulations and our standards. There can be no assurance that we can prevent or detect acts of fraud or violation of law or our compliance standards by the third parties that we deal with. Repeated incidences of fraud or compliance failures would adversely impact the performance of our loan portfolio.

Risks Related to Old National s Stock

We may not be able to pay dividends in the future in accordance with past practice.

Old National has traditionally paid a quarterly dividend to common stockholders. The payment of dividends is subject to legal and regulatory restrictions. Any payment of dividends in the future will depend, in large part, on Old National s earnings, capital requirements, financial condition and other factors considered relevant by Old National s Board of Directors.

The price of Old National s common stock may be volatile, which may result in losses for investors.

General market price declines or market volatility in the future could adversely affect the price of Old National s common stock. In addition, the following factors may cause the market price for shares of Old National s common stock to fluctuate:

- announcements of developments related to Old National s business;
- fluctuations in Old National s results of operations;
- sales or purchases of substantial amounts of Old National s securities in the marketplace;

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general conditions in Old National s banking niche or the worldwide economy;

a shortfall or excess in revenues or earnings compared to securities analysts expectations;

changes in analysts recommendations or projections; and

Old National s announcement of new acquisitions or other projects.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

As of December 31, 2012, Old National and its affiliates operated a total of 180 banking centers, loan production or other financial services offices, primarily in the states of Indiana, Illinois and Kentucky. Of these facilities, 38 were owned.

The executive offices of Old National are located at 1 Main Street, Evansville, Indiana. This building, which houses Old National s general corporate functions, is leased from an unaffiliated third party. The lease term expires December 31, 2031, and provides for the tenant s option to extend the term of the lease for four five-year periods. In addition, we lease 142 financial centers from unaffiliated third parties. The terms of these leases range from six months to twenty-four years. See Note 19 to the consolidated financial statements.

ITEM 3. LEGAL PROCEEDINGS

In the normal course of business, Old National Bancorp and its subsidiaries have been named, from time to time, as defendants in various legal actions. Certain of the actual or threatened legal actions include claims for substantial compensatory and/or punitive damages or claims for indeterminate amounts of damages.

Old National contests liability and/or the amount of damages as appropriate in each pending matter. In view of the inherent difficulty of predicting the outcome of such matters, particularly in cases where claimants seek substantial or indeterminate damages or where investigations and proceedings are in the early stages, Old National cannot predict with certainty the loss or range of loss, if any, related to such matters, how or if such matters will be resolved, when they will ultimately be resolved, or what the eventual settlement, or other relief, if any, might be. Subject to the foregoing, Old National believes, based on current knowledge and after consultation with counsel, that the outcome of such pending matters will not have a material adverse effect on the consolidated financial condition of Old National, although the outcome of such matters could be material to Old National s operating results and cash flows for a particular future period, depending on, among other things, the level of Old National s revenues or income for such period. Old National will accrue for a loss contingency if (1) it is probable that a future event will occur and confirm the loss and (2) the amount of the loss can be reasonably estimated.

In November 2002, several beneficiaries of certain trusts filed a complaint against Old National and Old National Trust Company in the United States District Court for the Western District of Kentucky relating to the administration of the trusts in 1997. This litigation was fully and finally settled in the first quarter of 2012. The Company had previously accrued $2 million in the third quarter of 2011 in anticipation of negotiating the final settlement and resolution of the matter. The matter was fully settled for the amount of the accrual. However, a portion of the settlement funds were put temporarily in escrow to account for uncertain contingencies. These funds, less contingencies (if any), were released to the beneficiaries in December 2012 pursuant to the terms of the settlement agreement.

In November 2010, Old National was named in a class action lawsuit in Vanderburgh County Circuit Court challenging Old National Bank s checking account practices associated with the assessment of overdraft fees. On May 1, 2012, the plaintiff was granted permission to file a First Amended Complaint which names additional plaintiffs and amends certain claims. The plaintiffs seek damages and other relief, including restitution. Old National believes it has meritorious defenses to the claims brought by the plaintiffs. At this phase of the litigation, it is not possible for management of Old National to determine the probability of a material adverse outcome or reasonably estimate the amount of any loss. No class has yet been certified and discovery is ongoing. On June 13, 2012, Old National filed a motion to dismiss the First Amended Complaint, which has not yet been ruled upon. On September 7, 2012, the plaintiffs filed a motion for class certification.

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ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

PART II

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

Old National s common stock is traded on the New York Stock Exchange (NYSE) under the ticker symbol ONB. The following table lists the high and low closing sales prices as reported by the NYSE, share volume and dividend data for 2012 and 2011:

	Price Per Share		Share	Dividend
	High	Low	Volume	Declared
2012				
First Quarter	**$ 13.29**	**$ 11.52**	**35,989,100**	**$ 0.09**
Second Quarter	**13.21**	**10.92**	**26,520,600**	**0.09**
Third Quarter	**14.10**	**11.84**	**25,206,900**	**0.09**
Fourth Quarter	**13.90**	**10.94**	**31,430,300**	**0.09**
2011				
First Quarter	$ 12.15	$ 10.35	29,575,800	$ 0.07
Second Quarter	11.33	10.16	34,157,500	0.07
Third Quarter	11.05	8.67	52,288,900	0.07
Fourth Quarter	11.99	9.05	47,713,600	0.07

There were 23,525 shareholders of record as of December 31, 2012. Old National declared cash dividends of $0.36 per share during the year ended December 31, 2012 and $0.28 per share during the year ended December 31, 2011. Old National s ability to pay cash dividends depends primarily on cash dividends received from Old National Bank. Dividend payments from Old National Bank are subject to various regulatory restrictions. See Note 21 to the consolidated financial statements for additional information.

The following table summarizes the purchases of equity securities made by Old National during the fourth quarter of 2012:

Period	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs
10/01/12 10/31/12	600	$ 13.75	600	1,933,564
11/01/12 11/30/12	250,176	12.16	250,176	1,683,388
12/01/12 12/31/12	9,567	11.87	9,567	1,673,821
Total	260,343	$ 12.15	260,343	1,673,821

On January 26, 2012, the Board of Directors approved the repurchase of up to 2.0 million shares of common stock over a twelve month period beginning January 26, 2012 and ending January 31, 2013. During the fourth quarter of 2012, Old National repurchased 250,000 shares on the open market. During the twelve months ended December 31, 2012, Old National also repurchased a limited number of shares associated with employee share-based incentive programs.

Subsequent to year-end, the Board of Directors approved the repurchase of up to 2.0 million shares of common stock over a twelve month period that runs through January 31, 2014. On January 24, 2013, the Board of Directors also declared an increase in its quarterly common stock dividend to $.10 per share, an 11.1% increase over the previous cash dividend level of $.09 per share. Old National s recent financial performance and strong capital position allowed it to increase the cash dividend.

EQUITY COMPENSATION PLAN INFORMATION

The following table contains information concerning the 2008 Equity Incentive Plan approved by security holders, as of December 31, 2012.

2008 EQUITY COMPENSATION PLAN

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Equity compensation plans approved by security holders	4,095,556	$ 17.71	3,535,002
Equity compensation plans not approved by security holders			
Total	4,095,556	$ 17.71	3,535,002

The following table compares cumulative five-year total shareholder returns, assuming reinvestment of dividends, for the Company s common stock to cumulative total returns of a broad-based equity market index and two published industry indices.

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The comparison of shareholder returns (change in December year end stock price plus reinvested dividends) for each of the periods assumes that $100 was invested on December 31, 2007, in common stock of each of the Company, the S&P Small Cap 600 Index, the NYSE Financial Index and the SNL Bank and Thrift Index with investment weighted on the basis of market capitalization.

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ITEM 6. SELECTED FINANCIAL DATA

(dollars in thousands, except per share data)	2012	2011	2010	2009	2008
Operating Results					
Net interest income	**$ 308,757**	$ 272,873	$ 218,416	$ 231,399	$ 243,325
Conversion to fully taxable equivalent (1)	**13,188**	11,821	13,482	20,831	19,326
Net interest income tax equivalent basis	**321,945**	284,694	231,898	252,230	262,651
Provision for loan losses	**5,030**	7,473	30,781	63,280	51,464
Noninterest income	**189,816**	182,883	170,150	163,460	166,969
Noninterest expense	**365,758**	348,521	314,305	338,956	297,229
Net income available to common shareholders	**91,675**	72,460	38,214	9,845	62,180
Common Share Data (2)					
Weighted average diluted shares	**96,833**	94,772	86,928	71,367	65,776
Net income (diluted)	**$ 0.95**	$ 0.76	$ 0.44	$ 0.14	$ 0.95
Cash dividends	**0.36**	0.28	0.28	0.44	0.69
Common dividend payout ratio (3)	**37.80**	36.59	63.75	308.59	73.51
Book value at year-end	**11.81**	10.92	10.08	9.68	9.56
Stock price at year-end	**11.87**	11.65	11.89	12.43	18.16
Balance Sheet Data (at December 31)					
Loans (4)	**$ 5,209,185**	$ 4,771,731	$ 3,747,270	$ 3,908,276	$ 4,777,514
Total assets	**9,543,623**	8,609,683	7,263,892	8,005,335	7,873,890
Deposits	**7,278,953**	6,611,563	5,462,925	5,903,488	5,422,287
Other borrowings	**237,493**	290,774	421,911	699,059	834,867
Shareholders equity	**1,194,565**	1,033,556	878,805	843,826	730,865
Performance Ratios					
Return on average assets (ROA)	**1.04%**	0.86%	0.50%	0.17%	0.82%
Return on average common shareholders equity (ROE)	**8.34**	7.24	4.40	1.41	9.49
Average equity to average assets	**12.49**	11.94	11.46	9.06	8.67
Net interest margin (5)	**4.23**	3.87	3.40	3.50	3.82
Efficiency ratio (6)	**71.83**	73.80	79.25	80.45	69.39
Asset Quality (7)					
Net charge-offs to average loans	**0.17%**	0.49%	0.75%	1.40%	0.87%
Allowance for loan losses to ending loans	**1.05**	1.22	1.93	1.81	1.41
Allowance for loan losses	**$ 54,763**	$ 58,060	$ 72,309	$ 69,548	$ 67,087
Underperforming assets (8)	**301,919**	340,543	77,108	78,666	69,883
Other Data					
Full-time equivalent employees	**2,684**	2,551	2,491	2,812	2,507
Branches and financial centers	**180**	183	161	172	117

(1) Calculated using the federal statutory tax rate in effect of 35% for all periods adjusted for the TEFRA interest disallowance applicable to certain tax-exempt obligations.
(2) Diluted data assumes the exercise of stock options and the vesting of restricted stock.
(3) Cash dividends divided by income available to common stockholders.
(4) Includes residential loans and finance leases held for sale.
(5) Defined as net interest income on a tax equivalent basis as a percentage of average earning assets.
(6) Defined as noninterest expense before amortization of intangibles as a percent of fully taxable equivalent net interest income and noninterest income, excluding net gains from securities transactions. This presentation excludes intangible amortization and net securities gains, as is common in other company disclosures, and better aligns with true operating performance.
(7) Excludes residential loans and finance leases held for sale.
(8) Includes nonaccrual loans, renegotiated loans, loans 90 days past due still accruing and other real estate owned. Includes $130.1 million and $215.7 million of covered assets in 2012 and 2011, respectively, acquired in an FDIC assisted transaction, which are covered by loss sharing agreements with the FDIC providing for specified loss protection.

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

The following discussion is an analysis of our results of operations for the fiscal years ended December 31, 2012, 2011 and 2010, and financial condition as of December 31, 2012 and 2011. This discussion and analysis should be read in conjunction with our consolidated financial statements and related notes. This discussion contains forward-looking statements concerning our business. Readers are cautioned that, by their nature, forward-looking statements are based on estimates and assumptions and are subject to risks, uncertainties, and other factors. Actual results may differ materially from our expectations that are expressed or implied by any forward-looking statement. The discussion in Item 1A, Risk Factors, lists some of the factors that could cause our actual results to vary materially from those expressed or implied by any forward-looking statements, and such discussion is incorporated into this discussion by reference.

GENERAL OVERVIEW

Old National is a financial holding company incorporated in the State of Indiana and maintains its principal executive offices in Evansville, Indiana. Old National, through Old National Bank, provides a wide range of services, including commercial and consumer loan and depository services, lease financing and other traditional banking services. Old National also provides services to supplement the traditional banking business including fiduciary and wealth management services, investment and brokerage services, investment consulting, insurance and other financial services.

The Company s basic mission is to be THE community bank in the cities and towns it serves. The Company focuses on establishing and maintaining long-term relationships with customers, and is committed to serving the financial needs of the communities in its market area. Old National provides financial services primarily in Indiana, eastern and southeastern Illinois, and central and western Kentucky.

CORPORATE DEVELOPMENTS IN FISCAL 2012

Net income for 2012 was $91.7 million, an increase of $19.2 million from 2011. Diluted earnings per share available to common shareholders were $0.95 per share, an increase of $0.19 per share from 2011.

The improvement in 2012 net income was primarily the result of accretion income associated with acquired loans, lower cost funding sources, modest organic loan growth, and improved credit. Partially offsetting the higher net revenue were higher noninterest expenses associated with our recent acquisitions.

The Company successfully integrated Indiana Community Bancorp at the end of the third quarter. This transaction strengthens our position as the third largest branch network in Indiana and allows us to expand our services into Columbus, Indiana and other vibrant regions in the south central Indiana market.

Subsequent to year-end, the Company also announced its intent to enter into the southwest lower Michigan market through the acquisition of 24 Bank of America branches. The entry into this new market and the full ramp-up of lenders at the former Indiana Community Bancorp locations give rise to our favorable commercial loan growth outlook.

BUSINESS OUTLOOK

While we believe the interest rate environment will continue to pose challenges for 2013 revenue growth, our clients are expressing more optimism regarding the state of the economy.

Our goals for 2013 are much the same as they were in 2012: increase revenue, reduce expenses and target partnership opportunities that align with our financial and strategic goals.

While we remain committed to a risk-conscious approach to lending, we know how vital it is to generate new loan growth in 2013 and beyond. We believe our new partnerships, and the new client base they represent, position us well to achieve this growth.

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As we did in 2012, we will continue to look for ways to enhance the Company s efficiency ratio through process improvements, organizational streamlining and other cost reduction strategies.

We continue to target additional partnerships. We are focused on expanding our wealth management business and community banks in growth markets that are either within or near our existing franchise. Such strategic consolidations should improve the Company s bottom line while expanding our distribution network, which helps build long-term shareholder value.

RESULTS OF OPERATIONS

The following table sets forth certain income statement information of Old National for the years ended December 31, 2012, 2011, and 2010:

(dollars in thousands)	2012	2011	2010
Income Statement Summary:			
Net interest income	**$ 308,757**	$ 272,873	$ 218,416
Provision for loan losses	**5,030**	7,473	30,781
Noninterest income	**189,816**	182,883	170,150
Noninterest expense	**365,758**	348,521	314,305
Other Data:			
Return on average common equity	**8.34%**	7.24%	4.40%
Efficiency ratio (1)	**71.83%**	73.80%	79.25%
Tier 1 leverage ratio	**8.56%**	8.29%	9.01%
Net charge-offs to average loans	**0.17%**	0.49%	0.75%

(1) Efficiency ratio is defined as noninterest expense before amortization of intangibles as a percent of fully taxable equivalent net interest income and noninterest income, excluding net gains from securities transactions. This presentation excludes intangible amortization and net securities gains, as is common in other company disclosures, and better aligns with true operating performance. This is a non-GAAP financial measure that management believes to be helpful in understanding Old National s results of operations.

Comparison of Fiscal Years 2012 and 2011

Net Interest Income

Net interest income is the most significant component of our earnings, comprising over 61% of 2012 revenues. Net interest income and margin are influenced by many factors, primarily the volume and mix of earning assets, funding sources and interest rate fluctuations. Other factors include level of accretion income on purchased loans, prepayment risk on mortgage and investment-related assets and the composition and maturity of earning assets and interest-bearing liabilities. Loans typically generate more interest income than investment securities with similar maturities. Funding from client deposits generally cost less than wholesale funding sources. Factors such as general economic activity, Federal Reserve Board monetary policy and price volatility of competing alternative investments, can also exert significant influence on our ability to optimize the mix of assets and funding and the net interest income and margin.

Net interest income is the excess of interest received from earning assets over interest paid on interest-bearing liabilities. For analytical purposes, net interest income is also presented in the table that follows, adjusted to a taxable equivalent basis to reflect what our tax-exempt assets would need to yield in order to achieve the same after-tax yield as a taxable asset. We used the federal statutory tax rate in effect of 35% for all periods adjusted for the TEFRA interest disallowance applicable to certain tax-exempt obligations. This analysis portrays the income tax benefits associated in tax-exempt assets and helps to facilitate a comparison between taxable and tax-exempt assets. Management believes that it is a standard practice in the banking industry to present net interest margin and net interest income on a fully taxable equivalent basis. Therefore, management believes these measures provide useful information for both management and investors by allowing them to make peer comparisons.

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(dollars in thousands)	2012	2011	2010
Net interest income	$ 308,757	$ 272,873	$ 218,416
Conversion to fully taxable equivalent	13,188	11,821	13,482
Net interest income taxable equivalent basis	$ 321,945	$ 284,694	$ 231,898
Average earning assets	7,617,060	7,359,092	6,814,607
Net interest margin	4.05%	3.71%	3.21%
Net interest margin taxable equivalent basis	4.23%	3.87%	3.40%

Net interest income was $308.8 million in 2012, a 13.2% increase from the $272.9 million reported in 2011. Taxable equivalent net interest income was $321.9 million in 2012, a 13.1% increase from the $284.7 million reported in 2011. The net interest margin on a fully taxable equivalent basis was 4.23% for 2012, a 36 basis point increase compared to the 3.87% reported in 2011. The increase in both net interest income and net interest margin is primarily due to the acquisition of Integra Bank on July 29, 2011 and Indiana Community Bancorp (IBT) on September 15, 2012 combined with a change in the mix of interest earning assets and interest-bearing liabilities. The accretion associated with the purchased assets benefited net interest margin by 75 basis points in 2012 compared to 50 basis points in 2011. We expect this benefit to decline over time. The yield on average earning assets increased 10 basis points from 4.60% to 4.70% while the cost of interest-bearing liabilities decreased 32 basis points from 0.96% to 0.64%. Average earning assets increased by $258.0 million, or 3.5%. Average interest-bearing liabilities increased $28.8 million, or 0.5%. The increase in average earning assets consisted of a $418.5 million increase in loans, a $36.8 million decrease in lower yielding investment securities and a $123.7 million decrease in money market and other interest-earning investments. The increase in average interest-bearing liabilities consisted of a $113.2 million increase in interest-bearing deposits, a $50.3 million increase in short-term borrowings and a $134.7 million decrease in other borrowings. Noninterest-bearing deposits increased by $272.8 million.

Significantly affecting average earning assets during 2012 was the increase in the size of the loan portfolio combined with the reduction in the size of the investment portfolio and the decrease in interest earning cash balances at the Federal Reserve. Included in average earning assets for 2012 are approximately $169.3 million from the Indiana Community Bancorp acquisition, which was completed on September 15, 2012, and $543.5 million from the Integra Bank acquisition, which was completed on July 29, 2011. Included in average earning assets for 2011 was $319.5 million from the Integra Bank acquisition. The increase in average loans during 2012 is primarily a result of the Indiana Community Bancorp and Integra Bank acquisitions. However, in 2012 we continued to experience growth in our residential mortgage loan portfolio and late in the year began to experience modest growth in our commercial loan portfolio. The loan portfolio, which generally has an average yield higher than the investment portfolio, was approximately 63% of interest earning assets at December 31, 2012.

Positively affecting margin was an increase in noninterest-bearing demand deposits combined with decreases in time deposits and other borrowings. During the fourth quarter of 2012, we terminated $50.0 million of FHLB advances. On June 30, 2012 we redeemed $13.0 million of subordinated notes and $3.0 million of trust preferred securities. During 2011, we prepaid $119.2 million of FHLB advances and $80.0 million of structured repurchase agreements. In the fourth quarter of 2011, $150.0 million of subordinated bank notes matured. Year over year, time deposits and other borrowings, which have an average interest rate higher than other types of deposits, have decreased as a percent of total funding. Year over year, noninterest-bearing demand deposits have increased as a percent of total funding.

The following table presents a three-year average balance sheet and for each major asset and liability category, its related interest income and yield or its expense and rate for the years ended December 31.

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THREE-YEAR AVERAGE BALANCE SHEET AND NET INTEREST ANALYSIS

	2012			**2011**			**2010**		
(tax equivalent basis, dollars in thousands)	**Average Balance**	**Interest & Fees**	**Yield/ Rate**	**Average Balance**	**Interest & Fees**	**Yield/ Rate**	**Average Balance**	**Interest & Fees**	**Yield/ Rate**
Earning Assets									
Money market and other interest- earning investments (7)	**$ 29,161**	**$ 54**	**0.18%**	$ 152,848	$ 362	0.24%	$ 177,786	$ 431	0.24%
Investment securities: (6)									
U.S. Treasury & Government-sponsored agencies (1)	**1,826,297**	**41,790**	**2.29**	1,969,590	52,369	2.66	2,150,562	77,208	3.59
States and political subdivisions (3)	**684,648**	**37,464**	**5.47**	580,851	34,135	5.88	536,295	33,181	6.19
Other securities	**214,556**	**8,162**	**3.80**	211,862	9,102	4.30	198,747	9,307	4.68
Total investment securities	**2,725,501**	**87,416**	**3.21**	2,762,303	95,606	3.46	2,885,604	119,696	4.15
Loans: (2)									
Commercial (3) (4)	**1,309,457**	**64,783**	**4.95**	1,326,746	63,953	4.82	1,271,515	56,153	4.42
Commercial real estate	**1,370,321**	**98,897**	**7.22**	1,308,401	78,912	6.03	1,007,636	44,992	4.47
Residential real estate (5)	**1,197,046**	**53,830**	**4.50**	847,722	41,267	4.87	464,676	26,209	5.64
Consumer, net of unearned income	**985,574**	**52,907**	**5.37**	961,072	58,314	6.07	1,007,390	62,849	6.24
Total loans (4) (5)	**4,862,398**	**270,417**	**5.56**	4,443,941	242,446	5.46	3,751,217	190,203	5.07
Total earning assets									