FIRST MERCHANTS CORP
Form DEF 14A
March 27, 2009

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

SCHEDULE 14A INFORMATION

PROXY STATEMENT PURSUANT TO SECTION 14(A) OF THE

SECURITIES EXCHANGE ACT OF 1934

Filed by the Registrant |X|

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Check the appropriate box:

|_| Preliminary Proxy Statement

|_| Confidential, For Use of the Commission Only (as permitted by Rule 14a-6(e)(2))

|X| Definitive Proxy Statement

|_| Definitive Additional Materials

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FIRST MERCHANTS CORPORATION

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March 27, 2009

FIRST MERCHANTS CORPORATION

PROXY STATEMENT FOR

ANNUAL MEETING OF SHAREHOLDERS

TO BE HELD MAY 6, 2009

To the shareholders of First Merchants Corporation:

This proxy statement has been made available to you on the Internet or has been sent to you via mail or email in connection with the solicitation on behalf of the Board of Directors (the "Board") of First Merchants Corporation ("First Merchants") of proxies to be voted at the annual meeting of First Merchants' shareholders to be held May 6, 2009. If you received a paper or electronic copy, the proxy materials also include a proxy card that can be used for voting your shares. The distribution of these proxy materials is expected to commence on or about March 27, 2009.

The purpose of this proxy solicitation includes voting on the following items, as stated in the accompanying notice of the annual meeting:

(1) To elect five directors, four to hold office for terms of three years and one to hold office for a term of one year; in each case, the directors will hold office until their successors are duly elected and qualified.

(2) To vote on an advisory, non-binding resolution approving the compensation of the First Merchants Corporation executive officers.

(3) To act on a proposal to approve the First Merchants Corporation 2009 Employee Stock Purchase Plan.

(4) To act on a proposal to approve the First Merchants Corporation 2009 Long-Term Equity Incentive Plan.

(5) To ratify the appointment of the firm of BKD, LLP as the independent auditor for 2009.

(6) To transact such other business as may properly come before the meeting.

This proxy statement contains information concerning each of the above voting items. Voting item 2 is new and merits additional explanation. First Merchants is participating in the U. S. Treasury Department's Capital Purchase Program (the "CPP") under the Emergency Economic Stabilization Act of 2008 (the "EESA"). First Merchants' decision to participate in the CPP was based on our conclusion that the Program offers a unique opportunity to add low cost capital to supplement our existing capital, which will allow us to remain well-capitalized while continuing to support economic growth in the markets we serve and provide additional protection against the uncertain duration and severity of the current economic downturn. On February 20, 2009, First Merchants received $116 million of equity capital under the CPP by issuing to the Treasury Department 116,000 shares of preferred stock paying cumulative dividends at a rate of 5% per year for the first 5 years and 9% per year thereafter, and a warrant to purchase up to 991,453 shares of First Merchants common stock, at an initial per share price of $17.55 (based on the market price for the stock during the 20 trading days preceding the Treasury Department's preliminary approval of First Merchants' participation in the CPP). The number of shares of common stock that can be purchased under the warrant will be reduced by 50% if First Merchants redeems at least 50% of the preferred stock within 3 years. Except under limited circumstances, such as if First Merchants were to fail to pay dividends on the preferred stock for an aggregate of 6 or more quarterly dividend periods, the preferred stock is non-voting. On February 17, 2009, President Obama signed into law the American Recovery and Reinvestment Act of 2009 (the "ARRA") which, among other things, amended the EESA by adding several requirements relating to executive compensation and corporate governance that are applicable to CPP participants, including First Merchants. One of these requirements is that the shareholders must have the opportunity to vote on a separate, non-binding resolution to approve the compensation of a CPP participant's executive officers, as disclosed and discussed in the participant's proxy statement, in the compensation discussion and analysis, the compensation tables, and related material. Voting item 2 fulfills this requirement. Further explanation of this voting item is contained on page 28. The Compensation Discussion and Analysis," the compensation tables, and related material are on pages 11-28.

This is the second year that we haven taken advantage of the Securities and Exchange Commission ("SEC") rule that allows companies to furnish their proxy materials over the Internet, enabling us to reduce the cost of delivering these materials and lessening the environmental impact of our annual meeting. Under this rule, we are mailing a Notice Regarding the Availability of Proxy Materials to most of our shareholders who haven't previously informed us that they prefer a paper copy of the proxy materials. The Notice contains instructions on how to access the proxy materials over the Internet. It also contains instructions on how shareholders may receive a paper or electronic copy of the proxy materials, including a proxy statement, annual report and a proxy card. Any shareholder who doesn't receive a Notice Regarding the Availability of Proxy Materials will receive a paper copy of the proxy materials by mail.

VOTING

Each share of First Merchants common stock issued and outstanding as of the close of business on February 27, 2009, the record date for the annual meeting, is entitled to be voted on all items being voted upon at the meeting. As of the close of business on February 27, 2009, there were 21,178,488 shares outstanding and entitled to vote.

You may vote shares held directly in your name as shareholder of record in person at the annual meeting. Even if you plan to attend the annual meeting, we recommend that you also vote by proxy as described below so that your vote will be counted if you later decide not to attend the meeting.

Whether you hold shares directly as the shareholder of record or through a broker, trustee or other nominee as the beneficial owner, you may direct how your shares are voted without attending the annual meeting. There are three ways to vote by proxy:

- **By Internet** – Shareholders who received a Notice Regarding the Availability of Proxy Materials may submit proxies over the Internet by following the instructions on the Notice. Shareholders who received a paper or electronic copy of a proxy card may submit proxies over the Internet by following the instructions on the proxy card.

- **By Telephone** – Shareholders who live in the United States or Canada may submit proxies by telephone by calling toll-free 1-800-690-6903 on a touch-tone telephone and following the instructions. Shareholders who received a Notice Regarding the Availability of Proxy Materials should have their Notice in hand when calling, and shareholders who received a paper or electronic copy of a proxy card should have the proxy card in hand when calling.

- **By Mail** – Shareholders who received a paper or electronic copy of a proxy card may submit proxies by mail by completing, signing and dating their proxy card and mailing it in the postage-paid envelope we have provided or return it to First Merchants Corporation, c/o Broadridge, 51 Mercedes Way, Edgewood, NY 11717.

After submitting a proxy, you have the right to revoke it any time before it is exercised by giving written notice of revocation to the Secretary received prior to the annual shareholders' meeting, by submitting a new proxy via Internet, telephone or mail, or by voting in person at the meeting. Your shares will be voted in accordance with your specific instructions given when submitting your proxies. In the absence of specific instructions to the contrary, proxies will be voted “for” election to the Board of all nominees listed in Item 1 of the proxy, “for” the proposal to approve the First Merchants Corporation 2009 Employee Stock Purchase Plan, “for” the proposal to approve the First Merchants Corporation 2009 Long-Term Equity Incentive Plan, and “for” ratification of the appointment of the firm of BKD, LLP as First Merchants’ independent auditor for 2009. If any director-nominee named in this proxy statement becomes unable or declines to serve (an event which the Board does not anticipate), the persons named as proxies will have discretionary authority to vote for a substitute nominee named by the Board, if the Board determines to fill such nominee’s position.

Each share of First Merchants common stock is entitled to one vote. Directors are elected by a plurality of the votes cast by the shares entitled to vote in the election at a meeting at which a quorum is present. Shareholders do not have a right to cumulate their votes for directors. The affirmative vote of a majority of the shares present and voting at the meeting in person or by proxy is required for approval of all items submitted to the shareholders for their consideration other than the election of directors. Abstentions will be counted for the purpose of determining whether a quorum is present but for no other purpose. Broker non-votes will not be counted. The Secretary will count the votes and announce the preliminary results of the voting at the annual meeting. The final results will be published in First Merchants’ quarterly report on Form 10-Q for the second quarter of 2009.

SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

Security Ownership of Certain Beneficial Owners

To the best of our knowledge, the following table shows the only beneficial owner of more than 5% of the outstanding common stock of First Merchants as of February 27, 2009.

Name and Address of Beneficial Owner	Amount and Nature of Beneficial Ownership	Percent of Class
Dimensional Fund Advisors LP 1299 Ocean Avenue Santa Monica, CA 90401	1,520,459[1]	7.18%

(1) Based on a Schedule 13G filing with the SEC, Dimensional Fund Advisors LP (“Dimensional”), an investment advisor registered under Section 203 of the Investment Advisors Act of 1940, furnishes investment advice to four investment companies registered under the Investment Advisors Act of 1940 and serves as investment manager to certain other commingled group trusts and separate accounts. These investment companies, trusts and accounts are the “Funds.” In its role as investment advisor or manager, Dimensional possesses investment and/or voting power over the shares of First Merchants common stock owned by the Funds and may be deemed to be the beneficial owner of these shares under rules of the SEC. However, all of these shares are owned by the Funds, and Dimensional disclaims beneficial ownership of such shares for any other purpose.

Security Ownership of Directors and Executive Officers

The following table lists the amount and percent of First Merchants common stock beneficially owned on February 27, 2009 by directors (including directors who are retiring as of the 2009 annual meeting of shareholders), director nominees, the Chief Executive Officer, the Chief Financial Officer, the three other most highly compensated executive officers, and by the directors and all of First Merchants' executive officers as a group. Unless otherwise indicated, the beneficial owner has sole voting and investment power. The information provided in the table is based on First Merchants' records and information filed with the SEC and provided to First Merchants.

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The number of shares beneficially owned by each person is determined under rules of the SEC, and the information is not necessarily indicative of beneficial ownership for any other purpose. Under those rules, beneficial ownership includes shares which a person has the right to acquire beneficial ownership of on or before April 28, 2009 (60 days after February 27, 2009) by exercising stock options ("Vested Options") awarded to participants under First Merchants' Long-term Equity Incentive Plan. It also includes shares of restricted stock ("Restricted Shares") awarded to participants under that Plan or under First Merchants' Equity Compensation Plan for Non-Employee Directors that are still subject to restrictions.

Beneficial Owner	**Amount and Nature of Beneficial Ownership**	**Percent of Class**
Thomas B. Clark	16,869(1)	*
Michael L. Cox	171,454(2)	*
Jerry R. Engle	42,436(3)	*
Roderick English	5,347(4)	*
Jo Ann M. Gora	5,347(5)	*
William L. Hoy	12,739(6)	*
Barry J. Hudson	459,892(7)	2.15%
Michael C. Rechin	45,746(8)	*
Charles E. Schalliol	13,177(9)	*
Patrick A. Sherman	5,550	*
Terry L. Walker	23,811(10)	*
Jean L. Wojtowicz	6,684(11)	*
Robert R. Connors	38,833(12)	*
Mark K. Hardwick	53,974(13)	*
David W. Spade	9,899(14)	*
Michael J. Stewart	3,868(15)	*
Directors and Executive Officers as a Group (19 persons)	955,039(16)	4.44%

* Percentage beneficially owned is less than 1% of the outstanding shares.

(1) Includes 10,413 shares that he has the right to acquire by exercising Vested Options.

(2) Includes 52,754 shares held jointly with his spouse, Sharon Cox, and 110,948 shares that he has the right to acquire by exercising Vested Options.

(3) Includes 1,600 Restricted Shares and 37,424 shares held jointly with his spouse, Terri Engle.

(4) Includes 719 Restricted Shares and 4,628 shares that he has the right to acquire by exercising Vested Options.

(5) Includes 719 Restricted Shares and 4,628 shares that she has the right to acquire by exercising Vested Options.

(6) Includes 719 Restricted Shares, 917 shares that he holds as custodian for his daughter, and 1,157 shares that he has the right to acquire by exercising Vested Options.

(7) Includes 719 Restricted Shares, 327,756 shares owned by Mutual Security, Inc., 10,024 shares held jointly with his spouse, Elizabeth Hudson, 43,521 shares held by his spouse, 13,626 shares held by his spouse as custodian for his children and 16,478 shares that he has the right to acquire by exercising Vested Options.

(8) Includes 7,000 Restricted Shares and 30,000 shares that he has the right to acquire by exercising Vested Options.

(9) Includes 1,349 Restricted Shares and 4,628 shares that he has the right to acquire by exercising Vested Options.

(10) Includes 810 Restricted Shares, 13,611 shares held jointly with his spouse, Cheryl L. Walker, 551 shares held by his spouse and 2,314 shares that he has the right to acquire by exercising Vested Options.

(11) Includes 899 Restricted Shares and 5,785 shares that she has the right to acquire by exercising Vested Options.

(12) Includes 3,600 Restricted Shares, 722 shares held jointly with his spouse, Ann Connors, and 31,056 shares that he has the right to acquire by exercising Vested Options.

(13) Includes 5,100 Restricted Shares, 401 shares held by his spouse, Catherine Hardwick, and 40,658 shares that he has the right to acquire by exercising Vested Options.

(14) Includes 2,000 Restricted Shares, 193 shares held jointly with his spouse, Sandra Spade, and 4,000 shares that he has the right to acquire by exercising Vested Options.

(15) Includes 3,000 Restricted Shares and 750 shares held in a joint trust with his spouse, Barbara Stewart.

(16) Includes 36,534 Restricted Shares and 293,470 shares that First Merchants' directors and executive officers have the right to acquire by exercising Vested Options.

INFORMATION REGARDING DIRECTORS

VOTING ITEM 1 – ELECTION OF DIRECTORS

First Merchants' Bylaws allow the Board to fix the number of directors by resolution. The Board has fixed the number of directors as of the 2009 annual meeting of shareholders at eleven. The Board is divided into three classes serving staggered three-year terms or until their successors are elected and qualified. Directors for each class are elected at the annual meeting of shareholders held in the year in which the term for their class expires; except that directors filling vacancies caused by resignation, death or other incapacity, or an increase in the number of directors, are elected by majority vote of the Board until the next annual meeting of shareholders.

Five directors will be elected at the annual meeting. Three of the five persons who have been nominated for election to the Board are currently members of the Board. They include William L. Hoy and Barry J. Hudson, who have been nominated to serve three-year terms in Class III that expire as of the 2012 annual meeting of shareholders, and Michael J. Rechin, who has been nominated to serve a one-year term in Class I that expires as of the 2010 annual meeting of shareholders. Mr. Rechin was previously in Class III but is moving to Class I so that the classes will be as nearly equal in number as possible. The other two nominees, Jerry R. Engle and Patrick A. Sherman, are former directors of Lincoln Bancorp ("Lincoln") who have been nominated for election to the Board for three-year terms in Class III that expire as of the 2012 annual meeting of shareholders, under an Agreement of Reorganization and Merger between First Merchants and Lincoln dated as of September 2, 2008. The Agreement provides that First Merchants will take all necessary action to cause Mr. Engle, who was the Chairman of the Board of Directors, President and Chief Executive Officer of Lincoln, and another current director of Lincoln chosen by First Merchants to be nominated for election as members of First Merchants' Board for a 3-year term at the first annual meeting of the shareholders of First Merchants following the merger of Lincoln into First Merchants. Mr. Sherman is the other director of Lincoln who was chosen by First Merchants to be nominated for election as a member of First Merchants' Board. There are no family relationships among First Merchants' executive officers and directors.

The following persons have been nominated for election to the Board:

Name, Age and Prior Service	**Business Experience (Past 5 Years)**
Class III (Terms expire 2012):	
Jerry R. Engle age 64 New director	Mr. Engle was the Chairman of the Board of Directors, President and Chief Executive Officer of Lincoln and the President and Chief Executive Officer of its wholly owned subsidiary, Lincoln Bank, from 2005 to 2008. From 2004 to 2005 he was Vice Chairman of Lincoln's Board and Executive Vice President and Chief Operating Officer of Lincoln Bank. On April 17, 2009, Lincoln Bank will be merged into First Merchants Bank of Central Indiana, National Association ("FMBCI"), a wholly owned subsidiary of First Merchants, and Mr. Engle will become the Indianapolis Regional President of FMBCI.
William L. Hoy age 60 Director since 2007	Chief Executive Officer of The Columbus Sign Company, a custom sign and graphic fabricator, since 1990, and Vice President and Treasurer of Innocom Corporation, an environmental graphic design and custom display company, since 1992.
Barry J. Hudson age 69 Director since 1999	Retired Chairman of the Board of Directors, President and Chief Executive Officer of First National Bank of Portland, a wholly owned subsidiary of First Merchants that was merged with First Merchants Bank, National Association, another wholly owned subsidiary of First Merchants, in 2007.
Patrick A. Sherman age 61 New director	Partner, Sherman & Armbruster certified public accountants, since 1975.
Class I (Term expires 2010):	
Michael C. Rechin age 50	President and Chief Executive Officer of First Merchants since 2007, and Executive Vice President and Chief Operating Officer of First Merchants from 2005 to 2007. Mr. Rechin was Executive Vice President of National City Bank of Indiana from 1995 to 2005.

Director since 2005

THE BOARD RECOMMENDS THAT SHAREHOLDERS VOTE "FOR" THE ELECTION OF EACH NOMINEE FOR DIRECTOR NAMED ABOVE.

The First Merchants directors whose terms are not expiring as of the 2009 annual meeting of shareholders are listed below. They will continue to serve as directors for the remainder of their terms or until otherwise provided in First Merchants' Bylaws. Information regarding each of the continuing directors is provided below.

Continuing Directors

The following persons will continue to serve as directors:

Name, Age and Prior Service	**Business Experience (Past 5 Years)**
Class I (Terms expire 2010):	
Charles E. Schalliol age 61 Director since 2004	Of counsel, Baker & Daniels LLP law firm, since 2007. Mr. Schalliol was Director, Indiana State Office of Management and Budget, from 2005 to 2007, President and Chief Executive Officer of BioCrossroads, an economic development organization focused on life sciences companies, from 2003 to 2005, Executive Director, Corporate Finance & Investment Banking, Eli Lilly and Company, a pharmaceuticals company, from 1996 to 2003, and Founder and Managing Director of Lilly Venture Funds from 1999 to 2003. Mr. Schalliol is also a director of Heritage-Crystal Clean, Inc., which is listed on the NASDAQ Stock Market.
Terry L. Walker age 62 Director since 2006	Chairman of the Board of Directors and Chief Executive Officer, Muncie Power Products, Inc., a manufacturer and distributor of power take-offs and hydraulic components for the truck equipment industry, since 2005. Mr. Walker was Muncie Power's President from 2000 to 2008 and its Chief Operating Officer from 2000 to 2005.
Class II (Terms expire 2011):	
Thomas B. Clark age 63 Director since 1989	Retired Chairman of the Board of Directors, President and Chief Executive Officer, Jarden Corporation, a provider of niche consumer products for the home.
Roderick English age 57 Director since 2005	President and Chief Executive Officer, The James Monroe Group, LLC, a provider of business management and consulting services, since 2006. Mr. English was Senior Vice President of Human Resources and Communications, Remy International, Inc. (formerly, Delco Remy International, Inc.), a manufacturer of electrical and powertrain products for autos, trucks and other vehicles, from 1994 to 2006.

Jo Ann M. Gora age 63 Director since 2004	President, Ball State University, since 2004. Dr. Gora served as Chancellor of the University of Massachusetts at Boston from 2001 to 2004. She was Provost and Vice President for Academic Affairs at Old Dominion University from 1992 to 2001.
Jean L. Wojtowicz age 51 Director since 2004	President and Chief Executive Officer, Cambridge Capital Management Corp., a manager of non-traditional sources of financing, since 1983. Ms. Wojtowicz is also a director of Vectren Corporation, which is listed on the New York Stock Exchange.

Retiring Director

Michael L. Cox is a current director of First Merchants and is retiring as such effective May 6, 2009, the date of the 2009 annual meeting of shareholders. He is retiring as a director in accordance with the provisions of an agreement entered into between Mr. Cox and First Merchants on January 23, 2007, concerning his retirement as the President and CEO of First Merchants. Under the terms of this agreement, Mr. Cox retired as the

President and CEO of First Merchants on April 24, 2007. He has provided services to First Merchants as a nonemployee consultant since his retirement, and he will continue to do so until April 24, 2009. In his capacity as a consultant, he reports directly to Michael C. Rechin, First Merchants' President and CEO, and performs services as requested by Mr. Rechin. These services generally include, among other things, advice and assistance with matters relating to mergers, acquisitions and other business expansion initiatives. Mr. Cox has also continued to represent First Merchants as the Past Chairman of the Board of Directors of the Indiana Bankers Association, and as a director of the Indiana State Chamber of Commerce. These services generally do not occupy more than 50% of Mr. Cox's time. He was paid $175,000 in the first year and is being paid $100,000 in the second year for these services, in substantially equal monthly installments.

Meetings of the Board

The Board held 6 meetings during 2008. All of the directors except Barry J. Hudson attended at least 75% of the total number of meetings of the Board and the committees on which they served. Mr. Hudson attended 6 of the 9 meetings (66 2/3%) of the Board and the committees on which he served during 2008.

Directors' Attendance at Annual Meeting of Shareholders

First Merchants' directors are encouraged to attend the annual meeting of shareholders. At the 2008 annual meeting, all 11 directors were in attendance.

Board Independence

The Board has determined that each of First Merchants' directors and director-nominees is an "independent director," as defined in the NASDAQ Stock Market Rules, except for Michael C. Rechin, First Merchants' President and Chief Executive Officer, and Jerry R. Engle, Indianapolis Regional President of FMBCI.

All of the members of the Nominating and Governance Committee, the Compensation and Human Resources Committee, and the Audit Committee are "independent directors," as defined in the NASDAQ Stock Market Rules.

Shareholder Communications with the Board

Shareholders may communicate with the Board by e-mail at *bod@firstmerchants.com*. All such e-mails will be automatically forwarded to the Chairperson of the Nominating and Governance Committee, Thomas B. Clark, who will arrange for such communications to be relayed to the other directors.

COMMITTEES OF THE BOARD

Standing Committees/Committee Charters

The Board's standing committees are the Audit Committee, the Nominating and Governance Committee, and the Compensation and Human Resources Committee. Each of these Committees has a charter, which is included among the documents under "Corporate Governance Disclosures" on First Merchants' website at *http://www.firstmerchants.com/about-us.cfm*. The following information is provided regarding the composition, functions and number of meetings held by these committees in 2008:

Audit Committee

The Audit Committee is composed of directors Jean L. Wojtowicz (Chairperson), Thomas B. Clark, William L. Hoy and Terry L. Walker. The Committee met 8 times during 2008. The Audit Committee assists the Board in overseeing senior management's efforts to monitor, mitigate and manage all types of risk to the organization through (1) the integrity of the accounting, compiling and reporting of financial statements and other financial information that the Corporation provides to governmental bodies and the public; (2) the Corporation's compliance with legal and regulatory requirements; (3) the independent auditor's qualifications and independence; (4) the performance of the Corporation's independent auditor and the internal audit function; and (5) the Corporation's compliance with ethical requirements. The Audit Committee has the sole authority to appoint, retain, compensate, evaluate and terminate the independent auditor (subject to shareholder ratification) and the senior internal audit executive. The Audit Committee reviews and discusses with management and the external auditor First Merchants' audited financial statements and, based on this review, makes a recommendation to the Board on inclusion of these financial statements in First Merchants' annual report on Form 10-K. In accordance with SEC rules, First Merchants has identified Ms. Wojtowicz and Mr. Clark as "Audit Committee financial experts." They are both "independent directors" as that term is used in the NASDAQ Stock Market Rules.

Audit Committee Report Concerning Audited Financial Statements

The Audit Committee has reviewed and discussed First Merchants' audited financial statements for 2008 with management. The Audit Committee has discussed with the independent auditor, BKD, LLP, the matters required to be discussed by the Statement on Auditing Standards No. 61, as amended (AICPA, Professional Standards, Vol. 1. AU Section 380), as adopted by the Public Company Accounting Oversight Board ("PCAOB") in Rule 3200T. The Audit Committee has received the written disclosures and the letter from the independent auditor required by the applicable requirements of the PCAOB regarding the independent auditor's communications with the Audit Committee concerning independence and has discussed with the independent auditor the independent auditor's independence. Based on these reviews and discussions, the Audit Committee recommended to the Board that the audited financial statements be included in First Merchants' Annual Report on Form 10-K for the 2008 fiscal year for filing with the SEC.

The above report is submitted by:

FIRST MERCHANTS CORPORATION AUDIT COMMITTEE

Jean L. Wojtowicz, Chairperson

Thomas B. Clark

William L. Hoy

Terry L. Walker

Nominating and Governance Committee

The Nominating and Governance Committee is composed of directors Thomas B. Clark (Chairperson), Jo Ann M. Gora, Charles E. Schalliol and Jean L. Wojtowicz. The Committee met 2 times during 2008. The Nominating and Governance Committee's goal is to ensure the Board's continued and enhanced effectiveness and independence. It oversees First Merchants' compliance with laws and regulations that relate to its governance structure and processes, including those of the SEC and NASDAQ, makes recommendations concerning the size and composition of the Board, as well as criteria for Board membership, reviews the credentials of persons suggested as prospective directors, nominates persons to serve as directors and as officers of the Board, provides for periodic self-assessment of the Board's effectiveness, and reviews and makes recommendations for changes to First Merchants' Code of Business Conduct and the Code of Ethics for Senior Financial Officers. The Code of Business Conduct and the Code of Ethics for Senior Financial Officers are included among the documents under "Corporate Governance Disclosures" on First Merchants' website at *http://www.firstmerchants.com/about-us.cfm*.

In nominating persons to serve as directors, the Nominating and Governance Committee considers the person's ethical character, reputation, relevant expertise and experience, accomplishments, leadership skills, demonstrated business judgment, contribution to Board diversity, "independence" (as defined in the NASDAQ Stock Market Rules) if a non-employee director, residence in First Merchants' market area, ability and willingness to devote sufficient time to director responsibilities, and willingness to maintain a meaningful ownership interest in First Merchants and assist First Merchants in developing new business. For incumbent directors whose terms are expiring, the Nominating and Governance Committee also considers the quality of their prior service to First Merchants, including the nature and extent of their participation in First Merchants' governance and their contributions of management and financial expertise and experience to the Board and

First Merchants. For new director candidates, the Committee also considers whether their skills are complementary to those of existing Board members and whether they will fulfill the Board's needs for management, financial, technological or other expertise. The Nominating and Governance Committee considers candidates coming to its attention through current Board members, search firms, shareholders and other persons.

Article IV, Section 9, of First Merchants' Bylaws, describes the process by which a shareholder may suggest a candidate for consideration by the Nominating and Governance Committee as a director nominee. Under this process, a suggestion by a shareholder of a director nominee must include: (a) the name, address and number of First Merchants shares owned by the shareholder; (b) the name, address, age and principal occupation of the suggested nominee; and (c) such other information concerning the suggested nominee as the shareholder may wish to submit or the Committee may reasonably request. A suggestion for a director nominee submitted by a shareholder must be in writing and delivered or mailed to the Secretary, First Merchants Corporation, 200 East Jackson Street, Muncie, Indiana 47305. Suggestions for nominees from shareholders are evaluated in the same manner as other nominees.

Of the directors and director nominees that the Nominating and Governance Committee approved for inclusion on First Merchant's proxy card for the 2009 annual meeting of shareholders, William L. Hoy, Barry J. Hudson and Michael C. Rechin are directors standing for re-election, and Jerry R. Engle and Patrick A. Sherman were nominated under a provision in the Agreement of Reorganization and Merger between First Merchants and Lincoln dated as of September 2, 2008 requiring that Mr. Engle and another Lincoln director chosen by First Merchants would be nominated for election to the Board for a 3-year term.

Compensation and Human Resources Committee

The Compensation and Human Resources Committee is composed of directors Charles E. Schalliol (Chairperson), Thomas B. Clark and Roderick English. The Committee met 2 times during 2008. The Committee establishes First Merchants' general compensation philosophy, oversees the development and implementation of policies and programs to carry out this compensation philosophy, and evaluates the effectiveness of these policies and programs, in consultation with senior management. The Committee recommends to the Board the compensation to be paid to First Merchants' non-employee directors.

The Compensation and Human Resources Committee reviews the performance of and approves the compensation and benefits to be paid to First Merchants' executive officers and senior management employees and the chief executive officers and regional presidents of its subsidiaries. In so doing, the Committee relies in part on the recommendations of the President and Chief Executive Officer, Michael C. Rechin, and other executive officers, as appropriate, concerning the performance, compensation and benefits of First Merchants' executive officers (other than themselves) and senior management employees, as well as the chief executive officers and regional presidents of First Merchants' subsidiaries. The Committee has delegated its authority to review the performance of and approve the compensation and benefits to be paid to other employees of First Merchants and its subsidiaries to Mr. Rechin and the respective chief executive officers of First Merchants' subsidiaries.

The Compensation and Human Resources Committee recommends to the Board the adoption, amendment and termination of First Merchants' incentive compensation, equity-based compensation and deferred compensation plans; and it administers or oversees the administration of these plans, the day-to-day administrative responsibilities having been delegated to senior management, including President and CEO, Michael C. Rechin, and the Senior Vice President and Director of Human Resources, Kimberly J. Ellington. The plans that are being submitted for shareholder approval at the 2009 annual meeting – the First Merchants Corporation 2009 Employee Stock Purchase Plan and the First Merchants Corporation 2009 Long-Term Equity Incentive Plan – will be administered by the Committee.

The Compensation and Human Resources Committee is authorized to directly engage counsel and consultants, including compensation consultants, to assist it in carrying out its responsibilities. The Committee has used compensation consultants in the past to conduct market assessments and to make recommendations concerning

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additions or changes to compensation programs and plan designs, but it did not do so during 2007 or 2008. From time to time Mr. Rechin and Ms. Ellington provide information to the Committee and make recommendations, on their own initiative or as requested by the Committee, concerning existing and proposed compensation policies and programs for executives and other employees of First Merchants and its subsidiaries.

Compensation and Human Resources Committee Interlocks and Insider Participation

No member of the Compensation and Human Resources Committee – Charles E. Schalliol, Thomas B. Clark or Roderick English – was an officer or employee of First Merchants or any of its subsidiaries during 2008. None of these members has ever been an officer or employee of First Merchants or any of its subsidiaries. No member of the Compensation and Human Resources Committee or executive officer of First Merchants had a relationship during 2008 requiring disclosure in this proxy statement under SEC regulations.

Compensation and Human Resources Committee Report

The Compensation and Human Resources Committee has reviewed and discussed with management the Compensation Discussion and Analysis required by SEC regulations (set forth immediately following this report under “Compensation of Executive Officers”). Based on this review and discussion, the Compensation and Human Resources Committee recommended to the Board that the Compensation Discussion and Analysis be included in First Merchants’ proxy statement on Schedule 14A and incorporated by reference in First Merchants’ annual report on Form 10-K for the fiscal year ended December 31, 2008.

The above report is submitted by:

FIRST MERCHANTS CORPORATION COMPENSATION AND HUMAN RESOURCES COMMITTEE

Charles E. Schalliol (Chairperson)

Thomas B. Clark

Roderick English

COMPENSATION OF EXECUTIVE OFFICERS

Compensation Discussion and Analysis

The Compensation and Human Resources Committee is responsible for the design, implementation and evaluation of First Merchants’ executive compensation programs, aided by the company’s CEO, CFO, the Director of Human Resources, and other employees and outside advisors as the Committee deems necessary or helpful. The compensation programs are designed to reward excellent performance and to provide incentives to achieve current and long-term strategic goals, with the ultimate objective of achieving a superior return on shareholders’ investment. The programs are intended to be competitive with other companies’ programs in order to attract and retain the most qualified executives.

In its choices of compensation programs, the Committee tries to strike an appropriate balance between cash and non-cash compensation. The material elements of these programs are salary, non-equity incentive pay, equity-based compensation, including both restricted stock awards and stock options, retirement benefits, and change of control agreements. Salary and non-equity incentive pay advance shorter-term goals by providing an immediate or near-term reward for exceptional performance, whereas equity-based compensation is designed to reward the accomplishment of longer-term goals and to further align executive officers' financial interests with those of other shareholders by tying the value of such compensation to sustained increases in the price of First Merchants stock. The retirement plans, the vesting provisions in equity-based compensation, and the change of control agreements increase the company's ability to retain executives.

For 2008, First Merchants' "Named Executive Officers" ("NEOs") and their titles were:

- Michael C. Rechin, the President and Chief Executive Officer;
- Mark K. Hardwick, the Executive Vice President and Chief Financial Officer;
- Michael J. Stewart, the Executive Vice President and Chief Banking Officer;
- Robert R. Connors, the Senior Vice President and Chief Information Officer; and
- David W. Spade, the Senior Vice President and Chief Credit Officer.

The following paragraphs discuss each of the material elements of the compensation awarded to, earned by, or paid to these NEOs during 2008, with references to information contained in the compensation tables and related material on pages 20-28, as appropriate. The compensation tables generally contain information concerning the NEOs' compensation through December 31, 2008; however, a complete understanding of First Merchants' compensation programs going forward requires consideration of important developments during the first two months of 2009 that will affect some elements of the NEOs' compensation. They relate to First Merchants' participation in the U. S. Treasury Department's Capital Purchase Program (the "CPP") under the Emergency Economic Stabilization Act of 2008, as further described on page 1 of this proxy statement. In order for First Merchants to participate in the CPP, during the period that preferred stock issued to the Treasury Department under the CPP remains outstanding, First Merchants' compensation programs for executive officers must comply with the standards applicable to CPP participants. They include the following restrictions imposed by the American Recovery and Reinvestment Act of 2009 (the "ARRA"), which was signed into law on February 17, 2009:

(1) Compensation must exclude incentives for the NEOs to take unnecessary and excessive risks that threaten First Merchants' value.

(2) First Merchants must implement provisions to recover any bonus, retention award or incentive compensation paid to NEOs and any of the next 20 most highly-compensated employees based on statements of earnings, revenues, gains or other criteria that are later found to be materially inaccurate.

(3) First Merchants must prohibit any compensation plan that would encourage manipulation of the company's reported earnings to enhance the compensation of any of its employees.

(4) First Merchants is prohibited from making "golden parachute payments" or severance payments (essentially, any payment for departure from the company for any reason, except for payments for services performed or benefits accrued) to an NEO or any of the next 5 most highly-compensated employees.

(5) First Merchants is prohibited from paying or accruing any bonus, retention award or incentive compensation to the NEOs, except that long-term restricted stock may be paid if that stock (i) doesn't fully vest while the preferred stock remains outstanding, (ii) has a value that doesn't exceed 1/3 of the receiving employee's total annual compensation, and (iii) is subject to such other terms as the Secretary of the Treasury may determine is in the public interest. A bonus payment required to be paid pursuant to a written employment contract executed on or before February 11, 2009 is not prohibited under this standard.

(6) The Compensation and Human Resources Committee must meet at least semi-annually to discuss and evaluate employee compensation plans in light of an assessment of any risk posed to First Merchants by such plans.

(7) The Board must establish a company-wide policy regarding excessive or luxury expenditures, which may include excessive expenditures on (i) entertainment or events, (ii) office and facility renovations, (iii) aviation or other transportation services, or

(iv) other activities or events that are not reasonable expenditures for conferences, staff development, reasonable performance incentives, or other similar measures conducted in the normal course of the company's business operations.

(8) First Merchants is subject to a $500,000 cap on deductibility of annual compensation for each of its NEOs under the provisions of Internal Revenue Code Section 162(m)(5).

(9) First Merchants' CEO and CFO must provide a written certification of compliance with the above CPP standards and file this certification with the SEC with the annual filings required under securities laws.

The Treasury Department has not yet provided much guidance concerning the interpretation and application of the restrictions imposed by the ARRA, so it is possible that the NEOs' compensation will be affected by these restrictions in ways that are not apparent at the present time. The Treasury Department may issue additional rules and regulations in the future that will restrict or otherwise affect the compensation of executives of CPP participants. For these reasons, the discussion of the NEOs' compensation in this section of the proxy statement may be altered by subsequent developments. Each of the NEOs has acknowledged in a letter agreement with First Merchants that his compensation will be subject to the standards and restrictions applicable to executive officers of CPP participants during the period that the preferred stock issued to the Treasury Department remains outstanding.

The material elements of First Merchants' compensation programs are discussed below.

Salaries.

The Compensation and Human Resources Committee annually reviews the NEOs' salaries each February, after First Merchants' audited financial statements for the preceding fiscal year have been issued. Salary adjustments, if any, approved by the Committee become effective as of the first payroll in March. The Committee believes that, by waiting until the financial statements are issued, salary adjustments for the NEOs can be more accurately and effectively tied to their success in meeting financial targets and other strategic goals for the fiscal year just ended. It also allows First Merchants to communicate decisions concerning salary adjustments to the NEOs at the same time as those related to incentive plan payments and equity-based awards, thus ensuring a clear and consistent message regarding performance and underlining First Merchants' emphasis on growing a performance-based culture.

The Compensation and Human Resources Committee does not "benchmark" the NEOs' salaries, which the SEC defines as using compensation data about other companies as a reference point on which, either wholly or in part, to base, justify or provide a framework for a compensation decision. However, the Committee does rely on broad-based third party surveys, particularly those that include financial institutions of a similar size and/or geographic location as First Merchants, to gain a general understanding of current compensation practices. The Committee determines the NEOs' salaries subjectively, based mostly on their responsibilities and the Committee's review of their individual performance and contributions to First Merchants' performance – especially its long-term and short-term financial performance. In assessing the performance of the NEOs other than the CEO, the Committee relies heavily on the recommendations of the CEO. The Committee has the sole responsibility for assessing the CEO's performance and establishing his salary. In determining the NEOs' salaries, the Committee also takes into account their experience, budgetary considerations, and the salaries paid to executives holding similar positions with First Merchants' competitors in the financial services industry. The Committee believes, on the basis of the information it has compiled through surveys and otherwise that Messrs. Rechin and Hardwick's salaries as CEO and CFO, respectively, of First Merchants are below the median for executives holding similar positions with comparably-sized institutions in the financial services industry, taking into consideration levels of experience and performance. For this reason, as the Summary Compensation Table shows, they have been granted larger than usual salary increases over the past three years with the intent of moving them closer to the median and recognizing their worth to First Merchants and the importance of retaining them.

Mr. Rechin's 2007 salary of $309,423 was based on an annual salary of $275,000 until April 24, 2007, when he was promoted from Executive Vice President and COO to President and CEO. Thereafter, it was based on an annual salary of $325,000, in recognition of his additional responsibilities. In 2008, his salary was increased to $350,000, a 7.7% increase from $325,000, in recognition of the level of his performance since becoming CEO. Mr. Hardwick's salary for 2007 was $209,000; and it was increased to $250,000 in 2008, a 19.6% increase. Mr. Hardwick's increase was based in part on his performance and in part on the Committee's belief that the larger increase was merited in order to compensate him at a level closer to the salaries paid to executives with similar responsibilities at other companies. First Merchants hired Mr. Stewart in January 2008 as its first Chief Banking Officer. He came to First Merchants with substantial valuable and relevant experience with other financial institutions. His 2008 salary as one of the company's two Executive Vice Presidents, was based on an annual salary of $245,000 – nearly the same as the salary paid to Mr. Hardwick, First Merchants' other Executive Vice President. Mr. Connors' 2007 salary of $192,200 was increased to $199,900 in 2008, a 4.0% increase. Mr. Spade's 2007 salary of $175,000 was increased to $180,700 in 2008, a 3.3% increase. These increases were generally in line with the merit increases given to the company's other senior management employees in 2008.

As national and international economic conditions became increasingly worse during 2008, especially in the financial services industry, financial plans and goals adopted prior to the beginning of the year became increasingly difficult to meet. While First Merchants had net income after income taxes totaling $20.6 million in 2008, performing significantly better than most other financial institutions, its diluted earnings per share decreased to $1.14 from $1.73 per share in 2007. In consideration of the uncertain economic environment that is likely to continue throughout the current year and perhaps into 2010, First Merchants has decided not to increase senior management salaries, including those of the NEOs, for 2009. The Committee recognizes that in normal times, applying normal standards, the NEOs' 2008 performance would uniformly justify merit salary increases; however, it is apparent that the present circumstances are unique and that it is in the best interests of First Merchants and its shareholders to not increase executive salaries for 2009. If the economy, and First Merchants' financial performance, improves more rapidly than presently expected, the Committee may review this decision prior to its next scheduled review in February 2010.

The restrictions imposed by the ARRA include a $500,000 cap on the deductibility of annual compensation under the provisions of Internal Revenue Code Section 162(m)(5). None of the NEOs' annual compensation presently exceeds this limit.

Non-Equity Incentive Pay.

Non-equity incentive compensation is available to the NEOs through the First Merchants Corporation Senior Management Incentive Compensation Program, which affords them the opportunity to earn additional cash compensation, determined as a percentage of their salaries, as incentive pay by meeting individual goals that are closely related to First Merchants' financial success. Under the Program, at the beginning of each year – no later than February – the NEOs are given targets they must meet in order to receive a payout of 100% of their assigned percentage the following February. The Compensation and Human Resources Committee determines the payments for a fiscal year and approves their payment after First Merchants' audited financial statements for the year have been issued, contemporaneously with its determination of salaries, equity compensation, and the parameters of the Senior Management Incentive Compensation Program for the following year. An NEO must be employed at the time the payment is due under the Program, except in the case of the NEO's death, disability or retirement. There are thresholds under the Program below which no payout is made, as well as maximum payouts that are larger than the target payouts. The amounts paid out increase on the basis of a pre-established schedule between the thresholds and the targets and the targets and the maximum payouts. The Committee has the authority to modify the Program, make final award determinations, set conditions for eligibility and awards, define extraordinary accounting events in calculating earnings, establish future payout schedules, determine circumstances and causes for which payouts can be withheld, and abolish the Program.

The Committee has determined that it would be in the long-term financial interest of First Merchants and its shareholders to base the target payouts to Messrs. Rechin, Hardwick and Stewart under the Senior

Management Incentive Compensation Program entirely on year-over-year growth in First Merchants' earnings per share, calculated on a diluted GAAP basis. For 2008, the Committee established Messrs. Rechin, Hardwick and Stewart's incentive payments under the Program for meeting their targets at 45%, 40% and 40%, respectively, of their salaries. The Committee established the target at which they would receive these payments at a 10% increase in earnings per share, with a threshold of a 3% increase in earnings per share below which no payment would be made and a maximum of a 20% increase that would earn a payment of twice the target amount. The range of payments that were possible for Messrs. Rechin, Hardwick and Stewart under the Program for 2008 is shown in the Grants of Plan-Based Awards Table on page 22. As the Summary Compensation Table on page 21 shows, Messrs. Rechin and Hardwick received payments of $69,620 and $41,800, respectively, under the Program for 2007 based on First Merchants' earnings per share increase of about 5% over 2006. However, since First Merchants' earnings per share decreased between 2007 and 2008, they did not receive a payment under the Program for 2008.

For 2008, the target payouts to Messrs. Connors and Spade under the Program were based 80% on First Merchants' year-over-year growth in First Merchants' earnings per share, calculated on a diluted GAAP basis, and 20% on their accomplishment of personal objectives assigned by the CEO at the beginning of the year. The Committee established the incentive payouts for both of them for meeting their targets at 30% of their salaries. The earnings per share targets and thresholds and maximums were the same for Messrs. Connors and Spade as for Messrs. Rechin, Hardwick and Stewart. Whether they accomplished all or part of their personal objectives was determined by the CEO. The range of payouts that were possible for Messrs. Connors and Spade under the Program for 2008 is shown in the Grants of Plan-Based Awards Table on page 22. Their maximum payouts were 170% of their target amounts due to the inclusion of the personal objectives component in their payout calculations. As the Summary Compensation Table on page 21 shows, Messrs. Connors and Spade received payments for 2007 of $37,479 and $30,188, respectively, based on First Merchants' earnings per share increase over 2006 and their accomplishment of personal objectives. For 2008, while neither Mr. Connors nor Mr. Spade received a payment based on their earnings per share targets due to the decrease in First Merchants' earnings per share between 2007 and 2008, Mr. Connors received $11,520 under the Program because he accomplished all of his personal objectives and Mr. Spade received $6,180 because he accomplished part of his personal objectives.

The NEOs will continue to be covered by the Senior Management Incentive Compensation Program for 2009, with each NEO being eligible for a payment of the same percentage of his salary for meeting his target as in 2008 – that is, 45%, 40%, 40%, 30% and 30% for Messrs. Rechin, Hardwick, Stewart, Connors and Spade, respectively; and all of the payouts for Messrs. Rechin, Hardwick and Stewart, and 80% of the payouts for Messrs. Connors and Spade will be based on the year-over-year growth in First Merchants' earnings per share, calculated on a diluted GAAP basis, from 2008. The Compensation and Human Resources Committee made two changes to the Program for 2009 that may affect the NEOs' payouts. First, the schedule for incentive payouts based on First Merchants' year-over-year growth in First Merchants' earnings per share was changed. The target earnings per share increase, at which the pre-established percentage of the NEOs' salary will be paid, will continue to be 10%; however, the schedule for payouts above the target up to the maximum has been changed to require incrementally higher earnings per share increases in order for an NEO to earn a larger payout; e.g., for an NEO to earn the maximum payment of twice the targeted payout, First Merchants' earnings per share would have to increase by 50% compared to 20% under the 2008 schedule. The reason for this change is that a greater earnings per share percentage increase for 2009 is more achievable than it was for 2008 because the base is lower due to the decrease in earnings per share between 2007 and 2008. Second, for Messrs. Connors and Spade only, the other 20% of their payouts will be tied to improving First Merchants' consolidated efficiency ratio instead of being based on their accomplishment of personal objectives as it was in 2008. The Committee and the CEO believe this incentive is more in line with their responsibilities and, since it can be measured objectively, is preferable to a reward for accomplishing personal objectives – which often involves a subjective element.

The restrictions imposed by the ARRA includes a requirement that NEOs' compensation must exclude incentives to take unnecessary and excessive risks that threaten First Merchants' value. The Compensation and Human Resources Committee is required to meet at least semi-annually to discuss and evaluate employee compensation plans in light of an assessment of any risk posed to First Merchants by such plans. The

Committee does not presently believe that First Merchants' incentive compensation program provide any incentives for NEOs to take unnecessary or excessive risks that threaten First Merchants' value, in view of theSenior Management Incentive Compensation Program's reliance on year-over-year earnings per share increases as the sole (or, in the cases of Messrs. Connors and Spade, principal) basis for determining incentive payouts. The Program is intended to reward First Merchants' long-term growth in a way that would normally result in improvement in its market value as reflected in its share price. Nevertheless, the Committee plans to meet at least semi-annually with First Merchants' CEO, CFO and Chief Risk Officer to discuss and evaluate the company's employee compensation plans and assess the types and level of risk posed by these plans.

The ARRA also prohibits First Merchants from paying or accruing any bonus, retention award or incentive compensation to the NEOs while preferred stock issued to the Treasury Department under the CPP remains outstanding. However, notwithstanding this prohibition, First Merchants may pay compensation to the NEOs in the form of long-term restricted stock if that stock (i) doesn't fully vest while the preferred stock remains outstanding, (ii) has a value that doesn't exceed 1/3 of the receiving NEO's total annual compensation, and (iii) is subject to such other terms as the Secretary of the Treasury may determine is in the public interest. A bonus payment required to be paid pursuant to a written employment contract executed on or before February 11, 2009 is also permitted under this standard. It appears that this standard will affect the incentive compensation payable to the NEOs under the Senior Management Incentive Compensation Program by requiring that, rather than being paid in cash as the Program provides, any payout earned under the Program be paid to the NEO in the form of First Merchants restricted stock that doesn't fully vest while any of the preferred stock issued to the Treasury Department under the CPP remains outstanding. On the other hand, based on the Committee's prior approach to allocating compensation between salary and other forms of incentive compensation, the 1/3 of total annual compensation limit isn't likely to limit the amount of the NEOs' potential payouts under the Program compensation. Since, as noted above, the Treasury Department has provided little guidance concerning the interpretation and application of the restrictions imposed by the ARRA, uncertainty remains as to exactly how the NEOs' compensation will be affected by this restriction. In addition, the Treasury Department may impose other restrictions on the compensation payable to executives of CPP participants. For these reasons, the discussion of the NEOs' non-equity incentive pay in this section of the proxy statement may be altered by subsequent developments.

Equity-Based Compensation.

The NEOs have the opportunity to receive equity-based compensation under the First Merchants Corporation 1999 Long-term Equity Incentive Plan. The awards available under the Plan include incentive and non-qualified options to acquire First Merchants stock and grants of restricted First Merchants stock. The Plan provides that the Compensation and Human Resources Committee has the authority to grant awards, decide who will receive awards, determine the types and sizes of awards, determine the terms, conditions, vesting periods, and restrictions applicable to awards, adopt, alter and repeal administrative rules and practices governing the Plan, interpret the terms and provisions of the Plan and any awards granted under the Plan, prescribe the forms of award agreements, and otherwise supervise the administration of the Plan. The Committee generally approves stock option and restricted stock awards under the Plan at a meeting held each year in February, at the same time salary adjustments and non-equity incentive payments are approved. The Committee also sometimes grants an award at other times, e.g., when an executive is hired. In making stock option and restricted stock awards, the Committee relies heavily on the recommendations of the CEO except for the awards to the CEO.

The annual awards to senior executives, including the NEOs, under the Plan are comprised of a combination of stock options and restricted stock, whereas the awards to other participants are generally in the form of restricted stock. The Committee believes that stock options should be a significant component of First Merchants' equity-based compensation program for the NEOs because the financial incentive provided by stock options depends entirely on increasing the price of First Merchants shares, thus furthering aligning the NEOs' financial interests with those of First Merchants' shareholders. The ratio of stock options to restricted stock annually awarded to the NEOs averages about 3-1. A share of restricted stock is valued at slightly more than 3 times the value of an option to purchase a share of stock.

The stock options granted to the NEOs under the Plan are incentive stock options up to the statutory limit; and the rest, if any, are non-qualified options. The exercise price for the stock options is the closing price of First Merchants stock as recorded by NASDAQ on the date of the grant. The options vest (become exercisable) 2 years later, or, if earlier, on the date the grantee retires, dies or becomes disabled. The restricted stock granted to the NEOs under the Plan vests (the restrictions lapse, giving the grantee complete ownership rights) if the grantee is still employed by First Merchants 3 years after the award is made, or, if earlier, on the date the grantee retires, dies or becomes disabled. The restricted stock partially vests if the grantee's employment is involuntarily terminated without "cause." Under this circumstance, the vested portion is a fraction, the numerator of which is the number of full years that have elapsed between the date of the award and the date of termination and the denominator of which is 3. The grantee is entitled to vote the shares of restricted stock and receive the dividends on the stock.

The Outstanding Equity Awards at Fiscal Year-End 2008 Table on page 24 provides information concerning each of the stock options granted to the NEOs through December 31, 2008 that have not expired, as well as information concerning the awards of restricted stock that had not vested as of December 31, 2008. As the Table shows, the Compensation and Human Resources Committee granted Mr. Rechin options to purchase 12,000 shares of First Merchants stock on February 8, 2007 and 15,000 shares on February 27, 2008, and it awarded him 3,000 shares of restricted First Merchants stock on February 8, 2007 and 4,000 shares on February 27, 2008. The Committee also granted Mr. Rechin options to purchase 20,000 shares of First Merchants stock on February 24, 2009, and it awarded him 4,000 shares of restricted First Merchants stock on the same date. The Committee granted Mr. Hardwick options to purchase 8,000 shares of First Merchants stock on February 8, 2007 and 8,000 shares on February 27, 2008, and it awarded him 2,400 shares of restricted First Merchants stock on February 8, 2007 and 2,700 shares on February 27, 2008. The Committee also granted Mr. Hardwick options to purchase 8,000 shares of First Merchants stock on February 24, 2009, and it awarded him 3,200 shares of restricted First Merchants stock on the same date. The Committee granted Mr. Stewart options to purchase 6,000 shares of First Merchants stock when he was hired on January 29, 2008, and it awarded him 3,000 shares of restricted First Merchants stock on the same date. The Committee also granted Mr. Stewart options to purchase 8,000 shares of First Merchants stock on February 24, 2009, and it awarded him 3,200 shares of restricted First Merchants stock on the same date. The Committee granted Mr. Connors options to purchase 4,500 shares of First Merchants stock on February 8, 2007 and 3,000 shares on February 27, 2008, and it awarded him 1,600 shares of restricted First Merchants stock on February 8, 2007 and 2,000 shares on February 27, 2008. The Committee also granted Mr. Connors options to purchase 3,000 shares of First Merchants stock on February 24, 2009, and it awarded him 2,000 shares of restricted First Merchants stock on the same date. The Committee granted Mr. Spade options to purchase 4,000 shares of First Merchants stock on February 8, 2007 and 4,000 shares on February 27, 2008, and it awarded him 1,000 shares of restricted First Merchants stock on February 8, 2007 and 1,000 shares on February 27, 2008. The Committee also granted Mr. Spade options to purchase 3,000 shares of First Merchants stock on February 24, 2009, and it awarded him 1,000 shares of restricted First Merchants stock on the same date. The exercise price for the stock options granted to the NEOs on February 8, 2007 was $26.31/share; the exercise price for the stock options granted to the NEOs (other than Mr. Stewart) on February 27, 2008 was $28.25/share; the exercise price for the stock options granted to Mr. Stewart on January 29, 2008 was $25.44/share: and the exercise price for the stock options granted to the NEOs on February 24, 2009 was $11.14/share. As of February 27, 2009, the date of this proxy statement, all of the unexercised stock options granted to the NEOs under the 1999 Long-term Equity Incentive Plan are out-of-the-money.

The 1999 Long-term Equity Incentive Plan expires in 2009, and no additional awards of restricted stock or stock options may be made under the Plan after April 14, 2009. On February 4, 2009, the Board adopted the First Merchants Corporation 2009 Long-Term Equity Incentive Plan, subject to shareholder approval which is being sought at the 2009 annual shareholder meeting. The 2009 Equity Incentive Plan is similar to the 1999 Plan; however, it includes two additional provisions applicable to NEOs participating in the Plan that, together with the vesting provisions in the 1999 Plan which continue in the 2009 Plan, are intended to encourage additional share ownership by the NEOs and thereby increase the commonality of interest between the NEOs and the shareholders. First, the 2009 Plan provides that NEOs are required to hold 25% of all "net shares" (defined as the number of shares issued to the NOE under an award after subtracting the number of shares, if any, transferred or surrendered by the NEO to pay the exercise price of a stock option and/or to pay any withholding taxes associated with the award) issued to the NEO under the Plan, including both restricted stock awards and shares issued upon the exercise of stock options, until the earlier of (i) the date of the NEO's death, retirement or other termination of employment, or (ii) the date of a change of control. Second, the 2009 Plan includes a guideline stating that NEOs who are selected as participants in the Plan should acquire and hold shares of First Merchants common stock equal in value to at least 100% of their then current annual salary within 6 years after first being selected to participate in the Plan. This guideline does not constitute a condition, restriction or risk of forfeiture applicable to any award made to an NEO under the Plan. Additional information concerning the 2009 Long-Term Equity Incentive Plan is provided on pages 35-39 under "Voting Item 4 – Proposal to Approve the First Merchants Corporation 2009 Long-Term Equity Incentive Plan." The full text of the Plan is set forth in Appendix B.

The ARRA prohibition on paying or accruing any bonus, retention award or incentive compensation to the NEOs while preferred stock issued to the Treasury Department under the CPP remains outstanding, discussed above in the section of this analysis covering the Senior Management Incentive Compensation Program, may also affect the benefits available to the NEOs under the Long-Term Equity Incentive Plan. As in the case of the Senior Management Incentive Compensation Program, uncertainty exists concerning the application of that prohibition, or the exception for long-term restricted stock, to the Long-Term Equity Incentive Plan. The exception's limitation of restricted stock to 1/3 of an NEO's total annual compensation limit is not likely to affect the size of the restricted stock awards that the Committee has typically made under the Plan. However, since the Treasury Department has provided little guidance concerning the interpretation and application of the restrictions imposed by the ARRA, uncertainty remains as to exactly how the NEOs' compensation under the Long-Term Equity Incentive Plan will be affected by this restriction. In addition, the Treasury Department may impose other restrictions on the compensation payable to executives of CPP participants. For these reasons, the discussion of the NEOs' equity-based compensation in this section of the proxy statement may be altered by subsequent developments.

Although not a material element of their equity-based compensation, several of the NEOs have participated in the First Merchants Corporation 2004 Employee Stock Purchase Plan, an Internal Revenue Code Section 423 employee stock purchase plan that is available to all employees of First Merchants and its participating subsidiaries. Under this Plan, participants could elect, prior to an annual offering period (July 1 to June 30), to purchase shares of First Merchants' stock at a price equal to 85% of the lesser of the closing price for the stock at the beginning of the offering period and the closing price for the stock at the end of the offering period, as reported by NASDAQ. The Plan has provided an attractive vehicle for participants to acquire First Merchants stock, which further aligns their financial interests with those of other shareholders. For the offering period ending June 30, 2008, the following NEOs participated in this Plan: Mr. Rechin, who purchased 681 shares, Mr. Hardwick, who purchased 596 shares, and Mr. Spade who purchased 298 shares. The purchase price for shares under the Plan was $15.43 per share. The 2004 Employee Stock Purchase Plan expires on June 30, 2009. On February 4, 2009, the Board adopted the First Merchants Corporation 2009 Employee Stock Purchase Plan, subject to shareholder approval which is being sought at the 2009 annual shareholder meeting. If approved, the 2009 Employee Stock Purchase Plan will become effective on July 1, 2009. It is similar to the 2004 Plan, except that the offering periods under the Plan will be 3 months rather than 12 months, corresponding with the calendar quarters, and the purchase price for shares will be equal to 85% of the average of the closing prices for the stock on each trading day during the offering period, as reported by NASDAQ, rather than 85% of the lesser of the closing price for the stock at the beginning of the offering period and the closing price for the stock at the end of the offering period, as reported by NASDAQ. Additional information concerning the 2009 Employee Stock Purchase Plan is provided on pages 31-34 under "Voting Item 3 – Proposal to Approve the First Merchants Corporation 2009 Employee Stock Purchase Plan." The full text of the Plan is set forth in Appendix A.

<u>Retirement Benefits</u>.

First Merchants maintains a qualified defined benefit pension plan, the First Merchants Corporation Retirement Pension Plan, which it "froze" as of March 1, 2005, meaning that, with some exceptions, employees no longer accrued benefits under the Plan. However, participants who were at least age 55 with 10 or more years of credited service on the date the Plan was frozen were "grandfathered;" that is, they continued

to accrue benefits under the Plan after that date. Employees who were not participating in the Plan on March 1, 2005 were not eligible to participate. The Plan pays benefits at retirement to participating employees of First Merchants and its participating subsidiaries. The benefits payable under this Plan, computed as a straight-life annuity although other forms of actuarially-equivalent benefits are available under the Plan, are based on the following formula: 1.6% of average final compensation (in general, the participant's highest 60 consecutive months' W-2 compensation, less incentive pay) plus .5% of average final compensation in excess of Social Security covered compensation, both times years of service to a maximum of 25 years. Although benefits are integrated with Social Security, they are not subject to any deduction for Social Security or other offset amounts. The benefits payable under the Plan at age 65 to the participants whose benefits were frozen are determined under the formula described above, based on their average final compensation as of March 1, 2005, times a fraction, the numerator of which is the participant's years of credited service as of March 1, 2005, and the denominator of which is the participant's years of credited service projected to age 65.

Of the NEOs, Messrs. Rechin, Stewart and Spade did not participate in the First Merchants Corporation Retirement Pension Plan. The benefits accruing to Messrs. Hardwick and Connors were frozen as of March 1, 2005, because they had not attained age 55 with 10 or more years of credited service as of that date. Assuming their employment continues to age 65, Messrs. Hardwick's and Connors' annual benefits under the plan, payable as a straight-life annuity, would be approximately $8,594 and $7,895, respectively.

First Merchants also maintains the First Merchants Corporation Retirement and Income Savings Plan, an Internal Revenue Code Section 401(k) qualified defined contribution plan under which participating employees of First Merchants and its subsidiaries can make pre-tax contributions to the Plan, up to statutory limits and limits set forth in the Plan, that are currently matched by the participant's employer at the rate of 50% of the participant's pre-tax contributions to the Plan, to a maximum of 6% of compensation (defined as W-2 compensation plus certain voluntary pre-tax contributions, up to the Internal Revenue Code Section 401(a)(17) maximum, which was $230,000 in 2008 and is $245,000 in 2009). Thus, the maximum matching employer contribution under the Plan is generally 3% of pay (less if the participant's compensation exceeds $245,000). First Merchants made matching contributions for 2008 under the Plan for NEOs Rechin, Hardwick, Stewart, Connors and Spade in the amounts of $6,900, $6,900, $6,900, $6,900 and $6,429, respectively. First Merchants also makes contributions, currently from 2% to 7% of compensation (up to the Internal Revenue Code Section 401(a)(17) maximum), on behalf of participants based on their years of service, in five-year increments (*i.e.*, 2% for 0-4 years of service, 3% for 5-9 years of service, 4% for 10-14 years of service, 5% for 15-19 years of service, 6% for 20-24 years of service, and 7% for 25 or more years of service). For 2008, the NEOs received service-weighted contributions as follows: Mr. Rechin, 2% of compensation, or $4,600; Mr. Hardwick, 4% of compensation, or $9,200; Mr. Stewart, 2% of compensation, or $4,600; Mr. Connors, 3% of compensation, or $6,900; and Mr. Spade, 2% of compensation, or $4,286. Finally, First Merchants is making "transition contributions" under the Plan equal to 3% of compensation for the years 2005 through 2009, for employees who were participants in the First Merchants Corporation Retirement Pension Plan when it was frozen and who had attained age 45 with 10 or more years of credited service as of March 1, 2005 (other than the "grandfathered" participants). None of the NEOs is eligible for a transition contribution under the Plan. Employee pre-tax contributions under the Plan are always fully vested, while matching, service-weighted and transition contributions vest 20% after each year of service.

First Merchants also maintains the First Merchants Corporation Defined Contribution Supplemental Executive Retirement Plan, which provides additional retirement benefits to executives designated by the Compensation and Human Resources Committee whose benefits under the First Merchants Corporation Retirement and Income Savings Plan are restricted due to the limit under Internal Revenue Code Section 401(a)(17) on the amount of compensation that can be considered for purposes of calculating pension benefits under a qualified plan ($230,000 in 2008 and $245,000 in 2009). Mr. Rechin is presently the sole participant in the Defined Contribution Supplemental Executive Retirement Plan. First Merchants contributes 12% of Mr. Rechin's annual compensation, including his base salary and his non-equity incentive pay, to the Plan. The Committee established this percentage after consulting with Mercer Human Resource Consulting, which assisted the Committee in designing the Plan in 2006. If Mr. Rechin continues to be employed by First Merchants until his normal retirement age, this contribution would provide an income replacement ratio of approximately 35%, based on a 7% return on the Plan's investments. Mercer Human Resource Consulting advised the Committee

that this income replacement ratio would provide retirement benefits to Mr. Rechin that are comparable to those paid to executives holding similar positions at peer companies in the banking industry. Mr. Rechin's benefit under the Plan is subject to a 5 year "cliff" vesting provision. He is not permitted to make employee contributions under the Plan. First Merchants' contribution for 2008 to this plan on behalf of Mr. Rechin was $45,494.

Change of Control Agreements.

First Merchants does not have an employment agreement with any of the NEOs. They are all deemed to be "at will" employees. However, First Merchants does have "double trigger" change of control agreements with all five of the NEOs. First Merchants believes that change of control agreements are in the best interests of First Merchants and its shareholders, because they would encourage key executives to remain with First Merchants and continue to act in First Merchants' and shareholders' interests in the event of a proposed acquisition or other change of control situation in which they might otherwise be influenced to leave due to the uncertainties of their own circumstances. Under the "double trigger" change of control agreements, severance benefits are payable to the NEOs only if: (1) a change of control occurs; and (2) the NEO's employment is terminated or constructively terminated following the change of control. Under First Merchants' agreements with the NEOs, this termination must occur within 24 months following the change of control in order for the agreement to apply and benefits to be payable. No benefits are payable under the agreements in the event of the executive's voluntary retirement, death or disability, or if the executive's employment is terminated for cause. The definitions of "change of control" and "constructive termination" as used in these agreements are contained on page 27, under "Termination of Employment and Change of Control Arrangements." The agreements also contain a definition of "cause" for termination. Payments under the change of control agreements are determined as a multiple of the sum of the executive's annual base salary at the time of receiving notice of termination and the executive's largest annual non-equity incentive payment under the Senior Management Incentive Compensation Program during the two years preceding the date of termination. This multiple is 2.99 for Messrs. Rechin, Hardwick and Stewart, and 1.50 for Messrs. Connors and Spade. The change of control agreements were not entered into in response to any effort to acquire control of First Merchants, and the Board is not aware of any such effort. Because they cover relatively few executives and represent a relatively small percentage of First Merchants' market capitalization, the Board does not believe that the existence of these agreements would discourage any such effort.

The restrictions imposed by the ARRA includes a prohibition against making "golden parachute payments" or severance payments (essentially, any payment for departure from the company for any reason, except for payments for services performed or benefits accrued) to an NEO or any of the next 5 most highly-compensated employees during the period that preferred stock issued to the Treasury Department under the CPP remains outstanding. This prohibition may prevent First Merchants from making any payments to NEOs under the provisions of the change of control agreements with its NEOs as long as the preferred stock issued by First Merchants to the Treasury Department remains outstanding. However, since, as noted above, the Treasury Department has provided little guidance concerning the interpretation and application of the restrictions imposed by the ARRA, uncertainty remains as to exactly how the NEOs' compensation will be affected by this prohibition. In addition, the Treasury Department may impose other restrictions on the compensation payable to executives of CPP participants. For these reasons, the discussion of the NEOs' change of control agreements in this section of the proxy statement may be altered by subsequent developments.

Summary Compensation Table

The following table provides information concerning all of the plan and non-plan compensation paid to the NEOs for 2006, 2007 and 2008.

Summary Compensation Table

Name and Principal position	Year	Salary(1)	Bonus(2)	Stock awards(3)	Option awards(3)	Non-equity incentive plan compen-sation(4)	Change in pension value and non-qualified deferred compensation earnings(5)	All other compensation(6)	Total
Michael C. Rechin	2006	280,288	100,100	14,864	21,844	3,300	0	51,788	472,184
President and Chief Executive Officer	2007	309, 423	0	57,833	83,434	69,620	0	69,270	589,580
	2008	346,154	0	31,755	41,694	0	0	67,114	486,717
Mark K. Hardwick	2006	193,699	0	14,864	19,113	19,950	2,495	15,434	265,555
Executive Vice President	2007	206,077	0	35,527	44,558	41,800	1,555	20,182	349,699
and Chief Financial Officer	2008	243,692	0	21,435	22,237	0	0	22,794	310,158
Michael J. Stewart									
Executive Vice President	2008	221,808	50,000	23,467	16,433	0	0	9,660	321,368
and Chief Banking Officer(7)									
Robert R. Connors									
Senior Vice President and	2006	185,704	0	10,405	10,922				
Chief Information Officer	2007	190,662	0	24,243	25,256				
	2008	198,796	0	15,878	8,339	16,398			