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ABN AMRO HOLDING N V  
 Form 424B2  
 October 31, 2007

CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities Offered	Maximum Aggregate Offering Price	Amount of Registration Fee(1)
Countrywide Financial Corp. Knock-in REX	\$500,000	\$15.35

(1) Pursuant to Rule 457(p) under the Securities Act of 1933, filing fees of \$94,671.00 have already been paid with respect to unsold securities that were previously registered pursuant to a Registration Statement on Form F-3 (No. 333-89136) of ABN AMRO Bank N.V. (the "Prior Registration Statement"), which was initially filed on May 24, 2002 and for which a post-effective amendment was filed on September 17, 2003 and have been carried forward. The \$15.35 fee with respect to the \$500,000 Knock-in Reverse Exchangeable Securities linked to the common stock of Countrywide Financial due October 31, 2008 sold pursuant to this registration statement is offset against those filing fees, and \$38,518.64 remains available for future registration fees. No additional fee has been paid with respect to this offering.

PRICING SUPPLEMENT (TO PROSPECTUS DATED SEPTEMBER 29, 2006 AND PROSPECTUS SUPPLEMENT DATED SEPTEMBER 29, 2006) CUSIP: 00078UF54	PRICING SUPPLEMENT NO. 331 TO REGISTRATION STATEMENT NOS. 333-137691, 333-137691-02 DATED OCTOBER 26, 2007 RULE 424(b)(2)
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[ABN AMRO LOGO]  
 \$500,000  
 ABN AMRO BANK N.V.  
 ABN NOTES (SM)  
 SENIOR FIXED RATE NOTES  
 FULLY AND UNCONDITIONALLY GUARANTEED BY  
 ABN AMRO HOLDING N.V.  
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27.50% KNOCK-IN REVERSE EXCHANGEABLE(SM) SECURITIES DUE OCTOBER 31, 2008  
 LINKED TO COMMON STOCK OF COUNTRYWIDE FINANCIAL CORPORATION

The Securities do not guarantee any return of principal at maturity. Instead, the payout at maturity will be based on the performance of the shares of common stock of Countrywide Financial Corporation, which we refer to as the Underlying Shares, during the life of the Securities, and in certain circumstances described below, we will exchange each Security at maturity for a predetermined number of the Underlying Shares rather than the principal amount of the Securities. THE MARKET VALUE OF THOSE UNDERLYING SHARES WILL BE LESS THAN THE PRINCIPAL AMOUNT OF EACH SECURITY AND COULD BE ZERO.

SECURITIES	27.50% Knock-in Reverse Exchangeable(SM) Securities due October 31, 2008.
PRINCIPAL AMOUNT	\$500,000
UNDERLYING SHARES	Common Stock, \$0.05 par value per share, of Countrywide Financial Corporation
INTEREST RATE	27.50% per annum, payable monthly in arrears on the last day of each month commencing on November 30, 2007 and ending on the maturity date.

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ISSUE PRICE 100%

ORIGINAL ISSUE DATE October 31, 2007

PRICING DATE October 26, 2007

MATURITY DATE October 31, 2008

INITIAL PRICE \$17.30 (the initial price is subject to adjustment for certain corporate events affecting the Underlying Shares, which we describe in "Description of Securities -- Adjustment Events").

KNOCK-IN LEVEL \$11.25, which is 65% of the initial price.

STOCK REDEMPTION AMOUNT 57.803 Underlying Shares for each \$1,000 principal amount of the Securities, which is equal to \$1,000 divided by the initial price.

DETERMINATION DATE The third trading day prior to the maturity date, subject to adjustment in certain circumstances which we describe in "Description of the Securities -- Determination Date."

PAYMENT AT MATURITY The payment at maturity is based on the performance of the Underlying Shares:

- o If the closing price of the Underlying Shares on the primary U.S. exchange or market for the Underlying Shares has not fallen below the knock-in level on any trading day from but not including the pricing date to and including the determination date, we will pay you the principal amount of each Security in cash.
- o If the closing price of the Underlying Shares on the primary U.S. exchange or market for the Underlying Shares falls below the knock-in level on any trading day from but not including the pricing date to and including the determination date:
  - we will deliver to you a number of Underlying Shares equal to the stock redemption amount, in the event that the closing price of the Underlying Shares on the determination date is below the initial price; or
  - we will pay you the principal amount of each Security in cash, in the event that the closing price of the Underlying Shares on the determination date is at or above the initial price.
- o You will receive cash in lieu of fractional shares.

The payment at maturity is subject to adjustment in certain circumstances.

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GUARANTEE The Securities will be fully and unconditionally guaranteed by ABN AMRO Holding N.V.

DENOMINATIONS The Securities may be purchased in denominations of \$1,000 and integral multiples thereof.

NO AFFILIATION WITH COUNTRYWIDE FINANCIAL CORPORATION Countrywide Financial Corporation, which we refer to as "Countrywide," is not an affiliate of ours and is not involved with this offering in any way. The obligations represented by the Securities are our obligations, not those of Countrywide. Investing in the Securities is not equivalent to investing in Countrywide common stock.

LISTING We do not intend to list the Securities on any securities exchange.

THE SECURITIES ARE NOT INSURED BY THE FEDERAL DEPOSIT INSURANCE CORPORATION OR ANY OTHER FEDERAL AGENCY.

THE SECURITIES INVOLVE RISKS NOT ASSOCIATED WITH AN INVESTMENT IN CONVENTIONAL DEBT SECURITIES. SEE "RISK FACTORS" BEGINNING ON PS-8.

The Securities and Exchange Commission and state securities regulators have not approved or disapproved these Securities, or determined if this Pricing Supplement or the accompanying Prospectus Supplement or Prospectus is truthful or complete. Any representation to the contrary is a criminal offense. The agents are not obligated to purchase the Securities but have agreed to use reasonable efforts to solicit offers to purchase the Securities. TO THE EXTENT THE FULL AGGREGATE PRINCIPAL AMOUNT OF THE SECURITIES BEING OFFERED BY THIS PRICING SUPPLEMENT IS NOT PURCHASED BY INVESTORS IN THE OFFERING, ONE OR MORE OF OUR AFFILIATES HAS AGREED TO PURCHASE THE UNSOLD PORTION, WHICH MAY CONSTITUTE A SUBSTANTIAL PORTION OF THE TOTAL AGGREGATE PRINCIPAL AMOUNT OF THE SECURITIES, AND TO HOLD SUCH SECURITIES FOR INVESTMENT PURPOSES. SEE "HOLDING OF THE SECURITIES BY OUR AFFILIATES AND FUTURE SALES" UNDER THE HEADING "RISK FACTORS" AND "PLAN OF DISTRIBUTION." This Pricing Supplement and the accompanying Prospectus Supplement and Prospectus may be used by our affiliates in connection with offers and sales of the Securities in market-making transactions.

	PRICE \$1,000 PER SECURITY		
	PRICE TO PUBLIC	AGENT'S COMMISSIONS(1)	PROCEEDS TO ABN AMRO BANK N.V.
Countrywide Financial Corporation	100%	3.25%	96.75%
Total	\$500,000	\$16,250	\$483,750

(1) For additional information see "Plan of Distribution" in this pricing supplement.

ABN AMRO INCORPORATED

In this Pricing Supplement, the "Bank," "we," "us" and "our" refer to ABN AMRO Bank N.V. and "Holding" refers to ABN AMRO Holding N.V., our parent company. We refer to the Securities offered hereby and the related guarantees as the "Securities" and to each individual security offered hereby as a "Security."

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Reverse Exchangeable (SM) and ABN Notes (SM) are service marks of ABN AMRO Bank N.V.

ANY SECURITIES ISSUED, SOLD OR DISTRIBUTED PURSUANT TO THIS PRICING SUPPLEMENT MAY NOT BE OFFERED OR SOLD (i) TO ANY PERSON/ENTITY LISTED ON SANCTIONS LISTS OF THE EUROPEAN UNION, UNITED STATES OR ANY OTHER APPLICABLE LOCAL COMPETENT AUTHORITY; (ii) WITHIN THE TERRITORY OF CUBA, SUDAN, IRAN AND MYANMAR; (iii) TO RESIDENTS IN CUBA, SUDAN, IRAN OR MYANMAR; OR (iv) TO CUBAN NATIONALS, WHEREVER LOCATED.

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### SUMMARY

THE FOLLOWING SUMMARY ANSWERS SOME QUESTIONS THAT YOU MIGHT HAVE REGARDING THE SECURITIES IN GENERAL TERMS ONLY. IT DOES NOT CONTAIN ALL THE INFORMATION THAT MAY BE IMPORTANT TO YOU. YOU SHOULD READ THE SUMMARY TOGETHER WITH THE MORE DETAILED INFORMATION THAT IS CONTAINED IN THE REST OF THIS PRICING SUPPLEMENT AND IN THE ACCOMPANYING PROSPECTUS AND PROSPECTUS SUPPLEMENT. YOU SHOULD CAREFULLY CONSIDER, AMONG OTHER THINGS, THE MATTERS SET FORTH IN "RISK FACTORS." IN ADDITION, WE URGE YOU TO CONSULT WITH YOUR INVESTMENT, LEGAL, ACCOUNTING, TAX AND OTHER ADVISORS WITH RESPECT TO ANY INVESTMENT IN THE SECURITIES.

#### WHAT ARE THE SECURITIES?

The Securities are interest paying, non-principal protected securities issued by us, ABN AMRO Bank N.V., and are fully and unconditionally guaranteed by our parent company, ABN AMRO Holding N.V. The Securities are senior notes of ABN AMRO Bank N.V. and have a maturity of one year. These Securities combine certain features of debt and equity by offering a fixed interest rate on the principal amount while the payment at maturity is determined based on the performance of the Underlying Shares. Therefore your principal is at risk.

The Securities have certain features that make them what we refer to as "Knock-in Reverse Exchangeable Securities." This means that if the closing price of the Underlying Shares on the primary U.S. securities exchange or organized market for the Underlying Shares, which we refer to as the relevant exchange, never falls below a certain price level, which we call the knock-in level, on any trading day from but not including the pricing date to and including the determination date (such period, the "Knock-in Period"), then we will pay you in cash the principal amount of each Security at maturity. On the other hand, if the closing price of the Underlying Shares on the relevant exchange falls below the knock-in level on any trading day during the Knock-in Period, then the payment at maturity will depend on the closing price of the Underlying Shares on the determination date. In this latter case, if the closing price of the Underlying Shares on the determination date is equal to or greater than the initial price, we will pay you in cash the principal amount of each Security you hold; if the closing price of the Underlying Shares on the determination date is less than the initial price, we will deliver to you, in exchange for each \$1,000 principal amount of Securities, a number of Underlying Shares equal to the stock redemption amount.

#### WHY IS THE INTEREST RATE ON THE SECURITIES HIGHER THAN THE INTEREST RATE PAYABLE ON YOUR CONVENTIONAL DEBT SECURITIES WITH THE SAME MATURITY?

The Securities offer a higher interest rate than the yield that would be payable on a conventional debt security with the same maturity issued by us or

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an issuer with a comparable credit rating. This is because you, the investor in the Securities, indirectly sell a put option to us on the Underlying Shares. The premium due to you for this put option is combined with a market interest rate on our senior debt to produce the higher interest rate on the Securities.

WHAT ARE THE CONSEQUENCES OF THE INDIRECT PUT OPTION THAT I HAVE SOLD YOU?

The put option you indirectly sell to us creates the feature of exchangeability. If the closing price of the Underlying Shares on the relevant exchange falls below the knock-in level on any trading day during the Knock-in Period, and on the determination date the closing price per Underlying Share is less than the initial price, you will receive a fixed number of Underlying Shares for each Security you hold, which we call the stock redemption amount. On the other hand, if the closing price of the Underlying Shares on the relevant exchange falls below the knock-in level, and on the determination date the closing price per Underlying Share is equal to or greater than the initial price, you will receive \$1,000 for each Security you hold. Because of the exchangeability of the Securities, and because we will determine whether you will receive cash or Underlying Shares by reference to the closing price of the Underlying Shares on the determination date, such securities are generally referred to as "reverse exchangeable securities." However, because this feature of exchangeability is created only if the closing price of the Underlying Shares on the relevant exchange falls below the knock-in level on any trading day during the Knock-in Period, we call the Securities "Knock-in Reverse Exchangeable Securities."

WHAT WILL I RECEIVE AT MATURITY OF THE SECURITIES?

The payment at maturity of the Securities will depend on (i) whether or not the closing price of the Underlying Shares fell below the knock-in level on any trading day during the Knock-in Period, and if so, (ii) the closing price of the Underlying Shares on

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the determination date. To determine closing prices, we look at the prices quoted by the relevant exchange.

- o If the closing price per Underlying Share on the relevant exchange has not fallen below the knock-in level on any trading day during the Knock-in Period, we will pay you the principal amount of each Security in cash.
- o If the closing price per Underlying Share on the relevant exchange has fallen below the knock-in level on any trading day during the Knock-in Period, we will either:
  - o deliver to you the stock redemption amount, in exchange for each Security, in the event that the closing price of the Underlying Shares is below the initial price on the determination date; or
  - o pay you the principal amount of each Security in cash, in the event that the closing price of the Underlying Shares is at or above the initial price on the determination date.

The payment at maturity is subject to adjustment in certain circumstances, which we describe in "Description of Securities -- Adjustment Events.

HOW ARE THE STOCK REDEMPTION AMOUNT AND KNOCK-IN LEVEL DETERMINED?

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The stock redemption amount for each \$1,000 principal amount of the Securities is equal to \$1,000 divided by the initial price. The value of any fractional shares you are entitled to receive, after aggregating your total holdings of the Securities, will be paid in cash based on the closing price of the Underlying Shares on the determination date.

The knock-in level is 65% of the initial price.

The initial price and consequently the stock redemption amount and knock-in level are subject to adjustment for certain corporate events affecting the Underlying Shares, which we describe in "Description of Securities -- Adjustment Events."

### WHAT INTEREST PAYMENTS CAN I EXPECT ON THE SECURITIES?

The Securities pay interest at a rate of 27.50% per annum. The interest rate is fixed at issue and is payable monthly in arrears. This means that irrespective of whether the Securities are exchanged at maturity for cash or the stock redemption amount, you will be entitled to monthly interest payments on the full principal amount of the Securities you hold, payable in cash.

### CAN YOU GIVE ME AN EXAMPLE OF THE PAYMENT AT MATURITY?

If, for example, in a hypothetical offering, the interest rate was 10% per annum, the initial price of a share of underlying stock was \$45.00 and the knock-in level for such offering was 80%, then the stock redemption amount would be 22.222 shares of underlying stock, or \$1,000 divided by \$45.00, and the knock-in level would be \$36.00, or 80% of the initial price.

If the closing price of that hypothetical underlying stock fell below the knock-in level of \$36.00 on any trading day during the Knock-in Period, then the payment at maturity would depend on the closing price of the underlying stock on the determination date. In this case, if the closing price of the underlying stock on the determination date is \$30.00 per share at maturity, which is below the initial price level, you would receive 22.222 shares of underlying stock for each \$1,000 principal amount of the securities. (In actuality, because we cannot deliver fractions of a share, you would receive on the maturity date for each \$1,000 principal amount of the securities 22 shares of underlying stock plus \$6.66 cash in lieu of 0.222 fractional shares, determined by multiplying 0.222 by \$30.00, the closing price per shares of underlying stock on the determination date.) In addition, over the life of the securities you would have received interest payments at a rate of 10% per annum. IN THIS HYPOTHETICAL EXAMPLE, THE MARKET VALUE OF THOSE 22 SHARES OF UNDERLYING STOCK (INCLUDING THE CASH PAID IN LIEU OF FRACTIONAL SHARES) THAT WE WOULD DELIVER TO YOU AT MATURITY FOR EACH \$1,000 PRINCIPAL AMOUNT OF SECURITY WOULD BE \$666.66, WHICH IS LESS THAN THE PRINCIPAL AMOUNT OF \$1,000, AND YOU WOULD HAVE LOST A PORTION OF YOUR INITIAL INVESTMENT. If, on the other hand, the closing price of the underlying stock on the determination date is \$50.00 per share, which is above the initial price level, you will receive \$1,000 in cash for each \$1,000 principal amount of the securities regardless of the knock-in level having been breached. In addition, over the life of the Securities you would have received interest payments at a rate of 10% per annum.

Alternatively, if the closing price of the underlying stock never falls below \$36.00, which is

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the knock-in level, on any trading day during the Knock-in Period, at maturity you will receive \$1,000 in cash for each security you hold regardless of the closing price of the underlying stock on the determination date. In addition, over the life of the securities you would have received interest payments at a rate of 10% per annum.

THIS EXAMPLE IS FOR ILLUSTRATIVE PURPOSES ONLY AND IS BASED ON A HYPOTHETICAL OFFERING. FOR EACH OFFERING OF SECURITIES, WE WILL SET THE INITIAL PRICE, KNOCK-IN LEVEL AND STOCK REDEMPTION AMOUNT (SUBJECT TO ADJUSTMENT FOR CERTAIN CORPORATE EVENTS AFFECTING THE APPLICABLE UNDERLYING SHARES) ON THE DATE WE PRICE THE SECURITIES, WHICH WE REFER TO AS THE PRICING DATE. IT IS NOT POSSIBLE, HOWEVER, TO PREDICT THE CLOSING PRICE OF ANY OF THE UNDERLYING SHARES ON THE DETERMINATION DATE OR AT ANY TIME DURING THE LIFE OF THE SECURITIES.

In this Pricing Supplement, we have provided under the heading "Hypothetical Sensitivity Analysis of Total Return of the Securities at Maturity" the total return of owning the Securities through maturity for various hypothetical closing prices of the Underlying Shares on the determination date in the case where the knock-in level has been breached and in the case where the knock-in level has not been breached.

DO I GET ALL MY PRINCIPAL BACK AT MATURITY?

You are not guaranteed to receive any return of principal at maturity. If the closing price of Underlying Shares falls below the knock-in level on any trading day during the Knock-in Period, and the closing price of the Underlying Shares is below the initial price on the determination date, we will deliver to you Underlying Shares. The market value of the Underlying Shares at the time you receive those shares will be less than the principal amount of the Securities and could be zero.

IS THERE A LIMIT TO HOW MUCH I CAN EARN OVER THE LIFE OF THE SECURITIES?

Yes. The amount payable under the terms of the Securities will never exceed the principal amount of the Securities payable at maturity plus interest payments you earn over the life of the Securities.

DO I BENEFIT FROM ANY APPRECIATION IN THE UNDERLYING SHARES OVER THE LIFE OF THE SECURITIES?

No. The amount paid at maturity for each \$1,000 principal amount of the Securities will not exceed \$1,000. As a result, if the Underlying Shares have appreciated above their price level on the pricing date, the payment you receive at maturity will not reflect that appreciation. UNDER NO CIRCUMSTANCES WILL YOU RECEIVE A PAYMENT AT MATURITY GREATER THAN THE PRINCIPAL AMOUNT OF THE SECURITIES THAT YOU HOLD AT THAT TIME.

WHAT IS THE MINIMUM REQUIRED PURCHASE?

You can purchase Securities in \$1,000 denominations or in integral multiples thereof.

IS THERE A SECONDARY MARKET FOR THE SECURITIES?

We do not intend to list the Securities on any securities exchange. Accordingly, there may be little or no secondary market for the Securities and, as such, information regarding independent market pricing for the Securities may be limited. You should be willing to hold your Securities until the maturity date.

Although it is not required to do so, we have been informed by our

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affiliate that when this offering is complete, it intends to make purchases and sales of the Securities from time to time in off-exchange transactions. If our affiliate does make such a market in the Securities, it may stop doing so at any time.

In connection with any secondary market activity in the Securities, our affiliate may post indicative prices for the Securities on a designated website or via Bloomberg. However, our affiliate is not required to post such indicative prices and may stop doing so at any time. INVESTORS ARE ADVISED THAT ANY PRICES SHOWN ON ANY WEBSITE OR BLOOMBERG PAGE ARE INDICATIVE PRICES ONLY AND, AS SUCH, THERE CAN BE NO ASSURANCE THAT ANY TRADE COULD BE EXECUTED AT SUCH PRICES. Investors should contact their brokerage firm for further information.

In addition, the issue price of the Securities includes the selling agents' commissions paid with respect to the Securities and the cost of hedging our obligations under the Securities. The cost of hedging includes the profit component that our affiliate has charged in consideration for assuming the risks inherent in managing the hedging the transactions. The fact that the issue price of the Securities includes these commissions and hedging costs is expected to adversely affect the secondary market prices of the Securities. See "Risk Factors--The Inclusion of Commissions and Cost of Hedging in the Issue Price is Likely to Adversely Affect Secondary Market Prices" and "Use of Proceeds."

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TELL ME MORE ABOUT ABN AMRO BANK N.V. AND ABN AMRO HOLDING N.V.

ABN AMRO Bank N.V. is an international banking group offering a wide range of banking products and financial services on a global basis through our network of offices and branches in 56 countries and territories as of year-end 2006. ABN AMRO Holding N.V. is the parent company of ABN AMRO Bank N.V. Holding's main purpose is to own the Bank and its subsidiaries. All of the Securities issued by the Bank hereunder are fully and unconditionally guaranteed by Holding.

On October 10, 2007 a consortium (the "Consortium") of the Royal Bank of Scotland Group plc, Fortis SA/NV and Fortis N.V., and Banco Santander Central Hispano SA announced that their tender offer for the shares of Holding had become unconditional and approximately 86% of the shares of Holding had been tendered to the Consortium. Shareholders who had tendered their shares received payment for their shares on October 17, 2007.

Holding is currently listed on Euronext and the New York Stock Exchange. ABN AMRO Bank N.V. is rated AA- by Standard & Poor's and Aa2 by Moody's.

WHERE CAN I FIND OUT MORE ABOUT COUNTRYWIDE?

Because the Underlying Shares are registered under the Securities Exchange Act of 1934, as amended, Countrywide is required to file periodically certain financial and other information specified by the Commission which is available to the public. You should read "Public Information Regarding the Underlying Shares" in this Pricing Supplement to learn how to obtain public information regarding the Underlying Shares and other important information. The historical highest intra-day price, lowest intra-day price and last day closing price of the Underlying Shares for each quarter since 2003 are set forth under the heading "Public Information Regarding the Underlying Shares" in this Pricing Supplement.

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WHO WILL DETERMINE WHETHER THE CLOSING PRICE OF THE UNDERLYING SHARES HAS FALLEN BELOW THE KNOCK-IN LEVEL, THE CLOSING PRICE OF THE UNDERLYING SHARES ON THE DETERMINATION DATE, THE STOCK REDEMPTION AMOUNT AND THE INITIAL PRICE?

We have appointed ABN AMRO Incorporated, which we refer to as AAI, to act as calculation agent for Wilmington Trust Company, the trustee for the Securities and Citibank, N.A., the securities administrator. As calculation agent, AAI will determine whether the closing price of the Underlying Shares has fallen below the knock-in level, the closing price of the Underlying Shares on the determination date, the stock redemption amount and the initial price. The calculation agent may adjust the initial price of the Underlying Shares and consequently the stock redemption amount and knock-in level, which we describe in the section called "Description of Securities -- Adjustment Events."

WHO INVESTS IN THE SECURITIES?

The Securities are not suitable for all investors. The Securities might be considered by investors who:

- o seek a higher interest rate than the current dividend yield on the Underlying Shares or the yield on a conventional debt security with the same maturity issued by us or an issuer with a comparable credit rating;
- o are willing to accept the risk of owning equity in general and the Underlying Shares in particular and the risk that they could lose their entire investment;
- o do not expect to participate in any appreciation in the price of the Underlying Shares; and
- o and are willing to hold the Securities until maturity.

You should carefully consider whether the Securities are suited to your particular circumstances before you decide to purchase them. In addition, we urge you to consult with your investment, legal, accounting, tax and other advisors with respect to any investment in the Securities.

WHAT ARE SOME OF THE RISKS IN OWNING THE SECURITIES?

Investing in the Securities involves a number of risks. We have described the most significant risks relating to the Securities under the heading "Risk Factors" in this Pricing Supplement which you should read before making an investment in the Securities.

Some selected risk considerations include:

- o CREDIT RISK. Because you are purchasing a security from us, you are assuming our credit risk. In addition, because the Securities are fully and unconditionally guaranteed by Holding, you are

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assuming the credit risk of Holding in the event that we fail to make any payment or delivery required by the terms of the Securities.

- o PRINCIPAL RISK. The Securities are not principal protected, which means there is no guaranteed return of principal. If the closing price of the Underlying Shares falls below the knock-in level on any trading day during

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the life of the Securities and the closing price on the determination date is less than the initial price, we will deliver to you a fixed number of Underlying Shares with a market value less than the principal amount of the Securities, which value may be zero.

- o LIQUIDITY AND MARKET RISK. We do not intend to list the Securities on any securities exchange. Accordingly, there may be little or no secondary market for the Securities and information regarding independent market pricing for the Securities may be limited. The value of the Securities in the secondary market, if any, will be subject to many unpredictable factors, including then prevailing market conditions.

### WHAT IF I HAVE MORE QUESTIONS?

You should read "Description of Securities" in this Pricing Supplement for a detailed description of the terms of the Securities. The Securities are senior notes issued as part of our ABN Notes(SM) program and guaranteed by Holding. The Securities offered by the Bank will constitute the Bank's unsecured and unsubordinated obligations and rank pari passu without any preference among them and with all our other present and future unsecured and unsubordinated obligations. The guarantee of Holding will constitute Holding's unsecured and unsubordinated obligations and rank pari passu without any preference among them and with all Holding's other present and future unsecured and unsubordinated obligations. You can find a general description of our ABN Notes(SM) program in the accompanying Prospectus Supplement. We also describe the basic features of this type of note in the sections called "Description of Notes" and "Notes Linked to Commodity Prices, Single Securities, Baskets of Securities or Indices".

You may contact our principal executive offices at Gustav Mahleraan 10, 1082 PP Amsterdam, The Netherlands. Our telephone number is (54-20) 628-9393.

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### RISK FACTORS

This section describes the most significant risks relating to the Securities. For a discussion of certain general risks associated with your investment in the Securities, please refer to the section entitled "Risk Factors" beginning on page S-3 of the accompanying prospectus supplement. YOU SHOULD CAREFULLY CONSIDER WHETHER THE SECURITIES ARE SUITED TO YOUR PARTICULAR CIRCUMSTANCES BEFORE YOU DECIDE TO PURCHASE THEM. IN ADDITION, WE URGE YOU TO CONSULT WITH YOUR INVESTMENT, LEGAL, ACCOUNTING, TAX AND OTHER ADVISORS WITH RESPECT TO ANY INVESTMENT IN THE SECURITIES.

THE SECURITIES ARE NOT ORDINARY SENIOR NOTES; THERE IS NO GUARANTEED RETURN OF PRINCIPAL

The Securities combine limited features of debt and equity. The terms of the Securities differ from those of ordinary debt securities in that we will not pay you a fixed principal amount in cash at maturity if the closing price of the Underlying Shares has fallen below the knock-in level on any trading day during the Knock-in Period and, in addition, the closing price of the Underlying Shares is below the initial price on the determination date. In such event, we will exchange each Security you hold for a number of Underlying Shares equal to the stock redemption amount. Such shares will have a market value of less than the principal amount of the Securities, and such value may be zero. You cannot predict the future performance of the Underlying Shares based on their historical performance. ACCORDINGLY, YOU COULD LOSE SOME OR ALL

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OF THE AMOUNT YOU INVEST IN THE SECURITIES.

THE SECURITIES WILL NOT PAY MORE THAN THE STATED PRINCIPAL AMOUNT AT MATURITY

The amount paid at maturity of the Securities in cash or Underlying Shares will not exceed the principal amount of the Securities. If the closing price of the Underlying Shares on the determination date is equal to or exceeds the initial price (regardless of whether the knock-in level has been previously breached), you will receive the principal amount of the Securities irrespective of any appreciation in the share price. You will not receive Underlying Shares or any other asset equal to the value of the Underlying Shares. As a result, if the Underlying Shares have appreciated above their closing price level on the pricing date, the payment you receive at maturity will not reflect that appreciation. UNDER NO CIRCUMSTANCES WILL YOU RECEIVE A PAYMENT AT MATURITY GREATER THAN THE PRINCIPAL AMOUNT OF THE SECURITIES THAT YOU HOLD AT THAT TIME.

WE DO NOT INTEND TO LIST THE SECURITIES ON ANY SECURITIES EXCHANGE; SECONDARY TRADING MAY BE LIMITED

You should be willing to hold your Securities until the maturity date. We do not intend to list the Securities on any securities exchange; accordingly, there may be little or no secondary market for the Securities and information regarding independent market pricing for the Securities may be limited. Even if there is a secondary market, it may not provide enough liquidity to allow you to trade or sell the Securities easily. Upon completion of the offering, our affiliate has informed us that it intends to purchase and sell the Securities from time to time in off-exchange transactions, but it is not required to do so. If our affiliate does make such a market in the Securities, it may stop doing so at any time. In addition, the total principal amount of the Securities being offered is not being purchased by investors in the offering, and one or more of our affiliates has agreed to purchase the unsold portion. Such affiliate or affiliates intend to hold the Securities for investment purposes, which may affect the supply of Securities available for secondary trading and therefore adversely affect the price of the Securities in any secondary trading. If a substantial portion of any Securities held by our affiliates were to be offered for sale following this offering, the market price of such Securities could fall, especially if secondary trading in such Securities is limited or illiquid.

MARKET PRICE OF THE SECURITIES INFLUENCED BY MANY UNPREDICTABLE FACTORS

The value of the Securities may move up and down between the date you purchase them and the determination date when the calculation agent determines the amount to be paid to the holders of the Securities on the maturity date.

Several factors, many of which are beyond our control, will influence the value of the Securities, including:

- o the market price of the Underlying Shares, in particular, whether the market price of the Underlying Shares has fallen below the knock-in level;

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- o the volatility (frequency and magnitude of changes) in the price of the Underlying Shares;
- o the dividend rate on the Underlying Shares. While dividend payments on the Underlying Shares, if any, are not paid to holders of the

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Securities, such payments may have an influence on the market price of the Underlying Shares and therefore on the Securities;

- o interest and yield rates in the market;
- o economic, financial, political and regulatory or judicial events that affect the stock markets generally and which may affect the closing price of the Underlying Shares and/or the Securities;
- o the time remaining to the maturity of the Securities; and
- o the creditworthiness of the Bank as issuer of the Securities and Holding as the guarantor of the Bank's obligations under the Securities. Any person who purchases the Securities is relying upon the creditworthiness of the Bank and Holding and has no rights against any other person. The Securities constitute the general, unsecured and unsubordinated contractual obligations of the Bank and Holding.

Some or all of these factors will influence the price that you will receive if you sell your Securities in the secondary market, if any, prior to maturity. For example, you may have to sell your Securities at a substantial discount from the principal amount if at the time of sale the market price of the Underlying Shares is at, below, or not sufficiently above the knock-in level. See "Risk Factors--The Inclusion of Commissions and Cost of Hedging in the Issue Price is Likely to Adversely Affect Secondary Market Prices."

THE INCLUSION OF COMMISSIONS AND COST OF HEDGING IN THE ISSUE PRICE IS LIKELY TO ADVERSELY AFFECT SECONDARY MARKET PRICES

Assuming no change in market conditions or any other relevant factors, the price, if any, at which the selling agents are willing to purchase Securities in secondary market transactions will likely be lower than the issue price, since the issue price included, and secondary market prices are likely to exclude, commissions paid with respect to the Securities, as well as the profit component included in the cost of hedging our obligations under the Securities. In addition, any such prices may differ from values determined by pricing models used by the selling agents, as a result of dealer discounts, mark-ups or other transaction costs.

AN INCREASE IN THE VALUE OF THE UNDERLYING SHARES WILL NOT INCREASE THE RETURN ON YOUR INVESTMENT

Owning the Securities is not the same as owning the Underlying Shares. Accordingly, the market value of your Securities may not have a direct relationship with the market price of the Underlying Shares, and changes in the market price of the Underlying Shares may not result in a comparable change in the market value of your Securities. If the price per Underlying Share increases above the initial price, the market value of the Securities may not increase. It is also possible for the price of the Underlying Shares to increase while the market price of the Securities declines.

POTENTIAL CONFLICTS OF INTEREST; NO SECURITY INTEREST IN THE UNDERLYING SHARES HELD BY US

We and our affiliates may carry out hedging activities that minimize our risks related to the Securities, including trading in the Underlying Shares. In particular, on or prior to the date of this Pricing Supplement, we, through our affiliates, hedged our anticipated exposure in connection with the Securities by taking positions in the Underlying Shares, options contracts on Underlying Shares listed on major securities markets, and/or other instruments that we deemed appropriate in connection with such hedging. Such hedging is carried out

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in a manner designed to minimize any impact on the price of the Underlying Shares. Our purchase activity, however, could potentially have increased the initial price of the Underlying Shares, and therefore inadvertently increased the level below which we would be required to deliver to you at maturity Underlying Shares, which, in turn, would have a value less than the principal amount of your Securities.

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Through our affiliates, we are likely to modify our hedge position throughout the life of the Securities by purchasing and selling Underlying Shares, options contracts on Underlying Shares listed on major securities markets or positions in other securities or instruments that we may wish to use in connection with such hedging. Although we have no reason to believe that our hedging activity or other trading activities that we, or any of our affiliates, engage in or may engage in has had or will have a material impact on the price of the Underlying Shares, we cannot give you any assurance that we have not or will not affect such price as a result of our hedging or trading activities. It is possible that we or one of more of our affiliates could receive substantial returns from these hedging activities while the value of the Securities may decline. We or one or more of our affiliates may also engage in trading the Underlying Shares and other investments relating to Countrywide on a regular basis as part of our or its general broker-dealer and other businesses, for proprietary accounts, for other accounts under management or to facilitate transactions for customers, including block transactions. Any of these activities could adversely affect the price of the Underlying Shares and, therefore, the value of the Securities. We or one or more of our affiliates may also issue or underwrite other securities or financial or derivative instruments with returns linked or related to changes in the value of the Underlying Shares. By introducing competing products into the marketplace in this manner, we or one or more of our affiliates could adversely effect the value of the Securities. It is also possible that any advisory services that we or our affiliates provide in the course of any business with Countrywide or its affiliates could lead to actions on the part of the issuer of the stock which might adversely affect the value of the Underlying Shares.

The indenture governing the Securities does not contain any restrictions on our ability or the ability of any of our affiliates to sell, pledge or otherwise convey all or any portion of the Underlying Shares acquired by us or our affiliates. Neither we nor Holding nor any of our affiliates will pledge or otherwise hold Underlying Shares for the benefit of holders of the Securities in order to enable the holders to exchange their Securities for Underlying Shares under any circumstances. Consequently, in the event of a bankruptcy, insolvency or liquidation involving us or Holding, as the case may be, any Underlying Shares that we or Holding own will be subject to the claims of our creditors or Holding's creditors generally and will not be available specifically for the benefit of the holders of the Securities.

### NO SHAREHOLDER RIGHTS IN THE UNDERLYING SHARES

As a holder of the Securities, you will not have voting rights or rights to receive dividends or other distributions or other rights that holders of Underlying Shares would have.

Because neither we nor Holding nor any of our affiliates are affiliated with Countrywide, we have no ability to control or predict the actions of Countrywide, including any corporate actions of the type that would require the calculation agent to adjust the initial price and consequently the knock-in level and stock redemption amount, and have no ability to control the public

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disclosure of these corporate actions or any other events or circumstances affecting Countrywide. COUNTRYWIDE IS NOT INVOLVED IN THE OFFER OF THE SECURITIES IN ANY WAY AND HAS NO OBLIGATION TO CONSIDER YOUR INTEREST AS AN OWNER OF THE SECURITIES IN TAKING ANY CORPORATE ACTIONS THAT MIGHT AFFECT THE VALUE OF YOUR SECURITIES. NONE OF THE MONEY YOU PAY FOR THE SECURITIES WILL GO TO COUNTRYWIDE.

### INFORMATION REGARDING COUNTRYWIDE

Neither we nor Holding nor any of our affiliates assume any responsibility for the adequacy of the information about Countrywide contained in this Pricing Supplement or in any of Countrywide's publicly available filings. AS AN INVESTOR IN THE SECURITIES, YOU SHOULD MAKE YOUR OWN INVESTIGATION INTO COUNTRYWIDE. NEITHER WE NOR HOLDING NOR ANY OF OUR AFFILIATES HAVE ANY AFFILIATION WITH COUNTRYWIDE, AND ARE NOT RESPONSIBLE FOR COUNTRYWIDE'S PUBLIC DISCLOSURE OF INFORMATION, WHETHER CONTAINED IN SEC FILINGS OR OTHERWISE.

### LIMITED ANTIDILUTION PROTECTION

AAI, as calculation agent, will adjust the initial price and consequently the stock redemption amount and knock-in level for certain events affecting the Underlying Shares, such as stock splits and corporate actions. The calculation agent is not required to make an adjustment for every corporate action which affects the Underlying Shares. For example, the calculation agent is not required to make any adjustments if Countrywide or anyone else makes a partial tender or partial exchange offer for the Underlying Shares. IF AN EVENT OCCURS THAT DOES NOT REQUIRE THE

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CALCULATION AGENT TO ADJUST THE AMOUNT OF THE UNDERLYING SHARES PAYABLE AT MATURITY, THE MARKET PRICE OF THE SECURITIES MAY BE MATERIALLY AND ADVERSELY AFFECTED.

### HOLDINGS OF THE SECURITIES BY OUR AFFILIATES AND FUTURE SALES

Certain of our affiliates have agreed to purchase for investment the portion of the Securities that has not been purchased by investors in this offering, which initially they intend to hold for investment purposes. As a result, upon completion of this offering, our affiliates may own a substantial portion of the aggregate principal amount of the Securities. Circumstances may occur in which our interests or those of our affiliates could be in conflict with your interests.

### POTENTIAL CONFLICTS OF INTEREST BETWEEN HOLDERS OF SECURITIES AND THE CALCULATION AGENT

As calculation agent, AAI will calculate the payout to you at maturity of the Securities. AAI and other affiliates may carry out hedging activities related to the Securities, including trading in the Underlying Shares, as well as in other instruments related to the Underlying Shares. AAI and some of our other affiliates also trade the Underlying Shares on a regular basis as part of their general broker dealer businesses. Any of these activities could influence AAI's determinations as calculation agent and any such trading activity could potentially affect the price of the Underlying Shares and, accordingly could effect the payout on the Securities. AAI IS AN AFFILIATE OF ABN AMRO BANK N.V.

In addition, if certain reorganization events occur as defined under "Description of Securities--Adjustment Events" the calculation agent may adjust

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the initial price and consequently the knock-in level and stock redemption amount to reflect the new securities issued in such reorganization event. The calculation agent may make such adjustment based on its assessment of the market value and volatility of those new securities, which may adversely affect the value of the Securities. The calculation agent's adjustment to the Securities may be influenced by, among other things, our or our affiliates' hedging transactions with respect to the Securities and our or their ability to hedge our obligations under the Securities following those reorganization events. While we do not currently anticipate the occurrence of a reorganization event, there can be no assurance that a reorganization event will not occur or that the calculation agent's adjustments upon a reorganization event will not adversely affect the value of the Securities.

Moreover, the issue price of the Securities includes the agents' commissions and certain costs of hedging our obligations under the Securities. Our affiliates through which we hedge our obligations under the Securities expect to make a profit. Since hedging our obligations entails risk and may be influenced by market forces beyond our affiliates' control, such hedging may result in a profit that is more or less than initially projected.

### TAX TREATMENT

You should also consider the tax consequences of investing in the Securities. Significant aspects of the tax treatment of the Securities are uncertain. We do not plan to request a ruling from the U.S. Internal Revenue Service (the "IRS") or from the Dutch authorities regarding the tax treatment of the Securities, and the IRS, the Dutch authorities or a court may not agree with the tax treatment described in the accompanying Prospectus Supplement. Please read carefully the sections entitled "United States Federal Taxation" (and in particular the subsection entitled "--Mandatorily Exchangeable Notes--Reverse Exchangeable and Knock-in Reverse Exchangeable Securities") and "Taxation in the Netherlands" in the accompanying Prospectus Supplement. You should consult your tax advisor about your own situation.

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### HYPOTHETICAL SENSITIVITY ANALYSIS OF TOTAL RETURN OF THE SECURITIES AT MATURITY

The following tables set out the total return to maturity of a Security, based on the assumptions outlined below and several variables, which include (a) whether the closing price of the Underlying Shares has fallen below the knock-in level on any trading day during the Knock-in Period and (b) several hypothetical closing prices for the Underlying Shares on the determination date. The information in the tables is based on hypothetical market values for the Underlying Shares. We cannot predict the market price or the closing price of the Underlying Shares on the determination date or at any time during the life of the Securities. THE ASSUMPTIONS EXPRESSED BELOW ARE FOR ILLUSTRATIVE PURPOSES ONLY AND THE RETURNS SET FORTH IN THE TABLE MAY OR MAY NOT BE THE ACTUAL RATES APPLICABLE TO A PURCHASER OF THE SECURITIES.

#### ASSUMPTIONS

Initial Price:	\$17.30 (the closing price on the day we priced the Securities)
Knock-in level:	\$11.25 (65% of the Initial Price)
Annual Interest on the Securities:	27.50%

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Term of the Securities: 1 year

Exchange Factor: 1.0 (we have assumed that no market disruption event occurs and the calculation agent does not need to adjust the exchange factor for any adjustment events during the term of the Securities).

PAYMENT AT MATURITY IF THE CLOSING PRICE OF THE UNDERLYING SHARES FALLS BELOW THE KNOCK-IN LEVEL ON ANY TRADING DAY DURING THE KNOCK-IN PERIOD:

ASSUMED COUNTRYWIDE CLOSING PRICE ON DETERMINATION DATE	VALUE OF PAYMENT AT MATURITY (a)	TWELVE MONTHLY INTEREST PAYMENTS (c)	TOTAL RETURN (b)	
			\$	%
+\$17.30	\$1,000.00	\$275.00	\$1,275.00	27.50%
\$17.30	\$1,000.00	\$275.00	\$1,275.00	27.50%
\$16.87	\$ 975.14	\$275.00	\$1,250.14	25.01%
\$16.09	\$ 930.05	\$275.00	\$1,205.05	20.51%
\$15.74	\$ 909.82	\$275.00	\$1,184.82	18.48%
\$14.17	\$ 819.07	\$275.00	\$1,094.07	9.41%
\$12.47	\$ 720.80	\$275.00	\$ 995.80	-0.42%
\$ 9.98	\$ 576.87	\$275.00	\$ 851.87	-14.81%
\$ 6.99	\$ 404.04	\$275.00	\$ 679.04	-32.10%
\$ 3.50	\$ 202.31	\$275.00	\$ 477.31	-52.27%
\$ 1.75	\$ 101.16	\$275.00	\$ 376.16	-62.38%
\$ 0.00	\$ 0.00	\$275.00	\$ 275.00	-72.50%

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PAYMENT AT MATURITY IF THE CLOSING PRICE OF THE UNDERLYING SHARES NEVER FALLS BELOW THE KNOCK-IN LEVEL ON ANY TRADING DAY DURING THE KNOCK-IN PERIOD:

ASSUMED COUNTRYWIDE CLOSING PRICE ON DETERMINATION DATE	VALUE OF PAYMENT AT MATURITY (d)	TWELVE MONTHLY INTEREST PAYMENTS (c)	TOTAL RETURN (b)	
			\$	%
+\$17.30	\$1,000.00	\$275.00	\$1,275.00	27.50%
\$17.30	\$1,000.00	\$275.00	\$1,275.00	27.50%
\$15.57	\$1,000.00	\$275.00	\$1,275.00	27.50%
\$14.79	\$1,000.00	\$275.00	\$1,275.00	27.50%
\$11.25	\$1,000.00	\$275.00	\$1,275.00	27.50%

(a) Based on the assumptions set forth above, if the closing price of the Underlying Shares falls below \$11.25 on any trading day during the Knock-in Period and, in addition, the closing price of the Underlying Shares is less than \$17.30 on the determination date, the payment at maturity will be made in Underlying Shares. For determining the value of the payment at maturity, we have assumed that the closing price of the Underlying Shares will be the same on the maturity date as on the determination date.

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- (b) The total return presented is exclusive of any tax consequences of owning the Securities. You should consult your tax adviser regarding whether owning the Securities is appropriate for your tax situation. See the sections titled "Risk Factors" in this Pricing Supplement and "United States Federal Taxation" and "Taxation in the Netherlands" in the accompanying Prospectus Supplement.
- (c) Interest on the Securities will be computed on the basis of a 360-day year of twelve 30-day months or, in the case of an incomplete month, the number of actual days elapsed. Accordingly, depending on the number of days in any monthly interest payment period, the coupon payable in such period and, consequently, the total interest payable over the life of the Securities, may be less than the amount reflected in this column.
- (d) Based on the assumptions set forth above, if the closing price of the Underlying Shares never falls below \$11.25 on any trading day during the Knock-in Period, the payment at maturity will be made in cash.

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### INCORPORATION OF DOCUMENTS BY REFERENCE

Holding is subject to the informational requirements of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and in accordance therewith, Holding files reports and other information with the Securities and Exchange Commission (the "Commission"). You may read and copy these documents at the SEC Headquarters Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549 (tel: 202-551-8090), and at the SEC's regional offices at Northeast Regional Office, 3 World Financial Center, Room 4300, New York, NY 10281 (tel: 212-336-1100) and Midwest Regional Office, 175 W. Jackson Boulevard, Suite 900, Chicago, Illinois 60604. Copies of this material can also be obtained from the Public Reference Room of the Commission at 100 F Street, N.E., Washington, D.C. 20549 at prescribed rates. Please call the Commission at 1-800-SEC-0330 for further information about the Public Reference Room. The Commission also maintains an Internet website that contains reports and other information regarding Holding that are filed through the Commission's Electronic Data Gathering, Analysis and Retrieval (EDGAR) System. This website can be accessed at [www.sec.gov](http://www.sec.gov). You can find information Holding has filed with the Commission by reference to file number 1-14624.

This Pricing Supplement is part of a registration statement that we and Holding filed with the Commission. This Pricing Supplement omits some information contained in the registration statement in accordance with Commission rules and regulations. You should review the information and exhibits in the registration statement for further information on us and Holding and the securities we and Holding are offering. Statements in this prospectus concerning any document we and Holding filed as an exhibit to the registration statement or that Holding otherwise filed with the Commission are not intended to be comprehensive and are qualified by reference to these filings. You should review the complete document to evaluate these statements.

The Commission allows us to incorporate by reference much of the information that we and Holding file with them, which means that we can disclose important information to you by referring you to those publicly available documents. The information that we and Holding incorporate by reference in this Pricing Supplement is considered to be part of this Pricing Supplement. Because we and Holding are incorporating by reference future filings with the Commission, this Pricing Supplement is continually updated and

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those future filings may modify or supersede some of the information included or incorporated in this Pricing Supplement. This means that you must look at all of the Commission filings that we and Holding incorporate by reference to determine if any of the statements in this Pricing Supplement or in any document previously incorporated by reference have been modified or superseded. This Pricing Supplement incorporates by reference all Annual Reports on Form 20-F filed by Holding since September 29, 2006, and any future filings that we or Holding make with the Commission (including any Form 6-K's that we or Holding subsequently file with the Commission) under Section 13(a), 13(c), 14 or 15(d) of the Exchange Act, that are identified in such filing as being specifically incorporated by reference into Registration Statement Nos. 333-137691 or 333-137691-02, of which this Pricing Supplement is a part, until we and Holding complete our offering of the Securities to be issued hereunder or, if later, the date on which any of our affiliates cease offering and selling these Securities.

You may request, at no cost to you, a copy of these documents (other than exhibits not specifically incorporated by reference) by writing or telephoning us at: ABN AMRO Bank N.V., ABN AMRO Investor Relations Department, Hoogoorddreef 66-68, P.O. Box 283, 1101 BE Amsterdam, The Netherlands (Telephone: (31-20) 628 3842).

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### PUBLIC INFORMATION REGARDING THE UNDERLYING SHARES

According to publicly available documents, Countrywide is a holding company which, through its subsidiaries, is engaged in mortgage lending and other real estate finance-related businesses, including mortgage banking, banking and mortgage warehouse lending, dealing in securities and insurance underwriting.

The Underlying Shares are registered under the Exchange Act. Companies with securities registered under the Exchange Act are required periodically to file certain financial and other information specified by the Commission. Information provided to or filed with the Commission can be inspected and copied at the public reference facilities maintained by the Commission at the SEC Headquarters Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549 (tel: 202-551-8090), and at the Commission's regional offices at Northeast Regional Office, 3 World Financial Center, Room 4300, New York, New York 10281 (tel: 212-336-1100) and Midwest Regional Office, 175 W. Jackson Boulevard, Suite 900, Chicago, Illinois 60604. Copies of this material can also be obtained from the Public Reference Room of the Commission at 100 F Street, N.E., Washington, D.C. 20549 at prescribed rates. Please call the Commission at 1-800-SEC-0330 for further information about the Public Reference Room. In addition, information provided to or filed with the Commission electronically can be accessed through a website maintained by the Commission. The address of the Commission's website is <http://www.sec.gov>. Information provided to or filed with the Commission by Countrywide pursuant to the Exchange Act can be located by reference to Commission file number 1-8422.

In addition, information regarding Countrywide Financial Corporation may be obtained from other sources including, but not limited to, press releases, newspaper articles and other publicly disseminated documents. We make no representation or warranty as to the accuracy or completeness of such reports.

THIS PRICING SUPPLEMENT RELATES ONLY TO THE SECURITIES OFFERED HEREBY AND DOES NOT RELATE TO THE UNDERLYING SHARES OR OTHER SECURITIES OF COUNTRYWIDE WE HAVE DERIVED ALL DISCLOSURES CONTAINED IN THIS PRICING SUPPLEMENT REGARDING

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COUNTRYWIDE FROM THE PUBLICLY AVAILABLE DOCUMENTS DESCRIBED IN THE PRECEDING PARAGRAPH. NEITHER WE NOR HOLDING NOR THE AGENTS HAVE PARTICIPATED IN THE PREPARATION OF SUCH DOCUMENTS OR MADE ANY DUE DILIGENCE INQUIRY WITH RESPECT TO COUNTRYWIDE IN CONNECTION WITH THE OFFERING OF THE SECURITIES. NEITHER WE NOR HOLDING NOR THE AGENTS MAKE ANY REPRESENTATION THAT SUCH PUBLICLY AVAILABLE DOCUMENTS OR ANY OTHER PUBLICLY AVAILABLE INFORMATION REGARDING COUNTRYWIDE ARE ACCURATE OR COMPLETE. FURTHERMORE, NEITHER WE NOR HOLDING CAN GIVE ANY ASSURANCE THAT ALL EVENTS OCCURRING PRIOR TO THE DATE HEREOF (INCLUDING EVENTS THAT WOULD AFFECT THE ACCURACY OR COMPLETENESS OF THE PUBLICLY AVAILABLE DOCUMENTS DESCRIBED IN THE PRECEDING PARAGRAPH) THAT WOULD AFFECT THE TRADING PRICE OF THE UNDERLYING SHARES (AND THEREFORE THE INITIAL PRICE AND THE KNOCK-IN LEVEL AND STOCK REDEMPTION AMOUNT) HAVE BEEN PUBLICLY DISCLOSED. SUBSEQUENT DISCLOSURE OF ANY SUCH EVENTS OR THE DISCLOSURE OF OR FAILURE TO DISCLOSE MATERIAL FUTURE EVENTS CONCERNING COUNTRYWIDE COULD AFFECT THE VALUE YOU WILL RECEIVE ON THE MATURITY DATE WITH RESPECT TO THE SECURITIES AND THEREFORE THE TRADING PRICES OF THE SECURITIES. NEITHER WE NOR HOLDING NOR ANY OF OUR AFFILIATES HAVE ANY OBLIGATION TO DISCLOSE ANY INFORMATION ABOUT COUNTRYWIDE AFTER THE DATE OF THIS PRICING SUPPLEMENT.

NEITHER WE NOR HOLDING NOR ANY OF OUR AFFILIATES MAKES ANY REPRESENTATION TO YOU AS TO THE PERFORMANCE OF THE UNDERLYING SHARES.

We and/or our affiliates may presently or from time to time engage in business with Countrywide, including extending loans to, or making equity investments in, or providing advisory services to Countrywide, including merger and acquisition advisory services. In the course of such business, we and/or our affiliates may acquire non-public information with respect to Countrywide and, in addition, one or more of our affiliates may publish research reports with respect to Countrywide. The statement in the preceding sentence is not intended to affect the rights of holders of the Securities under the securities laws. AS A PROSPECTIVE PURCHASER OF A SECURITY, YOU SHOULD UNDERTAKE SUCH INDEPENDENT INVESTIGATION OF COUNTRYWIDE AS IN YOUR JUDGMENT IS APPROPRIATE TO MAKE AN INFORMED DECISION WITH RESPECT TO AN INVESTMENT IN THE UNDERLYING SHARES.

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HISTORICAL INFORMATION

The Underlying Shares are traded on the NYSE under the symbol "CFC". The following table sets forth the published highest intra-day price for the quarter, lowest intra-day price for the quarter and last day closing price for the quarter of the Underlying Shares since 2003. We obtained the prices listed below from Bloomberg Financial Markets without independent verification. You should not take the historical prices of the Underlying Shares as an indication of future performance. NEITHER WE NOR HOLDING CAN GIVE ANY ASSURANCE THAT THE PRICE OF THE UNDERLYING SHARES WILL NOT DECREASE, SUCH THAT WE WILL DELIVER UNDERLYING SHARES AT MATURITY.

PERIOD	HIGH INTRA-DAY PRICE	LOW INTRA-DAY PRICE	LAST DAY CLOSING PRICE
-----	-----	-----	-----
2003			
First Quarter.....	\$14.68	\$12.62	\$14.38
Second Quarter.....	\$19.68	\$14.43	\$17.39
Third Quarter.....	\$19.83	\$15.88	\$19.57

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Fourth Quarter.....	\$27.27	\$19.38	\$25.28
2004			
First Quarter.....	\$32.41	\$23.13	\$31.97
Second Quarter.....	\$36.27	\$27.20	\$35.13
Third Quarter.....	\$39.83	\$32.75	\$39.39
Fourth Quarter.....	\$39.93	\$30.30	\$37.01
2005			
First Quarter.....	\$38.65	\$31.19	\$32.46
Second Quarter.....	\$40.31	\$30.54	\$38.61
Third Quarter.....	\$39.64	\$32.38	\$32.98
Fourth Quarter .....	\$36.74	\$29.35	\$34.19
2006			
First Quarter.....	\$37.23	\$31.86	\$36.70
Second Quarter.....	\$43.67	\$35.93	\$38.08
Third Quarter .....	\$39.99	\$32.20	\$35.04
Fourth Quarter.....	\$43.09	\$34.50	\$42.45
2007			
First Quarter .....	\$45.19	\$33.13	\$33.64
Second Quarter.....	\$42.24	\$32.32	\$36.35
Third Quarter.....	\$37.52	\$15.00	\$19.01
Fourth Quarter (through October 26, 2007).....	\$20.53	\$12.07	\$17.30

Neither we nor Holding make any representation as to the amount of dividends, if any, that Countrywide will pay in the future. In any event, as a holder of a Security, you will not be entitled to receive dividends, if any, that may be payable on the Underlying Shares.

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DESCRIPTION OF SECURITIES

Capitalized terms not defined herein have the meanings given to such terms in the accompanying Prospectus Supplement. The term "Security" refers to each \$1,000 principal amount of our 27.50% Knock-in Reverse Exchangeable Securities due October 31, 2008 linked to common stock of the Underlying Company and fully and unconditionally guaranteed by Holding.

Principal Amount:..... \$500,000

Underlying Shares..... Common Stock, \$0.05 par value per share, of Countrywide Financial Corporation

Underlying Company..... Countrywide Financial Corporation

Original Issue Date..... October 31, 2007

Pricing Date..... October 26, 2007

Issue Price..... 100%

Initial Price..... \$17.30 (the Closing Price per Underlying Share when we priced the Securities on the Pricing Date, divided by the Exchange Factor).

Knock-in Level..... 65% of the Initial Price, which will be determined by the Calculation Agent. The Initial Price and consequently the Knock-in Level may be adjusted for certain corporate events affecting

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the Underlying Company.

Maturity Date..... October 31, 2008

Specified Currency..... U.S. Dollars

CUSIP..... 00078UF54

Denominations..... The Securities may be purchased in denominations of \$1,000 and integral multiples thereof.

Form of Securities..... The Securities will be represented by a single registered global security, deposited with the Depository Trust Company.

Guarantee..... The payment and delivery obligations of ABN AMRO Bank N.V. under the Securities, when and as they shall become due and payable, whether at maturity or upon acceleration, are fully and unconditionally guaranteed by ABN AMRO Holding N.V.

Interest Rate..... 27.50% per annum, payable monthly in arrears on the last day of each month commencing on November 30, 2007 and ending on the Maturity Date, which shall represent (a) an interest coupon of 4.80% and (b) an option premium of 22.70% per annum.

Payment at Maturity..... If the Closing Price per Underlying Share has not fallen below the Knock-in Level on any Trading Day during the Knock-in Period, we will pay you the principal amount of each Security in cash. If the Closing Price per Underlying Share has fallen below the Knock-in Level on any Trading Day during the Knock-in Period, then (i) if the Closing Price per Underlying Share on the Determination Date is below the Initial Price, we will deliver to you, in exchange for each Security, a number of Underlying Shares equal to the Stock Redemption Amount or (ii) if the Closing Price per Underlying Share on the Determination Date is at or above the Initial Price, we will pay you the principal amount of each Security in cash. We will pay cash in lieu of delivering fractional Underlying Shares in an amount equal to the corresponding fractional Closing Price of the Underlying Shares, as determined by the Calculation Agent on the Determination Date. Following a Reorganization Event, the amount payable at maturity is subject to adjustments as described below under "--

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Adjustment Events."

Stock Redemption Amount..... The Calculation Agent will determine the Stock Redemption Amount on the Determination Date by

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dividing \$1,000 by the Initial Price of the Underlying Shares. The Initial Price and consequently the Stock Redemption Amount may be adjusted for certain corporate events affecting the Underlying Company. The interest payment on the Securities at maturity will be paid in cash.

Determination Date..... The third scheduled Trading Day prior to the Maturity Date; provided that if such day is not a Trading Day, or if a Market Disruption Event has occurred on such a Trading Day, the Determination Date shall be the immediately succeeding Trading Day; provided, further, that the Determination Date shall be no later than the second scheduled Trading Day preceding the Maturity Date, notwithstanding the occurrence of a Market Disruption Event on such second scheduled Trading Day.

Closing Price..... If the Underlying Shares (or any other security for which a closing price must be determined) are listed on a U.S. securities exchange registered under the Exchange Act, or are included in the OTC Bulletin Board Service, which we refer to as the OTC Bulletin Board (operated by the Financial Industry Regulatory Authority), the Closing Price for one Underlying Share (or one unit of any such other security) on any Trading Day means (i) the last reported sale price, regular way, in the principal trading session on such day on the principal securities exchange on which the Underlying Shares (or any such other security) are listed or admitted to trading or (ii) if not listed or admitted to trading on any such securities exchange or if such last reported sale price is not obtainable (even if the Underlying Shares, or other such security, are listed or admitted to trading on such securities exchange), the last reported sale price in the principal trading session on the over-the-counter market as reported on the Relevant Exchange or OTC Bulletin Board on such day. If the last reported sale price is not available pursuant to clause (i) or (ii) of the preceding sentence, the Closing Price for any Trading Day shall be the mean, as determined by the Calculation Agent, of the bid prices for the Underlying Shares (or any such other security) obtained from as many dealers in such security (which may include AAI or any of our other affiliates), but not exceeding three, as will make such bid prices available to the Calculation Agent. The term "OTC Bulletin Board Service" shall include any successor service thereto.

Relevant Exchange..... The primary U.S. securities organized exchange or market of trading for the Underlying Shares. If a Reorganization Event has occurred, the Relevant Exchange will be the stock exchange or securities market on which the Exchange Property (as defined below under "--Adjustment Events") that is a listed equity security is principally traded as

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determined by the Calculation Agent.

Trading Day..... A day, as determined by the Calculation Agent, on which trading is generally conducted on the Relevant Exchange.

Book Entry Note or  
Certificated Note..... Book Entry

Trustee..... Wilmington Trust Company

Securities Administrator..... Citibank, N.A.

Market Disruption Event..... Means, with respect to any securities for which a Closing Price must be determined:

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(i) either:

- (x) any suspension of or limitation imposed on trading in such securities by the primary exchange therefore or otherwise and whether by reason of movements in price exceeding limits permitted by such exchange or otherwise or by any exchange or quotation system on which trading in futures or options contracts relating to such securities is executed, or
- (y) any event (other than an event described in clause (z) below) that disrupts or impairs (as determined by the Calculation Agent) the ability of market participants in general (1) to effect transactions in or obtain market values for such securities on the primary exchange therefore or (2) to effect transactions in or obtain market values for futures or options contracts relating to such securities on any other exchange, or
- (z) the closure on any Trading Day of the primary exchange for such securities, or any exchange or quotation system on which trading in future or options relating such securities is executed, prior to its scheduled closing time unless such earlier closing time is announced by such exchange at least one hour prior to the earlier of (1) the actual closing time for the regular trading session on such exchange on such Trading Day and (2) the submission deadline for orders to be entered into such exchange for execution on such Trading Day; and

- (ii) a determination by the Calculation Agent in its sole discretion that the event described in clause (i) above materially interfered with our ability or the ability of any of our affiliates to unwind or adjust all or a material portion of the hedge with respect to the Securities.

For purposes of determining whether a market disruption event has occurred: (1) a limitation on the hours or number of days of trading will not constitute a market disruption event if it results from an announced change in the regular business hours of the relevant exchange; (2) a decision to permanently discontinue trading in the relevant futures or options contract will not constitute a market disruption event; (3) limitations pursuant to New York Stock Exchange Inc. Rule 70A (or any applicable rule or regulation enacted or promulgated by the New York Stock Exchange Inc., any other self-regulatory organization or the Commission of similar scope as determined by the calculation agent) on trading during significant market fluctuations shall constitute a suspension, absence or material limitation of trading; (4) a suspension of trading in a futures or options contract on such securities by the primary securities market trading in such futures or options, if available, by reason of (x) a price change exceeding limits set by such securities exchange or market, (y) an imbalance of orders relating to such contracts or (z) a disparity in bid and ask quotes relating to such contracts will constitute a suspension, absence or material limitation of trading in futures or options contracts related to such securities; and (5) a suspension, absence or material limitation of trading on the primary securities market on which futures or options contracts related to such securities are traded will not include any time when such securities market is itself closed for trading under ordinary circumstances.

The Calculation Agent shall as soon as reasonably practicable under the circumstances notify us, the trustee, the Depository Trust Company and the agents of the existence or occurrence of a Market Disruption Event on

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any day that but for the occurrence or existence of a Market Disruption Event would have been the Determination Date.

Exchange Factor..... The Exchange Factor will be set initially at 1.0, but will be subject to adjustment upon the

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occurrence of certain corporate events affecting the Underlying Shares. See "Adjustment Events" below.

Adjustment Events..... The Exchange Factor or the amounts paid at maturity will be adjusted as follows:

1. If the Underlying Shares are subject to a stock split or reverse stock split, then once such split has become effective, the Exchange Factor will be proportionately adjusted.
2. If the Underlying Shares are subject (i) to a stock dividend (i.e., the issuance of additional Underlying Shares) that is given ratably to all holders of Underlying Shares or (ii) to a distribution of the Underlying Shares as a result of the triggering of any provision of the corporate charter of the Underlying Company, in each case other than a stock split described in paragraph 1, then once the dividend has become effective and the Underlying Shares are trading ex-dividend, the Exchange Factor will be proportionally adjusted.
3. There shall be no adjustments to the Exchange Factor to reflect cash dividends or other distributions paid with respect to the Underlying Shares unless such cash dividends or other distributions constitute Extraordinary Dividends as described below (except that distributions described in paragraph 2 above shall not be subject to this paragraph). A cash dividend or other distribution with respect to the Underlying Shares shall be deemed to be an "Extraordinary Dividend" if such dividend or other distribution exceeds the immediately preceding non-Extraordinary Dividend for the Underlying Shares by an amount equal to at least 10% of the Closing Price of the Underlying Shares (as adjusted for any subsequent corporate event requiring an adjustment hereunder, such as a stock split or reverse stock split) on the Trading Day preceding the ex-dividend date for the payment of such Extraordinary Dividend (the "ex-dividend date"). If an Extraordinary Dividend occurs with respect to the Underlying Shares, the Exchange Factor with respect to the Underlying Shares will be adjusted on the ex-dividend date with respect to such Extraordinary Dividend so that the new Exchange Factor will equal the product of (i) the then-current Exchange Factor and (ii) a fraction, the numerator of which is the Closing Price on the Trading Day preceding the ex-dividend date, and the denominator of which is the amount by which the Closing Price on the Trading Day

preceding the ex-dividend date exceeds the Extraordinary Dividend Amount. The "Extraordinary Dividend Amount" with respect to an Extraordinary Dividend for the Underlying Shares shall equal (i) in the case of cash dividends or other distributions that constitute regular dividends, the amount per share of such Extraordinary Dividend minus the amount per share of the immediately preceding non-Extraordinary Dividend for the Underlying Shares or (ii) in the case of cash dividends or other distributions that do not constitute regular dividends, the amount per share of such Extraordinary Dividend. To the extent an Extraordinary Dividend is not paid in cash, the value of the non-cash component will be determined by the calculation agent, whose determination shall be conclusive. A distribution on the Underlying Shares described in clause (A), clause (D) or clause (E) in the definitions of

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"Reorganization Event" of paragraph 5 below that also constitutes an Extraordinary Dividend shall not cause an adjustment to the Exchange Factor pursuant to this paragraph 3.

4. If the Underlying Company issues rights or warrants to all holders of the Underlying Shares to subscribe for or purchase Underlying Shares at an exercise price per share less than the closing price of the Underlying Shares on both (i) the date the exercise price of such rights or warrants is determined and (ii) the expiration date of such rights or warrants, and if the expiration date of such rights or warrants precedes the maturity of this Note, then the Exchange Factor shall be adjusted to equal the product of the prior Exchange Factor and a fraction, the numerator of which shall be the number of Underlying Shares outstanding immediately prior to the issuance of such rights or warrants plus the number of additional Underlying Shares offered for subscription or purchase pursuant to such rights or warrants and the denominator of which shall be the number of Underlying Shares outstanding immediately prior to the issuance of such rights or warrants plus the number of additional Underlying Shares which the aggregate offering price of the total number of shares of the Underlying Shares so offered for subscription or purchase

pursuant to such rights or warrants would purchase at the closing price on the expiration date of such rights or warrants, which shall be determined by multiplying such total number of shares offered by the exercise price of such rights or warrants and dividing the product so obtained by such Closing Price.

5. If a Reorganization Event (as defined below) occurs, the payment at maturity will depend on (i) whether the Closing Price of the Underlying Shares fell below the Knock-in Level on any Trading Day from but not including the Pricing Date to and including one Trading Day prior to the date of the Reorganization Event (for purposes of this paragraph 5, we refer to such period as the "Relevant Period"), and (ii) the kind and amount of Exchange Property (as defined below) received by holders of Underlying Shares in the Reorganization Event.

In the case where the Closing Price of the Underlying Shares has fallen below the Knock-in Level on any Trading Day during the Relevant Period, each holder of a Security will receive at maturity, in respect of each \$1,000 principal amount of each Security, the lesser of: (i) \$1,000 in cash or (ii) Exchange Property in an amount with a value equal to the product of the Stock Redemption Amount times the Transaction Value (as defined below).

In the case where the Closing Price of the Underlying Shares has not fallen below the Knock-in Level on any Trading Day during the Relevant Period, then the payment at maturity will depend upon the type of Exchange Property received by holders of Underlying Shares in accordance with the following:

- (i) If the Exchange Property consists solely of equity securities listed on a securities exchange that, in the opinion of the Calculation Agent, maintains sufficient liquidity for trading in such Exchange Property, then the payment at maturity for each \$1,000 principal amount of Securities will depend on whether the Closing Price of such Exchange Property has fallen below the Knock-in Level on any Trading Day

commencing on the date of such Reorganization Event to and including the Determination Date:

- (a) If the Closing Price of such Exchange Property has not fallen below the Knock-in Level on any Trading Day commencing on the date of such Reorganization Event to and including the Determination Date, then each holder of a Security will receive the principal amount of \$1,000 in cash; or
- (b) If the Closing Price of such Exchange Property has fallen below the Knock-in Level on any Trading Day commencing on the date of such Reorganization Event to and including the Determination Date, then (x) if the Closing Price of such Exchange Property on the Determination Date is below the Initial Price, we will deliver to you, in exchange for each Security, Exchange Property with a value equal to the product of the Stock Redemption Amount times the Transaction Value and (y) if the Closing Price of such Exchange Property on the Determination Date is at or above the Initial Price, we will pay you \$1,000 in cash.

The Calculation Agent will adjust the Initial Price and consequently the Knock-in Level to reflect the new securities delivered in such Reorganization Event and the market value and volatility levels of such securities and any Exchange Factor adjustments to the Initial Price as of the effective date of the Reorganization Event. Following any such adjustment, the Initial Price will be such adjusted Initial Price, divided by the Exchange Factor (which shall have been reset to 1.0 immediately following the Reorganization Event). The Bank will provide notice to the Trustee and the Securities Administrator of the adjusted Knock-in Level and Initial Price as soon as

practicable after the date of such Reorganization Event.

- (ii) If the Exchange Property consists solely of property other than such listed equity securities, each holder of a Security will receive, on the Maturity Date, in exchange for each \$1,000 principal amount of Securities, the lesser of: (i) \$1,000 in cash or (ii) Exchange Property in an amount with a value equal to the product of the Stock Redemption Amount times the Transaction Value as of the Determination Date. We may, in lieu of delivering such Exchange Property, pay you the cash value of such Exchange Property as of the Determination Date, as determined by the Calculation Agent. We will notify the Trustee and the Securities Administrator of the amount and type of Exchange Property to be delivered or cash to be paid.
  
- (iii) If the Exchange Property consists of any combination of such listed equity securities and other property, then we will (a) deliver, on the Maturity Date, the portion of Exchange Property consisting of such other property with a value equal to the product of the Stock Redemption Amount (prior to any adjustment under this clause) times the Transaction Value of such portion of Exchange Property on the Determination

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Date or, at our election, pay the cash value thereof, as determined by the Calculation Agent, (b) proportionally adjust the Stock Redemption Amount to reflect the portion of the Exchange Property constituting such listed equity securities, (c) adjust the Initial Price and consequently the Knock-in Level to reflect such listed equity securities, the market value and volatility levels of such listed equity securities and any Exchange Factor adjustments to the Initial Price as of the effective date of the

Reorganization Event and (d) reduce the principal amount of each \$1,000 of Securities to an amount equal to such adjusted Stock Redemption Amount multiplied by such adjusted Initial Price. Following such adjustments, the amount paid at maturity for each Security will be determined as set forth under clause (i) above, except references to each \$1,000 principal amount of Security and \$1,000 in cash and the reference to \$1,000 in the definition of Stock Redemption Amount shall be references to the adjusted principal amount of Securities as described in clause (d) of the preceding sentence. In addition, following any such adjustment, the Initial Price will be such adjusted Initial Price, divided by the Exchange Factor (which shall have been reset to 1.0 immediately following the Reorganization Event). The Bank will provide notice to the Trustee and the Securities Administrator of any adjustments to the Securities as a result of this clause (iii) as soon as practicable after the date of such Reorganization Event.

"Reorganization Event" means (A) there has occurred any reclassification or change with respect to the Underlying Shares, including, without limitation, as a result of the issuance of any tracking stock by the Underlying Company; (B) the Underlying Company or any surviving entity or subsequent surviving entity of the Underlying Company (an "Underlying Company Successor") has been subject to a merger, combination or consolidation and is not the surviving entity; (C) any statutory exchange of securities of the Underlying Company or any Underlying Company Successor with another corporation occurs (other than pursuant to clause (B) above); (D) the Underlying Company is liquidated; (E) the Underlying Company issues to all of its shareholders equity securities of an issuer other than the Underlying Company (other than in a transaction described in clauses (B), (C) or (D) above) (a "Spin-off Event"); or (F) a tender or exchange offer or going-private transaction is consummated for all the outstanding Underlying Shares.

"Exchange Property" means securities, cash or any other assets distributed to holders of the Underlying Shares in any

Reorganization Event, including, (A) in the case of the issuance of tracking stock or in the case of a Spin-off Event, the Underlying Shares with respect to which the tracking stock or spun-off security was issued and (B) in the case of any other Reorganization Event where the Underlying Shares continue to be held by the holders receiving such distribution, the Underlying Shares.

"Transaction Value", at any date, means (A) for any cash received as Exchange Property in any such Reorganization Event, the amount of cash received per Underlying Share; (B) for any property other than cash or securities received in any such Reorganization Event, the

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market value, as determined by the Calculation Agent, as of the date of receipt, of such Exchange Property received per Underlying Share; and (C) for any security received in any such Reorganization Event (including in the case of the issuance of tracking stock, the reclassified Underlying Shares and, in the case of a Spin-off Event, the Underlying Shares with respect to which the spun-off security was issued), an amount equal to the Closing Price, as of the determination date, per share of such security multiplied by the quantity of such security received for each Underlying Share.

For purposes of clause (iii) above, if Exchange Property consists of more than one type of property that is not listed equity securities described in clause (iii) above, holders of Securities will receive at maturity a pro rata share of each such type of Exchange Property in proportion to the quantity of such Exchange Property received in respect of each Underlying Share. If Exchange Property includes a cash component, holders will not receive any interest accrued on such cash component. In the event Exchange Property consists of securities, those securities will, in turn, be subject to the antidilution adjustments set forth in paragraphs 1 through 5.

For purposes of this paragraph 5:

- (i) in the case of a consummated tender or exchange offer or going-private transaction involving Exchange Property of a

particular type, Exchange Property shall be deemed to include the amount of cash or other property paid by the offeror in the tender or exchange offer with respect to such Exchange Property (in an amount determined on the basis of the rate of exchange in such tender or exchange offer or going-private transaction); and

- (ii) in the event of a tender or exchange offer or a going-private transaction with respect to Exchange Property in which an offeree may elect to receive cash or other property, Exchange Property shall be deemed to include the kind and amount of cash and other property received by offerees who elect to receive cash.

With respect to paragraphs 1 to 5 above, no adjustments to the Exchange Factor shall be required unless such adjustment would require a change of at least 0.1% in the Exchange Factor then in effect. The Exchange Factor resulting from any of the adjustments specified above shall be rounded to the nearest one hundred-thousandth with five one-millionths being rounded upward.

No adjustments to the Exchange Factor or method of calculating the Exchange Factor shall be required other than those specified above. However, the Bank may, at its sole discretion, cause the Calculation Agent to make additional changes to the Exchange Factor upon the occurrence of corporate or other similar events that affect or could potentially affect market prices of, or shareholders' rights in, the Underlying Shares (or other Exchange Property) but only to reflect such changes, and not with the aim of changing relative investment risk. The adjustments specified above do not cover all events that could affect the Market Price or the Closing Price of the Underlying Shares, including, without limitation, a partial tender or partial exchange offer for the Underlying Shares.

The Calculation Agent shall be solely responsible for the determination

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and calculation of any adjustments to the Exchange Factor or method of calculating the Exchange Factor and of any related determinations

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and calculations with respect to any distributions of stock, other securities or other property or assets (including cash) in connection with any Reorganization Event described in paragraph 5 above, and its determinations and calculations with respect thereto shall be conclusive. The Calculation Agent will provide information as to any adjustments to the Exchange Factor or method of calculating the Exchange Factor upon written request by any holder of the Securities.

Alternate Exchange

Calculation in case

of an Event of Default..... In case an Event of Default with respect to the Securities shall have occurred and be continuing, the amount declared due and payable upon any acceleration of any Security shall be determined by AAI, as Calculation Agent, and shall be equal to the principal amount of the Security plus any accrued interest to, but not including, the date of acceleration.

Calculation Agent..... AAI. All determinations made by the Calculation Agent will be at the sole discretion of the Calculation Agent and will, in the absence of manifest error, be conclusive for all purposes and binding on you and on us.

Additional Amounts..... Subject to certain exceptions and limitations described in "Description of Debt Securities -- Payment of Additional Amounts" in the accompanying Prospectus, we will pay such additional amounts to holders of the Securities as may be necessary in order that the net payment of the principal of the Securities and any other amounts payable on the Securities, after withholding for or on account of any present or future tax, assessment or governmental charge imposed upon or as a result of such payment by The Netherlands (or any political subdivision or taxing authority thereof or therein) or the jurisdiction of residence or incorporation of any successor corporation (other than the United States), will not be less than the amount provided for in the Securities to be then due and payable.

Book Entry..... The indenture for the Securities permits us at anytime and in our sole discretion to decide not to have any of the Securities represented by one or more registered global securities. DTC has advised us that, under its current practices, it would notify its participants of our request, but will only withdraw beneficial interests from the global security at the request of each DTC participant.

Record Date..... The "record date" for any interest payment date is the calendar day prior to that interest payment date, whether or not that date is a business day.

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USE OF PROCEEDS

The net proceeds we receive from the sale of the Securities will be used for general corporate purposes and, in part, by us or one or more of our affiliates in connection with hedging our obligations under the Securities. The issue price of the Securities includes the selling agents' commissions (as shown on the cover page of the accompanying Prospectus Supplement) paid with respect to the Securities and the cost of hedging our obligations under the Securities. The cost of hedging includes the projected profit that our affiliates expect to realize in consideration for assuming the risks inherent in managing the hedging transactions. Since hedging our obligations entails risk and may be influenced by market forces beyond our or our affiliates' control, such hedging may result in a profit that is more or less than initially projected, or could result in a loss. See also "Risk Factors--The Inclusion of Commissions and Cost of Hedging in the Issue Price is Likely to Adversely Affect Secondary Market Prices" and "Potential Conflicts of Interest; No Security Interest in the Underlying Shares Held by Us" and "Plan of Distribution" in this Pricing Supplement and "Use of Proceeds" in the accompanying Prospectus.

TAXATION

Please review carefully the sections entitled "United States Federal Taxation" (and in particular the subsection entitled "--Mandatorily Exchangeable Notes--Reverse Exchangeable and Knock-in Reverse Exchangeable Securities") and "Taxation in the Netherlands" in the accompanying Prospectus Supplement. Prospective purchasers of the Securities should consult their own tax advisers as to the tax consequences of acquiring, holding and disposing of the Securities under the tax law of any state, local and foreign jurisdiction.

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PLAN OF DISTRIBUTION

We have appointed ABN AMRO Incorporated ("AAI") as agent for this offering. AAI has agreed to use reasonable efforts to solicit offers to purchase the Securities. We will pay AAI, in connection with sales of the Securities resulting from a solicitation such agent made or an offer to purchase such agent received, a commission of 3.25% of the initial offering price of the Securities. AAI has informed us that, as part of its distribution of the Securities, it intends to reoffer the Securities to other dealers who will sell the Securities. Each such dealer engaged by AAI, or further engaged by a dealer to whom AAI reoffers the Securities, will purchase the Securities at an agreed discount to the initial offering price of the Securities. AAI has informed us that such discounts may vary from dealer to dealer and that not all dealers will purchase or repurchase the Securities at the same discount. You can find a general description of the commission rates payable to the agents under "Plan of Distribution" in the accompanying Prospectus Supplement.

AAI is a wholly owned subsidiary of the Bank. AAI will conduct this offering in compliance with the requirements of NASD Rule 2720 of the Financial Industry Regulatory Authority (the successor to the National Association of Securities Dealers, Inc.) which is commonly referred to as FINRA, regarding a

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FINRA member firm's distributing the securities of an affiliate. When the distribution of the Securities is complete, AAI may offer and sell those Securities in the course of its business as broker-dealer. AAI may act as principal or agent in those transactions and will make any sales at prevailing secondary market prices at the time of sale. AAI may use this Pricing Supplement and the accompanying Prospectus and Prospectus Supplement in connection with any of those transactions. AAI is not obligated to make a market in the Securities and may discontinue any purchase and sale activities with respect to the Securities at any time without notice.

To the extent that the total aggregate principal amount of the Securities being offered by this Pricing Supplement is not purchased by investors in the offering, one or more of our affiliates has agreed to purchase the unsold portion, and to hold such Securities for investment purposes. See "Holding of the Securities by our Affiliates and Future Sales" under the heading "Risk Factors."

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FILED PURSUANT TO RULE 424(B)(2)  
REGISTRATION NOS. 333-137691  
333-137691-02

PROSPECTUS SUPPLEMENT  
(TO PROSPECTUS DATED SEPTEMBER 29, 2006)

[ABN AMRO BANK N.V. GRAPHIC OMITTED]

US\$ 7,500,000,000 ABN NOTES (SM)

fully and unconditionally guaranteed by ABN AMRO Holding N.V.

We, ABN AMRO Bank N.V., may offer from time to time senior notes. The specific terms of any notes that we offer will be included in a pricing supplement. The notes will have the following general terms:

- o The notes will bear interest at either a fixed rate or a floating rate that varies during the lifetime of the relevant notes, which, in either case, may be zero. Floating rates will be based on rates or indices specified in the applicable pricing supplement.
- o The notes will pay interest, if any, on the dates stated in the applicable pricing supplement.
- o The notes will be fully and unconditionally guaranteed by ABN AMRO Holding N.V.
- o The notes will be held in global form by The Depository Trust Company, unless the pricing supplement provides otherwise.

The pricing supplement may also specify that the notes will have additional terms, including the following:

- o The notes may be optionally or mandatorily exchangeable for securities of an entity that is not affiliated with us, for a basket or index of those securities, or for the cash value of those securities.
- o Payments on the notes may be linked to currency prices, commodity prices, securities of entities not affiliated with us, baskets of those securities or indices, or any combination of the above.

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- o The notes may be either callable by us or puttable by you.

INVESTING IN THE NOTES INVOLVES RISKS. SEE "RISK FACTORS" BEGINNING ON PAGE S-2.

THESE SECURITIES ARE NOT INSURED BY THE FEDERAL DEPOSIT INSURANCE CORPORATION OR ANY OTHER FEDERAL AGENCY. THE SECURITIES AND EXCHANGE COMMISSION AND STATE SECURITIES REGULATORS HAVE NOT APPROVED OR DISAPPROVED THESE SECURITIES, OR DETERMINED IF THIS PROSPECTUS SUPPLEMENT OR THE ACCOMPANYING PROSPECTUS IS TRUTHFUL OR COMPLETE. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

ABN AMRO Incorporated and LaSalle Financial Services, Inc. have agreed to use reasonable efforts to solicit offers to purchase these securities as our selling agents to the extent either or both are named in the applicable pricing supplement. Certain other selling agents to be named in the applicable pricing supplement may also be used to solicit such offers on a reasonable efforts basis. We refer to each selling agent individually as the "agent" and together as the "agents". The agents may also purchase these securities as principal at prices to be agreed upon at the time of sale. The agents may resell any securities they purchase as principal at prevailing market prices, or at other prices, as they determine.

ABN AMRO Incorporated and LaSalle Financial Services, Inc. may use this prospectus supplement and the accompanying prospectus in connection with offers and sales of the securities and related guarantees in market-making transactions.

ABN AMRO INCORPORATED

LASALLE FINANCA

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Acquisition by ESOP of Arrow Stock (40,890 Shares)

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(1,000)

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(1,000)

Allocation of ESOP Stock

(17,616 Shares)

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115

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328

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443

Shares Issued for Dividend Reinvestment Plans (49,982 Shares)

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842

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424

1,266

Acquisition of Subsidiary  
(26,240 Shares)

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459

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223

682

Purchase of Treasury Stock  
(106,761 Shares)

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(2,595)

(2,595)

Balance at September 30, 2010

15,625,512

\$15,626

\$190,227

\$22,184

\$(2,876)

\$(2,326)

\$(69,378)

\$153,457

<sup>1</sup> Included in the shares issued for the 3% stock dividend in 2010 were treasury shares of 124,042 and unallocated ESOP shares of 3,855.

<sup>2</sup> Cash dividends paid in 2010 have been restated for the September 2010 3% stock dividend.

See Notes to Unaudited Consolidated Interim Financial Statements.

See accompanying accountants' report.

**ARROW FINANCIAL CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY**

(In Thousands, Except Share and Per Share Amounts) (Unaudited)

	Unallo- Accumulated							
	Common			cated Other Com-				
	Shares	Common		Retained	ESOP	prehensive	Treasury	
	<u>Issued</u>	<u>Stock</u>	<u>Surplus</u>	<u>Earnings</u>	<u>Shares</u>	<u>Loss</u>	<u>Stock</u>	<u>Total</u>
Balance at December 31, 2008	14,728,543	\$14,729	\$163,215	\$25,454	\$(2,572)	\$ (9,404)	\$(65,620)	\$125,802
Comprehensive Income, Net of Tax:								
Net Income	---	---	---	16,675	---	---	---	16,675
Amortization of Net Retirement Plan Actuarial Loss								
(Pre-tax \$1,041)	---	---	---	---	---	629	---	629
Accretion of Net Retirement Plan Prior Service Credit								
(Pre-tax \$138)	---	---	---	---	---	(84)	---	(84)
Net Securities Gains Included								
In Net Income, Net of Tax								
(Pre-tax \$329)	---	---	---	---	---	(199)	---	(199)
Net Unrealized Securities Holding Gains Arising During the Period,								
Net of Tax (Pre-tax \$5,521)	---	---	---	---	---	3,334	---	<u>3,334</u>
Other Comprehensive Income								<u>3,680</u>
Comprehensive Income								<u>20,355</u>
3% Stock Dividend Cash Dividends Paid,	441,857	441	12,066	(12,507)	---	---	---	---
\$.71 per Share <sup>1</sup> Stock Options Exercised	---	---	370	(7,921)	---	---	500	(7,921) 870

(58,133 Shares) Shares Issued Under the Directors'								
Stock Plan (2,324 Shares) Shares Issued Under the Employee	---	---	38	---	---	---	21	59
Stock Purchase Plan (13,776 Shares)	---	---	217	---	---	---	119	336
Stock-Based Compensation Expense	---	---	139	---	---	---	---	139
Tax Benefit for Disposition of Stock Options	---	---	177	---	---	---	---	177
Allocation of ESOP Stock (20,103 Shares)	---	---	146	---	368	---	---	514
Acquisition of Subsidiary (4,398 Shares)	---	---	78	---	---	---	37	115
Shares Issued for Dividend Reinvestment Plans (50,135 Shares)	---	---	802	---	---	---	432	1,234
Purchase of Treasury Stock (96,568 Shares)	---	---	---	---	---	---	(2,376)	(2,376)
Balance at September 30, 2009	<u>15,170,400</u>	<u>\$15,170</u>	<u>\$177,248</u>	<u>\$21,701</u>	<u>\$(2,204)</u>	<u>\$(5,724)</u>	<u>\$(66,887)</u>	<u>\$139,304</u>

<sup>1</sup> Cash dividends paid in 2009 have been restated for the September 2010 3% stock dividend.

See Notes to Unaudited Consolidated Interim Financial Statements.

See accompanying accountants' report.

## ARROW FINANCIAL CORPORATION AND SUBSIDIARIES

### CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in Thousands)(Unaudited)

	Nine Months Ended September 30,	
	<u>2010</u>	<u>2009</u>
<b>Cash Flows from Operating Activities:</b>		
Net Income	\$16,704	\$16,675
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Provision for Loan Losses	1,125	1,348
Depreciation and Amortization	2,566	2,153
Compensation Expense for Allocated ESOP Shares	115	146
Gains on the Sale of Securities Available-for-Sale	(1,496)	(522)
Losses on the Sale of Securities Available-for-Sale	---	193
Loans Originated and Held-for-Sale	(15,041)	(20,694)
Proceeds from the Sale of Loans Held-for-Sale	15,568	21,020
		(326)
Net Gain on the Sale of Loans	(527)	
Net Loss (Gain) on the Sale of Premises and Equipment,		
Other Real Estate Owned and Repossessed Assets	1	(5)
Contributions to Pension Plans	(239)	(2,228)
Deferred Income Tax (Benefit) Expense	(654)	901
Shares Issued Under the Directors' Stock Plan	74	59
Stock-Based Compensation Expense	226	139

Net Increase in Other Assets	(561)	(945)
Net Decrease in Other Liabilities	<u>(2,497)</u>	<u>(1,733)</u>
<b>Net Cash Provided By Operating Activities</b>	<b><u>15,364</u></b>	<b><u>16,181</u></b>
<b>Cash Flows from Investing Activities:</b>		
Proceeds from the Sale of Securities Available-for-Sale	25,440	17,305
Proceeds from the Maturities and Calls of Securities Available-for-Sale	192,092	90,148
Purchases of Securities Available-for-Sale	(241,376)	(189,804)
Proceeds from the Maturities of Securities Held-to-Maturity	13,898	24,629
Purchases of Securities Held-to-Maturity	(3,300)	(53,011)
Net (Increase) Decrease in Loans	(43,436)	1,917
Proceeds from the Sales of Premises and Equipment,		
Other Real Estate Owned and Repossessed Assets	479	1,098
Purchases of Premises and Equipment	(1,095)	(1,641)
Acquisition of Subsidiary	264	---
Net Increase in Other Investments	<u>(539)</u>	<u>(159)</u>
<b>Net Cash Used In Investing Activities</b>	<b><u>(57,573)</u></b>	<b><u>(109,518)</u></b>
<b>Cash Flows from Financing Activities:</b>		
Net Increase in Deposits	103,029	157,419
Net (Decrease) Increase in Short-Term Borrowings	(4,730)	2,237
FHLB Advances	10,000	---
Purchases of Treasury Stock	(2,595)	(2,376)
Treasury Stock Issued for Stock-Based Plans	660	1,206
Tax Benefit from Exercise of Stock Options	67	177
Treasury Stock Issued for Dividend Reinvestment Plans	1,266	1,234
Acquisition of Unallocated Common Stock by the ESOP	(1,000)	---
Allocation of Common Stock Purchased by the ESOP	328	368
Cash Dividends Paid	<u>(8,202)</u>	<u>(7,921)</u>
		(6,663)
<b>Net Cash Provided By Financing Activities</b>	<b><u>98,823</u></b>	<b><u>152,344</u></b>
<b>Net Increase in Cash and Cash Equivalents</b>	<b>56,614</b>	<b>59,007</b>
Cash and Cash Equivalents at Beginning of Period	<u>67,116</u>	<u>58,338</u>
<b>Cash and Cash Equivalents at End of Period</b>	<b><u>\$123,730</u></b>	<b><u>\$117,345</u></b>
<b>Supplemental Disclosures to Statements of Cash Flow Information:</b>		
Interest on Deposits and Borrowings	\$17,910	\$20,229
Income Taxes	12,763	9,875
<b>Non-cash Investing and Financing Activities:</b>		
Transfer of Loans to Other Real Estate Owned and Repossessed Assets	400	459
Change in Net Unrealized Gains on Securities Available-for-Sale, Net of Tax	3,938	3,135
Additional Shares Issued for Acquisition of Subsidiary	682	115
Change in Retirement Plans Net Loss and Prior Service Cost, Net of Tax	376	545
Fair Value of Assets from Acquisition of Subsidiary	882	---
Fair Value of Liabilities from Acquisition of Subsidiary	465	---
See Notes to Unaudited Consolidated Interim Financial Statements.		

See accompanying accountants' report.

**ARROW FINANCIAL CORPORATION AND SUBSIDIARIES**

**NOTES TO UNAUDITED CONSOLIDATED INTERIM FINANCIAL STATEMENTS**

**September 30, 2010**

1. Accounting Policies

In the opinion of the management of Arrow Financial Corporation (Arrow), the accompanying unaudited consolidated interim financial statements contain all of the adjustments necessary to present fairly the financial position as of September 30, 2010 and December 31, 2009; the results of operations for the three and nine-month periods ended September 30, 2010 and 2009; the changes in stockholders' equity for the nine-month periods ended September 30, 2010 and 2009; and the cash flows for the nine-month periods ended September 30, 2010 and 2009. All such adjustments are of a normal recurring nature. The preparation of financial statements requires the use of management estimates. Certain prior period information has been reclassified to conform to the current year presentation. The unaudited consolidated interim financial statements should be read in conjunction with the audited annual consolidated financial statements of Arrow for the year ended December 31, 2009, included in Arrow's 2009 Form 10-K.

Recent Accounting Pronouncements:

*ASU 2010-20, Receivables (Topic 310) - Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses:* The main objective of this guidance is to provide financial statement users with greater transparency about an entity's allowance for credit losses and the credit quality of its financing receivables. This pronouncement requires additional disclosures to assist financial statement users in assessing an entity's credit risk exposures and evaluating the adequacy of its allowance for credit losses. These new disclosures are required for interim and annual reporting periods ending on or after December 15, 2010. We have determined that this pronouncement will not have a material impact on our financial condition or results of operations.

*ASU 2010-12, Income Taxes (Topic 740) – Accounting for Certain Tax Effects of the 2010 Health Care Reform Acts:* For measuring the impact on deferred tax assets and liabilities based on provisions of enacted law, the impact of both Acts, the Health Care and Education Reconciliation Act of 2010 and the Patient Protection and Affordable Care Act, should be considered. This pronouncement requires that income tax deductions for the cost of providing prescription drug coverage will be reduced by the amount of any subsidy received. The provisions were effect for reporting periods ending on or after March 31, 2010. We have determined that this pronouncement will not have a material impact on our financial condition or results of operations.

*ASU 2010-11, Derivatives and Hedging (Topic 815) - Scope Exception Related to Embedded Credit Derivatives:* Clarifies the scope exception for embedded credit derivative features related to the transfer of credit risk in the form of

subordination of one financial instrument to another. The amendments address how to determine which embedded credit derivative features, including those in collateralized debt obligations and synthetic collateralized debt obligations, are considered to be embedded derivatives that should not be analyzed for potential bifurcation and separate accounting. The amendments in this pronouncement are effective for each reporting entity at the beginning of its first fiscal quarter beginning after June 15, 2010 and will not have a material effect on our financial condition or results of operations.

*ASU 2010-06, Fair Value Measurements and Disclosures (Topic 820) - Improving Disclosures about Fair Value Measurements:* Requires additional disclosures about fair value measurements including:

1.

Disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe the reasons for the transfers.

2.

Present separately information about purchases, sales, issuances, and settlements on a gross basis (rather than net) for Level 3 fair value measurements.

3.

Present fair value disclosures for each class of assets and liabilities, and

4.

For Level 2 and 3 fair value measurements, provide disclosures about the valuation techniques and inputs used to measure fair value for both recurring and nonrecurring fair value measurements.

The new disclosures and clarifications of existing disclosures are effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances and settlements in the roll forward of activity in Level 3 fair value measurements, which are effective for interim and annual reporting periods beginning after December 15, 2010. This pronouncement will not have a material impact on the way we measure fair values.

2. Accumulated Other Comprehensive Loss (In Thousands)

The following table presents the components, net of tax, of accumulated other comprehensive loss as of September 30, 2010 and December 31, 2009:

	<u>2010</u>	<u>2009</u>
Retirement Plan Net Loss	\$(9,729)	\$(10,185)
Retirement Plan Prior Service Cost	315	395

Net Unrealized Securities Holding Gains	<u>7,088</u>	<u>3,150</u>
Total Accumulated Other Comprehensive Loss	<u>\$(2,326)</u>	<u>\$(6,640)</u>

### 3. Earnings Per Common Share (In Thousands, Except Per Share Amounts)

The following table presents a reconciliation of the numerator and denominator used in the calculation of basic and diluted earnings per common share (EPS) for the three-month and nine-month periods ended September 30, 2010 and 2009, restated for the September 2010 3% stock dividend:

	<u>Net Income (Numerator)</u>	<u>Shares (Denominator)</u>	<u>Per Share Amount</u>
For the Three Months Ended September 30, 2010:			
Basic EPS	\$5,575	11,257	<u>\$.50</u>
Dilutive Effect of Stock Options	<u>---</u>	<u>3</u>	
Diluted EPS	<u>\$5,575</u>	<u>11,260</u>	<u>\$.50</u>
For the Three Months Ended September 30, 2009:			
Basic EPS	\$5,062	11,239	<u>\$.45</u>
Dilutive Effect of Stock Options	<u>---</u>	<u>73</u>	
Diluted EPS	<u>\$5,062</u>	<u>11,312</u>	<u>\$.45</u>

	<u>Net Income (Numerator)</u>	<u>Shares (Denominator)</u>	<u>Per Share Amount</u>
For the Nine months Ended September 30, 2010:			
Basic EPS	\$16,704	11,275	<u>\$1.48</u>
Dilutive Effect of Stock Options	<u>---</u>	<u>27</u>	
Diluted EPS	<u>\$16,704</u>	<u>11,302</u>	<u>\$1.48</u>
For the Nine Months Ended September 30, 2009:			
Basic EPS	\$16,675	11,229	<u>\$1.48</u>
Dilutive Effect of Stock Options	<u>---</u>	<u>51</u>	
Diluted EPS	<u>\$16,675</u>	<u>11,280</u>	<u>\$1.48</u>

### 4. Investments, Debt and Equity Securities (In Thousands)

A summary of the amortized costs and the approximate fair values of securities at September 30, 2010 and December 31, 2009 is presented below. Amortized cost is reported net of other-than-temporary impairment charges.

#### Securities Available-for-Sale:

	Amortized	Fair	Gross Unrealized	Gross Unrealized
	<u>Cost</u>	<u>Value</u>	<u>Gains</u>	<u>Losses</u>
September 30, 2010:				
U.S. Treasury and Agency Obligations	\$166,940	\$167,655	\$ 715	\$ --
State and Municipal Obligations	65,941	66,148	210	3
Collateralized Mortgage Obligations	146,625	154,196	7,638	67
Mortgage-Backed Securities – Residential	74,819	78,154	3,335	---
Corporate and Other Debt Securities	1,497	1,390	---	107
Mutual Funds and Equity Securities	<u>1,379</u>	<u>1,398</u>	<u>53</u>	<u>34</u>
<u>Total Securities Available-for-Sale</u>	<u>\$457,201</u>	<u>\$468,941</u>	<u>\$11,951</u>	<u>\$211</u>

4. Investments, Debt and Equity Securities, continued**Securities Available-for-Sale:**

	Amortized	Fair	Gross Unrealized	Gross Unrealized
	<u>Cost</u>	<u>Value</u>	<u>Gains</u>	<u>Losses</u>
December 31, 2009:				
U.S. Treasury and Agency Obligations	\$122,768	\$123,331	\$ 566	\$ 3
State and Municipal Obligations	18,843	18,913	75	5
Collateralized Mortgage Obligations	196,359	199,781	4,625	1,203
Mortgage-Backed Securities – Residential	91,745	93,017	2,110	838
Corporate and Other Debt Securities	1,465	1,331	---	134
Mutual Funds and Equity Securities	<u>1,308</u>	<u>1,333</u>	<u>31</u>	<u>6</u>
<u>Total Securities Available-for-Sale</u>	<u>\$432,488</u>	<u>\$437,706</u>	<u>\$7,407</u>	<u>\$2,189</u>

**Securities Held-to-Maturity:**

	Amortized	Fair	Gross	Gross
	<u>Cost</u>	<u>Value</u>	<u>Unrealized</u>	<u>Unrealized</u>
			<u>Gains</u>	<u>Losses</u>
September 30, 2010:				
State and Municipal Obligations	\$157,106	\$164,070	\$6,980	\$16
Corporate and Other Debt Securities	<u>1,000</u>	<u>1,000</u>	<u>---</u>	<u>---</u>
Total Securities Held-to-Maturity	<u>\$158,106</u>	<u>\$165,070</u>	<u>\$6,980</u>	<u>\$16</u>
December 31, 2009:				
State and Municipal Obligations	\$167,931	\$170,183	\$2,706	\$454
Corporate and Other Debt Securities	<u>1,000</u>	<u>1,000</u>	<u>---</u>	<u>---</u>
Total Securities Held-to-Maturity	<u>\$168,931</u>	<u>\$171,183</u>	<u>\$2,706</u>	<u>\$454</u>

As reported in the Consolidated Balance Sheets, Other Investments include Federal Home Loan Bank of New York (“FHLBNY”) and Federal Reserve Bank (“FRB”) stock, which are reported at cost. FHLBNY and FRB stock are restricted investment securities and amounted to \$8,642 and \$832 at September 30, 2010, respectively and \$8,107 and \$828 at December 31, 2009, respectively. The required level of FHLBNY stock is based on the amount of FHLBNY borrowings and is pledged to secure those borrowings. While some Federal Home Loan Banks have stopped paying dividends and repurchasing stock upon reductions in debt levels, the FHLBNY continues to pay dividends and repurchase its stock. Accordingly, we have not recognized any impairment on our holdings of FHLBNY common stock. However, the FHLBNY has reported impairment issues among its holdings of mortgage-backed securities.

A summary of the maturities of securities as of September 30, 2010 is presented below. Mutual funds and equity securities, which have no stated maturity, are not included in the table below. Collateralized mortgage obligations and other mortgage-backed-securities are included in the schedule based on their expected average lives. Actual maturities will differ from the table below because issuers may have the right to call or prepay obligations with or without prepayment penalties.

<b><u>Maturities of Debt Securities:</u></b>	<b><u>Available-for-Sale</u></b>		<b><u>Held-to-Maturity</u></b>	
	Amortized	Fair	Amortized	Fair
	<u>Cost</u>	<u>Value</u>	<u>Cost</u>	<u>Value</u>
Within One Year:				
U.S. Treasury and Agency Obligations	\$ 103,000	\$ 103,441	\$ ---	\$ ---
State and Municipal Obligations	51,379	51,391	28,553	28,759
Collateralized Mortgage Obligations	15,273	15,335	---	---
Mortgage-Backed Securities –	<u>2,593</u>	<u>2,684</u>	<u>---</u>	<u>---</u>
Residential				
Total	<u>172,245</u>	<u>172,851</u>	<u>28,553</u>	<u>28,759</u>
From 1 - 5 Years:				
U.S. Treasury and Agency Obligations	63,940	64,214	---	---
State and Municipal Obligations	10,122	10,264	50,657	51,896
Collateralized Mortgage Obligations	97,366	101,609	---	---
Mortgage-Backed Securities –	30,352	32,145	---	---
Residential				
Corporate and Other Debt Securities	<u>115</u>	<u>115</u>	<u>---</u>	<u>---</u>
Total	<u>201,895</u>	<u>208,347</u>	<u>50,657</u>	<u>51,896</u>

4. **Investments, Debt and Equity Securities, continued**

<b><u>Maturities of Debt Securities, continued:</u></b>	<b><u>Available-for-Sale</u></b>		<b><u>Held-to-Maturity</u></b>	
	Amortized	Fair	Amortized	Fair
	<u>Cost</u>	<u>Value</u>	<u>Cost</u>	<u>Value</u>
From 5 - 10 Years:				
State and Municipal Obligations	1,584	1,637	65,798	70,645
Collateralized Mortgage Obligations	33,986	37,252	---	---

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Mortgage-Backed Securities – Residential	<u>21,858</u>	<u>22,780</u>	<u>---</u>	<u>---</u>
Total	<u>57,428</u>	<u>61,669</u>	<u>65,798</u>	<u>70,645</u>
Over 10 Years:				
State and Municipal Obligations	2,856	2,856	12,098	12,770
Collateralized Mortgage Obligations	---	---	---	---
Mortgage-Backed Securities – Residential	20,016	20,545	---	---
Corporate and Other Debt Securities	<u>1,382</u>	<u>1,275</u>	<u>1,000</u>	<u>1,000</u>
Total	<u>24,254</u>	<u>24,676</u>	<u>13,098</u>	<u>13,770</u>
Total Debt Securities	<u>\$455,822</u>	<u>\$467,543</u>	<u>\$158,106</u>	<u>\$165,070</u>

The fair value of securities pledged to secure repurchase agreements amounted to \$67,336 and \$72,020 at September 30, 2010 and December 31, 2009, respectively. The fair value of securities pledged to secure public and trust deposits and for other purposes totaled \$418,838 and \$360,885 at September 30, 2010 and December 31, 2009, respectively.

Mortgage-backed securities - residential at September 30, 2010 and December 31, 2009 included \$1,736 and \$2,147, respectively, of loans previously securitized by Arrow, which it continues to service.

**Temporarily Impaired Securities**

September 30, 2010

	<u>Less than 12 Months</u>		<u>12 Months or Longer</u>		<u>Total</u>	
	Fair	Unrealized	Fair	Unrealized	Fair	Unrealized
<b><u>Available-for-Sale Portfolio:</u></b>	<b><u>Value</u></b>	<b><u>Losses</u></b>	<b><u>Value</u></b>	<b><u>Losses</u></b>	<b><u>Value</u></b>	<b><u>Losses</u></b>
State & Municipal Obligations	\$ 7,499	\$ 3	\$ ---	\$ --	\$ 7,499	\$ 3
Collateralized Mortgage Obligations	14,314	67	---	---	14,314	67
Corporate & Other Debt Securities	---	---	1,274	107	1,274	107
Mutual Funds and Equity Securities	<u>1,112</u>	<u>28</u>	<u>42</u>	<u>6</u>	<u>1,154</u>	<u>34</u>
Total Securities Available-for-Sale	<u>\$22,925</u>	<u>\$98</u>	<u>\$1,316</u>	<u>\$113</u>	<u>\$24,241</u>	<u>\$211</u>
<b><u>Held-to-Maturity Portfolio</u></b>						
State & Municipal Obligations	\$---	\$---	\$690	\$16	\$690	\$16

The table above for September 30, 2010 consists of 18 securities where the current fair value is less than the related amortized cost. These unrealized losses do not reflect any significant deterioration of the credit worthiness of the issuing entities. The state and municipal obligations are general obligations supported by the general taxing authority of the issuer, and in some cases are insured. Obligations issued by school districts are supported by state aid. For any non-rated municipal securities, credit analysis shows no significant deterioration in the credit worthiness of the municipalities. CMOs are all agency-backed and rated AAA. Corporate and other debt securities consist of one private placement trust preferred, and one trust preferred pool. The private placement trust preferred is rated AAA by Standard & Poor's; the trust preferred pool is rated investment grade, with the privately issued securities securing the note performing. Subsequent to September 30, 2010, there were no securities downgraded below investment grade.

The unrealized losses on these temporarily impaired securities are primarily the result of changes in interest rates for fixed rate securities where the interest rate received is less than the current rate available for new offerings of similar

securities, changes in market spreads as a result of shifts in supply and demand, and/or changes in the level of prepayments for mortgage related securities. Because we do not currently intend to sell any of our temporarily impaired securities, and because it is more likely-than-not that we would not be required to sell the securities prior to recovery, the impairment is considered temporary.

#### 4. Investments, Debt and Equity Securities, continued

##### Temporarily Impaired Securities

December 31, 2009	<u>Less than 12 Months</u>		<u>12 Months or Longer</u>		<u>Total</u>	
	<u>Fair</u>	<u>Unrealized</u>	<u>Fair</u>	<u>Unrealized</u>	<u>Fair</u>	<u>Unrealized</u>
<u>Available-for-Sale Portfolio:</u>	<u>Value</u>	<u>Losses</u>	<u>Value</u>	<u>Losses</u>	<u>Value</u>	<u>Losses</u>
U.S. Treasury and Agency Securities	\$ 4,998	\$ 3	\$ ---	\$ ---	\$ 4,998	\$ 3
State & Municipal Obligations	1,230	5	---	---	1,230	5
Collateralized Mortgage Obligations	49,034	1,184	162	19	49,196	1,203
Mortgage-Backed Securities - Residential	36,547	836	1,402	2	37,949	838
Corporate & Other Debt Securities	946	54	305	80	1,251	134
Mutual Funds and Equity Securities	<u>20</u>	<u>---</u>	<u>20</u>	<u>6</u>	<u>40</u>	<u>6</u>
Total Securities Available-for-Sale	<u>\$92,775</u>	<u>\$2,082</u>	<u>\$1,889</u>	<u>\$107</u>	<u>\$94,664</u>	<u>\$2,189</u>
<u>Held-to-Maturity Portfolio</u>						
State & Municipal Obligations	\$14,270	\$270	\$6,624	\$184	\$20,894	\$454

The table above for December 31, 2009 consists of 103 securities where the current fair value is less than the related amortized cost. These unrealized losses do not reflect any significant deterioration of the credit worthiness of the issuing entities. The state and municipal obligations are general obligations supported by the general taxing authority of the issuer, and in some cases are insured. Obligations issued by school districts are supported by state aid. For any non-rated municipal securities, third party credit analysis shows no significant deterioration in the credit worthiness of the municipalities. CMOs are all agency-backed and are rated AAA, as are the mortgage-backed securities. Corporate and other debt securities consist of one private placement trust preferred, and one trust preferred pool. The private placement trust preferred is rated AAA by Standard & Poor's; the trust preferred pool is rated investment grade, with the privately issued securities securing the note performing. Subsequent to December 31, 2009, there were no securities downgraded below investment grade.

The unrealized losses on these temporarily impaired securities are primarily the result of changes in interest rates for fixed rate securities where the interest rate received is less than the current rate available for new offerings of similar securities, changes in market spreads as a result of shifts in supply and demand, and/or changes in the level of prepayments for mortgage related securities. Because we do not currently intend to sell any of our temporarily impaired securities, and because it is not more likely-than-not we would be required to sell the securities prior to recovery, the impairment is considered temporary.

##### Other-Than-Temporary Impairment

On a quarterly basis, Arrow performs an assessment to determine whether there have been any events or economic circumstances indicating that a security with an unrealized loss has suffered other-than-temporary impairment. A debt security is considered impaired if the fair value is less than its amortized cost basis at the reporting date. If impaired, Arrow then assesses whether the unrealized loss is other-than-temporary. An unrealized loss on a debt security is generally deemed to be other-than-temporary and a credit loss is deemed to exist if the present value of the expected future cash flows is less than the amortized cost basis of the debt security. As a result, the credit loss component of an other-than-temporary impairment write-down for debt securities is recorded in earnings while the remaining portion of the impairment loss is recognized, net of tax, in other comprehensive income provided that Arrow does not intend to sell the underlying debt security and it is more-likely-than not that Arrow would not be required to sell the debt security prior to recovery.

At September 30, 2010 and December 31, 2009 mutual funds and equity securities included shares of one common stock that had been deemed to be other-than-temporarily impaired. The common stock had a book value of \$1,469 prior to the recognition of \$375 in losses charged to earnings for the year ended December 31, 2009. The approximate fair value for this security was \$1,067 and \$1,094 at September 30, 2010 and December 31, 2009, respectively.

#### 5. Retirement Plans (In Thousands)

The following table provides the components of net periodic benefit costs for the three months ended September 30:

	Pension		Postretirement	
	Benefits		Benefits	
	<u>2010</u>	<u>2009</u>	<u>2010</u>	<u>2009</u>
Service Cost	\$282	\$264	\$ 36	\$39
Interest Cost	438	446	114	96
Expected Return on Plan Assets	(522)	(514)	---	---
Amortization of Prior Service Credit	(22)	(19)	(24)	(27)
Amortization of Net Loss	<u>233</u>	<u>323</u>	<u>17</u>	<u>24</u>
Net Periodic Benefit Cost	<u>\$409</u>	<u>\$500</u>	<u>\$143</u>	<u>\$132</u>

The following table provides the components of net periodic benefit costs for the nine months ended September 30:

	Pension		Postretirement	
	Benefits		Benefits	
	<u>2010</u>	<u>2009</u>	<u>2010</u>	<u>2009</u>
Service Cost	\$ 846	\$ 792	\$108	\$115
Interest Cost	1,314	1,340	338	291
Expected Return on Plan Assets	(1,576)	(1,544)	---	---

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Amortization of Prior Service Credit	(60)	(57)	(72)	(81)
Amortization of Net Loss	<u>703</u>	<u>969</u>	<u>51</u>	<u>72</u>
Net Periodic Benefit Cost	<u>\$1,227</u>	<u>\$1,500</u>	<u>\$425</u>	<u>\$397</u>

We are not required to make any contribution to our qualified pension plan in 2010 and therefore, do not expect to make any contribution during 2010. The expected 2010 contribution for the nonqualified plan is \$318. Arrow makes contributions for its postretirement benefits in an amount equal to actual expenses for the year. The expected contribution is estimated to be \$326 for 2010.

6. Stock-Based Compensation Plans (Dollars In Thousands)

Under our 2008 Long-Term Incentive Plan, we granted options in both the first quarters of 2010 and 2009 to purchase shares of our common stock. The fair values of the options were estimated on the date of grant using the Black-Scholes option-pricing model. The fair value of our grants is expensed over the four year vesting period. The expense for the second quarter of 2010 and 2009 was \$79 and \$49, respectively. The expense for the first nine months of 2010 and 2009 was \$226 and \$139, respectively. Other information on the options issued during 2010 and 2009 is presented in the following table:

Grants Issued During the First Quarter:	<u>2010</u>	<u>2009</u>
Shares Granted	73,336	73,403
Fair Value of Options Granted	\$6.43	\$4.35
Assumptions:		
Dividend Yield	3.80%	4.70%
Expected Volatility	35.3%	33.2%
Risk Free Interest Rate	3.14%	2.10%
Expected Lives (in years)	7.79	7.78

6. Stock-Based Compensation Plans, continued

The following table presents the activity in Arrow's compensatory stock options for the first nine months of 2010 and 2009 and has been restated for the September 2010 3% stock dividend:

	<u>2010</u>	<u>2009</u>
	Weighted-	Weighted-
	Average	Average
	Exercise	Exercise

Options:	<u>Shares</u>	<u>Price</u>	<u>Shares</u>	<u>Price</u>
Outstanding at January 1	452,494	\$21.70	460,999	\$20.57
Granted	73,336	23.86	74,463	21.36
Exercised	(27,315)	11.69	(61,675)	14.11
Forfeited	---	---	<u>(1,084)</u>	22.56
Outstanding at September 30	<u>498,515</u>	22.56	<u>472,703</u>	21.53
Exercisable at September 30	334,615	22.62	340,150	21.60

Arrow also sponsors an Employee Stock Purchase Plan under which employees purchase Arrow's common stock at a 5% discount below market price. Under current accounting guidance, a stock purchase plan with a discount of 5% or less is not considered a compensatory plan.

## 7. Guarantees

We do not issue any guarantees that would require liability-recognition or disclosure, other than standby letters of credit. Standby and other letters of credit are conditional commitments that are issued to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support public and private borrowing arrangements, including bond financing and similar transactions. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. Typically, these instruments have terms of twelve months or less. Some expire unused, and therefore, the total amounts do not necessarily represent future cash requirements. Some have automatic renewal provisions.

For letters of credit, the amount of the collateral obtained, if any, is based on management's credit evaluation of the counter-party. We had approximately \$17.7 million of standby letters of credit on September 30, 2010, most of which will expire within one year and some of which were not collateralized. At that date, all the letters of credit were for private borrowing arrangements. The fair value of our standby letters of credit at September 30, 2010 was insignificant.

## 8. Fair Value Measurements and Disclosures (In Thousands)

Current accounting guidance defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles (GAAP) and requires certain disclosures about fair value measurements. We do not have any nonfinancial assets or liabilities measured at fair value. The only assets or liabilities that Arrow measured at fair value on a recurring basis at September 30, 2010 and December 31, 2009 were securities available-for-sale. Arrow held no securities or liabilities for trading on such date. The fair value measurement of securities available-for-sale on such date was as follows:

### 8. Fair Value Measurements and Disclosures, continued

Fair Value Measurements at Reporting Date Using:  
Quoted Prices

<u>Description</u>	<u>Total</u>	Significant Other		
		In Active Markets for Identical Assets	Observable Inputs	Significant Unobservable Inputs
	<u>(Level 1)</u>	<u>(Level 2)</u>	<u>(Level 3)</u>	
September 30, 2010:				
Securities Available-for Sale:				
U.S. Treasury and Agency Obligations	\$167,655	\$---	\$167,655	\$ ---
State and Municipal Obligations	66,148	---	66,148	---
Collateralized Mortgage Obligations	154,196	---	154,196	---
Mortgage-Backed Securities - Residential	78,154	---	78,154	---
Corporate and Other Debt Securities	1,390	---	1,063	327
Mutual Funds and Equity Securities	<u>1,398</u>	<u>---</u>	<u>1,398</u>	<u>---</u>
Total Securities Available-for-Sale	<u>\$468,941</u>	<u>\$---</u>	<u>\$468,614</u>	<u>\$327</u>
December 31, 2009:				
Securities Available-for Sale:				
U.S. Treasury and Agency Obligations	\$123,331	\$---	\$123,331	\$ ---
State and Municipal Obligations	18,913	---	18,913	---
Collateralized Mortgage Obligations	199,781	---	199,781	---
Mortgage-Backed Securities - Residential	93,017	---	93,017	---
Corporate and Other Debt Securities	1,331	---	1,026	305
Mutual Funds and Equity Securities	<u>1,333</u>	<u>---</u>	<u>1,333</u>	<u>---</u>
Total Securities Available-for-Sale	<u>\$437,706</u>	<u>\$---</u>	<u>\$437,401</u>	<u>\$305</u>

Fair value for securities available-for-sale was determined utilizing an independent bond pricing service for identical assets or significantly similar securities. The pricing service uses a variety of techniques to arrive at fair value including market maker bids, quotes and pricing models. Inputs to the pricing models include recent trades, benchmark interest rates, spreads and actual and projected cash flows. There were no assets or liabilities measured at fair value on a nonrecurring basis at September 30, 2010 or December 31, 2009.

Level 3 securities available-for-sale at September 30, 2010 and December 31, 2009, in the table above, included one trust preferred pooled security. In our analysis of fair value, we determined that the market for this security was inactive. We reviewed the collateral within the pool and performed a discounted cash flow analysis using additional value estimates from unobservable inputs including expected cash flows after estimated deferrals and defaults. The discount rate used was based on a market based rate of return including an assumed risk premium for securities with similar credit characteristics plus a market price adjustment for the small size and lack of an established market for this type of security.

The following table is a reconciliation of the beginning and ending balances for September 30, 2010 and 2009 of the Level 3 assets of Arrow, i.e., as to which fair value is measured using significant unobservable inputs, all of which are securities available-for-sale:

	<u>2010</u>	<u>2009</u>
Beginning Balance, January 1	\$305	\$555
Transfers In	---	---
Principal payment received	(3)	(19)
Purchases, issuances and settlements	---	(340)
Total net losses (realized/unrealized):		
Included in earnings	---	(60)
Included in earnings, as a result of other-than-temporary impairment	---	---
Included in other comprehensive income	<u>25</u>	<u>157</u>
Ending Balance, September 30	<u>\$327</u>	<u>\$293</u>
The amount of total losses for the year included in earnings attributable to the change in unrealized gains or losses relating to assets still held at period-end, as a result of other-than-temporary impairment	<u>\$---</u>	<u>\$---</u>

#### 8. Fair Value Measurements and Disclosures, continued

There were no assets or liabilities that Arrow measured at fair value on a nonrecurring basis on September 30, 2010 or on December 31, 2009. Other impaired assets which might have been included in this table include other real estate owned, mortgage servicing rights, goodwill and other intangible assets. Arrow evaluates each of these assets for impairment on a quarterly basis, with no impairment recognized for these assets during the periods ended September 30, 2010 or December 31, 2009.

The following table presents a summary at September 30, 2010 and December 31, 2009 of the carrying amount and fair value of Arrow's financial instruments:

	<u>September 30, 2010</u>		<u>December 31, 2009</u>	
	Carrying	Fair	Carrying	Fair
	<u>Amount</u>	<u>Value</u>	<u>Amount</u>	<u>Value</u>
Interest-Bearing Deposits at Banks	\$ 83,122	\$ 83,122	\$ 22,730	\$ 22,730
Securities Available-for-Sale	468,941	468,941	437,706	437,706
Securities Held-to-Maturity	158,106	165,070	168,931	171,183
Other Investments	9,474	9,474	8,935	8,935
Net Loans	1,140,047	1,171,251	1,098,136	1,115,414
Non-maturity Deposits	1,164,110	1,164,110	1,050,565	1,050,565
Time Deposits	382,485	394,025	393,001	400,421
FHLBNY Advances	150,000	156,316	140,000	147,754
Junior Subordinated Obligations Issued to				
Unconsolidated Subsidiary Trusts	20,000	20,000	20,000	20,000
Accrued Interest Receivable	6,959	6,959	7,115	7,115
Accrued Interest Payable	2,122	2,122	2,257	2,257

Fair value for securities held-to-maturity was determined utilizing an independent bond pricing service for identical assets or significantly similar securities. The pricing service uses a variety of techniques to arrive at fair value including market maker bids, quotes and pricing models. Inputs to the pricing models include recent trades, benchmark interest rates, spreads and actual and projected cash flows.

Fair values for loans are estimated for portfolios of loans with similar financial characteristics. Loans are segregated by type such as commercial, commercial real estate, residential mortgage, indirect and other consumer loans. Each loan category is further segmented into fixed and adjustable interest rate terms and by performing and nonperforming categories. The fair value of performing loans is calculated by discounting scheduled cash flows through the estimated maturity using estimated market discount rates that reflect the credit and interest rate risk inherent in the loan. The estimate of maturity is based on historical experience with repayments for each loan classification, modified, as required, by an estimate of the effect of current economic and lending conditions. Fair value for nonperforming loans is generally based on recent external appraisals. If appraisals are not available, estimated cash flows are discounted using a rate commensurate with the risk associated with the estimated cash flows. Assumptions regarding credit risk, cash flows and discount rates are judgmentally determined using available market information and specific borrower information.

The fair value of time deposits is based on the discounted value of contractual cash flows, except that the fair value is limited to the extent that the customer could redeem the certificate after imposition of a premature withdrawal penalty. The discount rates are estimated using the FHLB NY yield curve, which is considered representative of Arrow's time deposit rates. The fair value of FHLB NY advances is estimated based on the discounted value of contractual cash flows. The discount rate is estimated using current rates on FHLB NY advances with similar maturities and call features.

Based on Arrow's capital adequacy, the book value of the outstanding trust preferred securities (Junior Subordinated Obligations Issued to Unconsolidated Subsidiary Trusts) are considered to approximate fair value since the interest rates are variable (indexed to three-month LIBOR) and Arrow is well-capitalized.

#### 9. Business Combinations (In Thousands)

On April 1, 2010, we acquired Loomis & LaPann, Inc., a property and casualty insurance agency ("Loomis"). Loomis will be operated as a wholly-owned subsidiary of our lead bank, Glens Falls National Bank and Trust Company. All the outstanding shares of Loomis were acquired in exchange for shares of Arrow common stock. We recorded the following intangible assets as a result of the acquisition (none of which are deductible for income tax purposes): goodwill of \$514 thousand and expirations of \$126 thousand. The value of the expirations is being amortized over twenty years. Under the acquisition agreement, we issued 26,296 shares of Arrow's common stock at closing and an additional 731 shares on May 27, 2010 in connection with a balance sheet adjustment to the purchase price as provided for in the acquisition agreement. The acquisition agreement also provides for annual contingent future payments of Arrow common stock based upon the financial performance and other results of Loomis over a three-year

period. The minimum contingent payment is zero and the maximum contingent payment over the entire three-year period is \$330 thousand payable solely in shares of the Company's common stock valued in accordance with the acquisition agreement.

### **Report of Independent Registered Public Accounting Firm**

The Board of Directors and Stockholders

Arrow Financial Corporation:

We have reviewed the consolidated balance sheet of Arrow Financial Corporation and subsidiaries (the Company) as of September 30, 2010, the related consolidated statements of income for the three and nine month periods ended September 30, 2010 and 2009 and the related consolidated statements of changes in stockholders' equity, and cash flows for the nine-month periods ended September 30, 2010 and 2009. These consolidated financial statements are the responsibility of the Company's management.

We conducted our reviews in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to the consolidated financial statements referred to above for them to be in conformity with U.S. generally accepted accounting principles.

We have previously audited, in accordance with standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of Arrow Financial Corporation and subsidiaries as of December 31, 2009, and the related consolidated statements of income, changes in stockholders' equity and cash flows for the year then ended (not presented herein); and in our report dated March 4, 2010, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying consolidated balance sheet as of December 31, 2009, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

Albany, New York

November 5, 2010

Item 2.

**ARROW FINANCIAL CORPORATION AND SUBSIDIARIES**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS OF**  
**FINANCIAL CONDITION AND RESULTS OF OPERATIONS**  
**SEPTEMBER 30, 2010**

**Note on Terminology** - In this Quarterly Report on Form 10-Q, the terms “Arrow,” “the registrant,” “the company,” “we,” “us,” and “our” generally refer to Arrow Financial Corporation and its subsidiaries as a group, except where the context indicates otherwise. Arrow is a two-bank holding company headquartered in Glens Falls, New York. Our banking subsidiaries are Glens Falls National Bank and Trust Company (Glens Falls National) whose main office is located in Glens Falls, New York, and Saratoga National Bank and Trust Company (Saratoga National) whose main office is located in Saratoga Springs, New York. Our non-bank subsidiaries include Capital Financial Group, Inc. (an insurance agency specializing in selling and servicing group health care policies), Loomis & LaPann, Inc. (a property and casualty insurance agency), North Country Investment Advisers, Inc. (a registered investment adviser that provides investment advice to our proprietary mutual funds) and Arrow Properties, Inc. (a real estate investment trust, or REIT), all of which are subsidiaries of Glens Falls National.

At certain points in this Report, our performance is compared with that of our “peer group” of financial institutions. Unless otherwise specifically stated, this peer group is comprised of the group of 303 domestic bank holding companies with \$1 to \$3 billion in total consolidated assets as identified in the Federal Reserve Board’s “Bank Holding Company Performance Report” for June 30, 2010 (the most recent such Report currently available), and peer group data has been derived from such Report.

**Forward Looking Statements** - The information contained in this Quarterly Report on Form 10-Q contains statements that are not historical in nature but rather are based on our beliefs, assumptions, expectations, estimates and projections about the future. These statements are “forward-looking statements” within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, and involve a degree of uncertainty and attendant risk. Words such as “expects,” “believes,” “anticipates,” “estimates” and variations of such words and similar expressions are intended to

identify such forward-looking statements. Some of these statements, such as those included in the interest rate sensitivity analysis in Item 3, entitled “Quantitative and Qualitative Disclosures About Market Risk,” are merely presentations of what future performance or changes in future performance would look like based on hypothetical assumptions and on simulation models. Other forward-looking statements are based on our general perceptions of market conditions and trends in business activity, both our own and in the banking industry generally, as well as current management strategies for future operations and development. Examples of forward-looking statements in this Report are referenced in the table below:

<b><u>Topic</u></b>	<b><u>Page</u></b>	<b><u>Location</u></b>
Estimation of potential losses related to Visa obligation	26	3 <sup>rd</sup> paragraph
Impact of Financial Turmoil	24	6 <sup>th</sup> paragraph
Impact of market rate structure on net interest margin, loan yields and deposit rates	28	1 <sup>st</sup> and 6 <sup>th</sup> paragraphs
	30	3 <sup>rd</sup> paragraph
	33	Last 3 paragraphs
Provision for loan losses	35	Last paragraph
Future level of residential real estate loans	32	2 <sup>nd</sup> paragraph
Future level of indirect consumer loans	32	Last paragraph
Future level of commercial loans	33	1 <sup>st</sup> paragraph
Impact of changing economy	38	1 <sup>st</sup> paragraph
Impact of changing capital standards and legislative developments	25	5 <sup>th</sup> paragraph
	27	2 <sup>nd</sup> paragraph
	38	5 <sup>th</sup> paragraph
Liquidity	40	5 <sup>th</sup> paragraph
Fees for other services to customers	43	1 <sup>st</sup> paragraph
	46	5 <sup>th</sup> paragraph
Interchange Fee Income	42	Last paragraph
Insurance commissions	43	2 <sup>nd</sup> paragraph
	47	1 <sup>st</sup> paragraph

These statements are not guarantees of future performance and involve certain risks and uncertainties that are difficult to quantify or, in some cases, to identify. In the case of all forward-looking statements, actual outcomes and results may differ materially from what the statements predict or forecast. Factors that could cause or contribute to such differences include, but are not limited to:

(a)

rapid and dramatic changes in economic and market conditions, such as the U.S. economy has recently experienced and continues to experience;

(b)

sharp fluctuations in interest rates, economic activity, and consumer spending patterns;

(c)

sudden changes in the market for products we provide, such as real estate loans;

(d)

significant new banking laws and regulations, as are presently anticipated or, as a result of the Dodd-Frank Act Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act");

(e)

enhanced competition from unforeseen sources; and

(f)

similar uncertainties inherent in banking operations or business generally.

In the current environment of substantial economic turmoil affecting all sectors of business in the U.S., including the financial sector, all forward-looking statements should be understood as embracing a substantial degree of uncertainty far exceeding that accompanying such statements under normal economic conditions.

*Readers are cautioned not to place undue reliance on forward-looking statements in this Report, which speak only as of the date hereof.* We undertake no obligation to revise or update these forward-looking statements to reflect the occurrence of unanticipated events. This Report should be read in conjunction with our Annual Report on Form 10-K for December 31, 2009 and our other filings with the Securities and Exchange Commission.

## USE OF NON-GAAP FINANCIAL MEASURES

The Securities and Exchange Commission (SEC) has adopted Regulation G, which applies to all public disclosures, including earnings releases, made by registered companies that contain "non-GAAP financial measures." GAAP is generally accepted accounting principles in the United States of America. Under Regulation G, companies making public disclosures containing non-GAAP financial measures must also disclose, along with each non-GAAP financial measure, certain additional information, including a reconciliation of the non-GAAP financial measure to the closest comparable GAAP financial measure and a statement of the Company's reasons for utilizing the non-GAAP financial measure as part of its financial disclosures. The SEC has exempted from the definition of "non-GAAP financial measures" certain commonly used financial measures that are not based on GAAP. When these exempted measures are included in public disclosures, supplemental information is not required. The following measures used in this Report, which are commonly utilized by financial institutions, have not been specifically exempted by the SEC and may constitute "non-GAAP financial measures" within the meaning of the SEC's new rules, although we are unable to state with certainty that the SEC would so regard them.

**Tax-Equivalent Net Interest Income and Net Interest Margin:** Net interest income, as a component of the tabular presentation by financial institutions of Selected Financial Information regarding their recently completed operations, is commonly presented on a tax-equivalent basis. That is, to the extent that some component of the institution's net interest income, which is presented on a before-tax basis, is exempt from taxation (e.g., is received by the institution as a result of its holdings of state or municipal obligations), an amount equal to the tax benefit derived from that component is added back to the net interest income total. This adjustment is considered helpful in comparing one

financial institution's net interest income to that of another institution or in analyzing any institution's net interest income trend line over time, to correct any analytical distortion that might otherwise arise from the fact that financial institutions vary widely in the proportions of their portfolios that are invested in tax-exempt securities, and that even a single institution may significantly alter the proportion of its own portfolio that is invested in tax-exempt obligations.

Moreover, net interest income is itself a component of a second financial measure commonly used by financial institutions, net interest margin, which is the ratio of net interest income to average earning assets. For purposes of this measure as well, tax-equivalent net interest income is generally used by financial institutions, again to provide a better basis of comparison from institution to institution and to better demonstrate a single institution's performance over time. We follow these practices.

**The Efficiency Ratio:** Financial institutions often use an "efficiency ratio" as a measure of expense control. The efficiency ratio typically is defined as the ratio of noninterest expense to net interest income and noninterest income. Net interest income as utilized in calculating the efficiency ratio is typically expressed on a tax-equivalent basis. Moreover, most financial institutions, in calculating the efficiency ratio, also adjust both noninterest expense and noninterest income to exclude from these items (as calculated under GAAP) certain recurring component elements of income and expense, such as intangible asset amortization (deducted from noninterest expense) and securities gains or losses (excluded from noninterest income). We follow these practices.

**Tangible Book Value per Share:** Tangible equity is total stockholders' equity less intangible assets. Tangible book value per share is tangible equity divided by total shares issued and outstanding. Tangible book value per share is often regarded as a more meaningful comparative ratio than book value per share as calculated under GAAP, that is, total stockholders' equity including intangible assets divided by total shares issued and outstanding. Intangible assets as a category of assets includes many items, but is essentially represented by goodwill for Arrow.

**Adjustments for Certain Items of Income or Expense:** In addition to our disclosures of net income, earnings per share, return on average assets, return on average equity and other financial measures in accordance with GAAP, we may also provide comparative disclosures that adjust these GAAP financial measures for certain material items of income or expense. We believe that these non-GAAP financial measures may be helpful in understanding the results of operations separate and apart from items that may, or could, have a disproportional positive or negative impact on any particular period. Additionally, we believe that the adjustment for certain items allows a better comparison from period to period in our results of operations with respect to our fundamental lines of business including the commercial banking business.

We believe that the non-GAAP financial measures disclosed by us from time to time are useful in evaluating our performance and that such information should be considered as supplemental in nature and not as a substitute for or superior to the related financial information prepared in accordance with GAAP. Our non-GAAP financial measures may differ from similar measures presented by other companies.

### Selected Quarterly Information:

(In Thousands, Except Per Share Amounts)

(Share and per share amounts have been restated for the September 2010 3% stock dividend)

	<u>Sep 2010</u>	<u>Jun 2010</u>	<u>Mar 2010</u>	<u>Dec 2009</u>	<u>Sep 2009</u>
Net Income	\$5,575	\$5,714	\$5,415	\$5,117	\$5,062

Transactions Recorded in Net Income(Net of Tax):

Other-Than-Temporary Impairment (OTTI) <sup>1</sup>	\$---	\$---	\$---	\$(227)	\$---
Net Securities Gains	373	530	---	17	29
Net Gains on Sales of Loans	285	21	13	56	10
Period End Shares Outstanding	11,234	11,300	11,277	11,245	11,244
Basic Average Shares Outstanding	11,257	11,307	11,260	11,238	11,239
Diluted Average Shares Outstanding	11,260	11,344	11,301	11,288	11,312
Basic Earnings Per Share	\$.50	\$.51	\$.48	\$.46	\$.45
Diluted Earnings Per Share	.50	.50	.48	.45	.45
Cash Dividends Per Share	.24	.24	.24	.24	.24

Average Assets	\$1,880,099	\$1,873,690	\$1,844,173	\$1,856,176	\$1,778,893
Average Equity	153,653	149,026	144,001	140,786	136,397
Return on Average Assets	1.18%	1.22%	1.19%	1.09%	1.13%
Return on Average Equity	14.39	15.38	15.25	14.42	14.72

Average Earning Assets	\$1,792,421	\$1,790,572	\$1,762,490	\$1,781,464	\$1,706,626
Average Interest-Bearing Liabilities	1,485,639	1,502,052	1,483,532	1,492,326	1,417,218
Interest Income, Tax-Equivalent <sup>2</sup>	21,829	22,530	22,512	23,032	22,499
Interest Expense	5,829	6,023	5,940	6,522	6,462
Net Interest Income, Tax-Equivalent <sup>2</sup>	16,000	16,507	16,572	16,510	16,037
Tax-Equivalent Adjustment	832	852	861	863	835
<b>Net Interest Margin <sup>2</sup></b>	<b>3.54%</b>	<b>3.70%</b>	<b>3.81%</b>	<b>3.68%</b>	<b>3.73%</b>

Efficiency Ratio Calculation: <sup>2</sup>

Noninterest Expense	\$12,106	\$12,002	\$11,540	\$11,699	\$11,401
Less: Intangible Asset Amortization	(67)	(65)	(73)	(77)	(79)
Net Noninterest Expense	<u>\$12,039</u>	<u>\$11,937</u>	<u>\$11,467</u>	<u>\$11,622</u>	<u>\$11,322</u>
Net Interest Income, Tax-Equivalent <sup>2</sup>	\$16,000	\$16,507	\$16,572	\$16,510	\$16,037
Noninterest Income	5,305	5,028	4,018	3,805	3,976
Less: Net Securities Losses (Gains) & OTTI	(618)	(878)	---	347	(48)
Net Gross Income	<u>\$20,687</u>	<u>\$20,657</u>	<u>\$20,590</u>	<u>\$20,662</u>	<u>\$19,965</u>
Efficiency Ratio <sup>2</sup>	58.20%	57.79%	55.69%	56.25%	56.71%

Period-End Capital Information:

Tier 1 Leverage Ratio	8.41%	8.71%	8.66%	8.43%	8.37%
Total Stockholders' Equity (i.e. Book Value)	\$153,457	\$152,703	\$145,804	\$140,818	\$139,304
Book Value per Share	13.66	13.51	12.93	12.52	12.39
Intangible Assets	17,209	17,206	16,630	16,712	16,353
Tangible Book Value per Share <sup>2</sup>	12.13	11.99	11.46	11.04	10.93

Asset Quality Information

Net Loans Charged-off as a

Percentage of Average Loans, Annualized	.05%	.05%	.08%	.09%	.08%
Provision for Loan Losses as a	.13	.13	.14	.16	.15

Percentage of Average Loans,  
Annualized  
Allowance for Loan Losses as a

Percentage of Loans, Period-end Allowance for Loan Losses as a	1.27	1.26	1.27	1.26	1.25
---	------	------	------	------	------

Percentage of Nonperforming Loans,  
Period-end  
Nonperforming Loans as a

Percentage of Nonperforming Loans, Period-end Nonperforming Loans as a	369.69	324.13	393.43	300.73	299.07
--	--------	--------	--------	--------	--------

Percentage of Loans, Period-end  
Nonperforming Assets as a

Percentage of Loans, Period-end Nonperforming Assets as a	.34	.39	.32	.42	.42
--	-----	-----	-----	-----	-----

Percentage of Total Assets, Period-end

Percentage of Total Assets, Period-end	.20	.24	.20	.26	.26
--	-----	-----	-----	-----	-----

<sup>1</sup> See page 26

<sup>2</sup> See "Use of Non-GAAP Financial Measures" on page 19.

### **Selected Nine-month Period Information:**

(Dollars In Thousands, Except Per Share Amounts)

(Share and per share amounts have been restated for the September 2010 3% stock dividend)

	<u>Sep 2010</u>	<u>Sep 2009</u>
Net Income	\$16,704	\$16,675
<b><u>Transactions Recorded in Net Income (Net of Tax):</u></b>		
Net Gain on Sale of Merchant Bank Card Processing see page 26	\$ ---	\$1,791
Income from Restitution Payment see page 46	---	271
FDIC Special Assessment see page 27	---	(475)
Net Securities Gains see page 34-35	903	199
Net Gain on Sales of Loans see page 42, 46	318	197
Period-End Shares Outstanding	11,234	11,244
Basic Average Shares Outstanding	11,275	11,229
Diluted Average Shares Outstanding	11,302	11,280
Basic Earnings Per Share	\$1.48	\$1.48
Diluted Earnings Per Share	1.48	1.48
Cash Dividends	.73	.71
Average Assets	\$1,866,119	\$1,728,934
Average Equity	148,929	132,903
Return on Average Assets	1.20%	1.29%
Return on Average Equity	15.00	16.77
Average Earning Assets	\$1,781,936	\$1,657,111
Average Interest-Bearing Liabilities	1,490,415	1,382,287
Interest Income, Tax-equivalent <sup>1</sup>	66,871	67,006

Interest Expense	17,792	19,970
Net Interest Income, Tax-equivalent <sup>1</sup>	49,079	47,036
Tax-equivalent Adjustment	2,545	2,318
Net Interest Margin <sup>1</sup>	3.68%	3.79%

Efficiency Ratio Calculation <sup>1</sup>

Noninterest Expense	\$35,648	\$34,893
Less: Intangible Asset Amortization	<u>(205)</u>	<u>(247)</u>
Net Noninterest Expense	<u>35,443</u>	<u>34,646</u>
Net Interest Income, Tax-equivalent <sup>1</sup>	49,079	47,036
Noninterest Income	14,351	15,787
Less: Net Securities Gains	<u>(1,496)</u>	<u>(329)</u>
Net Gross Income, Adjusted	<u>61,934</u>	<u>62,494</u>
Efficiency Ratio <sup>1</sup>	57.23%	55.44%

Period-End Capital Information:

Tier 1 Leverage Ratio	8.41%	8.37%
Total Stockholders' Equity (i.e. Book Value)	\$153,457	\$139,304
Book Value per Share	13.66	12.39
Intangible Assets	17,209	16,353
Tangible Book Value per Share <sup>1</sup>	12.13	10.93

Asset Quality Information:

Net Loans Charged-off as a		
Percentage of Average Loans, Annualized Provision for Loan Losses as a	.06%	.09%
Percentage of Average Loans, Annualized Allowance for Loan Losses as a	.13	.16
Percentage of Period-end Loans Allowance for Loan Losses as a	1.27	1.25
Percentage of Nonperforming Loans Nonperforming Loans as a	369.69	299.07
Percentage of Period-end Loans Nonperforming Assets as a	.34	.42
Percentage of Period-end Total Assets	.20	.26

<sup>1</sup> See "Use of Non-GAAP Financial Measures" on page 19.

**Average Consolidated Balance Sheets and Net Interest Income Analysis**

(see "Use of Non-GAAP Financial Measures" on page 19)

(Tax-equivalent Basis using a marginal tax rate of 35%)

(Dollars In Thousands)

<b><u>Quarter Ended September 30,</u></b>	<b><u>2010</u></b>			<b><u>2009</u></b>		
	Average <u>Balance</u>	Interest Income/ <u>Expense</u>	Rate Earned/ <u>Paid</u>	Average <u>Balance</u>	Interest Income/ <u>Expense</u>	Rate Earned/ <u>Paid</u>
Interest-Bearing Bank Deposits	\$ 49,487	\$ 33	0.26%	\$ 62,301	\$ 41	0.26%
Investment Securities:						
Taxable	406,360	3,495	3.41	367,254	3,541	3.83
Non-Taxable	188,378	2,146	4.52	177,250	2,204	4.93
Loans	<u>1,148,196</u>	<u>16,155</u>	5.58	<u>1,099,821</u>	<u>16,713</u>	6.03
Total Earning Assets	1,792,421	<u>21,829</u>	4.83	1,706,626	<u>22,499</u>	5.23
Allowance For Loan Losses	(14,503)			(13,721)		
Cash and Due From Banks	29,785			28,208		
Other Assets	<u>72,396</u>			<u>57,780</u>		
Total Assets	<u>\$1,880,099</u>			<u>\$1,778,893</u>		
Deposits:						
Interest-Bearing NOW Deposits	\$ 497,981	1,216	0.97	\$ 443,841	1,144	1.02
Regular and Money Market Savings	368,565	523	0.56	310,991	503	0.64
Time Deposits of \$100,000 or More	130,471	737	2.24	167,681	925	2.19
Other Time Deposits	<u>252,507</u>	<u>1,482</u>	2.33	<u>253,359</u>	<u>1,830</u>	2.87
Total Interest-Bearing Deposits	1,249,524	3,958	1.26	1,175,872	4,402	1.49
Short-Term Borrowings	66,115	33	0.20	61,346	30	0.19
Long-Term Debt	<u>170,000</u>	<u>1,838</u>	4.29	<u>180,000</u>	<u>2,030</u>	4.47
Total Interest-Bearing Liabilities	1,485,639	<u>5,829</u>	1.56	1,417,218	<u>6,462</u>	1.81
Demand Deposits	217,017			199,611		
Other Liabilities	<u>23,790</u>			<u>25,667</u>		
Total Liabilities	1,726,446			1,642,496		
Stockholders' Equity	<u>153,653</u>			<u>136,397</u>		
Total Liabilities and Stockholders' Equity	<u>\$1,880,099</u>			<u>\$1,778,893</u>		
Net Interest Income (Tax-equivalent Basis)		16,000			16,037	
Net Interest Spread			3.27			3.42
Net Interest Margin			3.54			3.73
Reversal of Tax-equivalent Adjustment		<u>(832)</u>	(.18)		<u>(835)</u>	(.19)
Net Interest Income, As Reported		<u>\$15,168</u>			<u>\$15,202</u>	

**Average Consolidated Balance Sheets and Net Interest Income Analysis**

(see "Use of Non-GAAP Financial Measures" on page 19)

(Tax-equivalent Basis using a marginal tax rate of 35%)

(Dollars In Thousands)

<b><u>Nine Months Ended September 30,</u></b>	<b><u>2010</u></b>			<b><u>2009</u></b>		
	Average	Interest	Rate	Average	Interest	Rate
	<u>Balance</u>	<u>Income/ Expense</u>	<u>Earned/ Paid</u>	<u>Balance</u>	<u>Income/ Expense</u>	<u>Earned/ Paid</u>
Interest-bearing Balances	\$ 54,213	\$ 107	0.26%	\$ 55,929	\$ 110	0.26%
Investment Securities:						
Taxable	410,822	11,370	3.70	340,784	10,659	4.18
Non-Taxable	186,621	6,659	4.77	161,245	6,146	5.10
Loans	<u>1,130,280</u>	<u>48,735</u>	5.76	<u>1,099,153</u>	<u>50,091</u>	6.09
Total Earning Assets	1,781,936	<u>66,871</u>	5.02	1,657,111	<u>67,006</u>	5.41
Allowance For Loan Losses	(14,289)			(13,523)		
Cash and Due From Banks	28,671			28,034		
Other Assets	<u>69,801</u>			<u>57,312</u>		
Total Assets	<u>\$1,866,119</u>			<u>\$1,728,934</u>		
Deposits:						
Interest-Bearing NOW Deposits	\$ 519,322	4,093	1.05	\$ 439,854	3,674	1.12
Regular and Money Market Savings	357,006	1,633	0.61	299,629	1,564	0.70
Time Deposits of \$100,000 or More	136,967	2,180	2.13	155,308	2,898	2.49
Other Time Deposits	<u>249,098</u>	<u>4,448</u>	2.39	<u>249,953</u>	<u>5,634</u>	3.01
Total Interest-Bearing Deposits	1,262,393	12,354	1.31	1,144,744	13,770	1.61
Short-Term Borrowings	64,053	95	0.20	57,543	97	0.23
Long-Term Debt	<u>163,969</u>	<u>5,343</u>	4.36	<u>180,000</u>	<u>6,103</u>	4.53
Total Interest-Bearing Liabilities	1,490,415	<u>17,792</u>	1.60	1,382,287	<u>19,970</u>	1.93
Demand Deposits	203,263			188,938		
Other Liabilities	<u>23,512</u>			<u>24,806</u>		
Total Liabilities	1,717,190			1,596,031		
Stockholders' Equity	<u>148,929</u>			<u>132,903</u>		
Total Liabilities and Stockholders' Equity	<u>\$1,866,119</u>			<u>\$1,728,934</u>		
Net Interest Income (Tax-equivalent Basis)		49,079			47,036	
Net Interest Spread			3.42			3.48
Net Interest Margin			3.68			3.79
Reversal of Tax-equivalent Adjustment		<u>(2,545)</u>	(.19)		<u>(2,318)</u>	(.19)
Net Interest Income, As Reported		<u>\$46,534</u>			<u>\$44,718</u>	

**OVERVIEW**

We reported net income for the third quarter of 2010 of \$5.6 million, representing diluted earnings per share (EPS) of \$.50. Both of these measures represent an increase of over 10% from the 2009 third quarter. Return on average equity (ROE) for the 2010 third quarter continued to be very strong at 14.39%, a slight decrease of 33 basis points from the ROE of 14.72% for the quarter ended September 30, 2009. Return on average assets (ROA) for the 2010 third quarter also continued to be very strong at 1.18%, an increase of 5 basis points from the ROA of 1.13% for the quarter ended September 30, 2009.

We reported net income for the first nine months of 2010 of \$16.7 million, representing EPS of \$1.48. These results were virtually identical to our net income and EPS for the first nine months of 2009. As we previously reported, however, our results for the first nine months of 2009 included a gain of \$1.79 million, or \$.16 per share, net of tax, recognized on the sale of our merchant bank card processing line of business to TransFirst LLC. Excluding this transaction, adjusted net income for the first nine months of 2009 was \$14.9 million, representing adjusted diluted EPS of \$1.32. These adjusted net income and EPS measures for the 2009 period are non-GAAP financial measures but provide a better comparison, we believe, to our earnings results for the 2010 period. Our diluted EPS for the first nine months of 2010 determined in accordance with GAAP was \$0.16 per share (or 12.1%) greater than the adjusted non-GAAP diluted EPS for the comparable 2009 period. We have provided a reconciliation of the 2009 non-GAAP measures to the comparable 2009 measures determined in accordance with GAAP, as required under Regulation G, in the table on page 45, and have also compared the 2009 non-GAAP earnings measures to the comparable 2010 earnings measures determined in accordance with GAAP.

Total assets were \$1.960 billion at September 30, 2010, which represented an increase of \$124.0 million, or 6.8%, above the level at September 30, 2009, and an increase of \$118.7 million, or 6.4%, from the December 31, 2009 level.

Stockholders' equity was \$153.5 million at September 30, 2010, an increase of \$14.2 million, or 10.2%, from the year earlier level. Stockholders' equity increased \$12.6 million from the December 31, 2009 level of \$140.8 million. The components of the change in stockholders' equity since year-end 2009 are presented in the Consolidated Statement of Changes in Stockholders' Equity on page 5, and are discussed in more detail in the section entitled, "Increase in Stockholder Equity."

Our risk-based capital ratios and Tier 1 leverage ratio continued to significantly exceed regulatory minimum requirements at period-end. At September 30, 2010 both of our banks, as well as the holding company, qualified as "well-capitalized" under federal bank regulatory guidelines. See the discussion under "Important New Capital and Liquidity Standards" on page 40 of this Report.

**Financial Market Turmoil:** The Dow Jones Industrial Average (Dow Jones) plunged from a high of over 14,000 in October 2007 to a low of under 6,500 in March 2009, then rebounded by March 2010 to over 11,000, and ranged between 9,600 and 11,200 for the next six months. This degree of market volatility has not been seen in many decades, and the market's turmoil is impacted by the continuing weakness in the U.S. economy. The financial sector and particularly banks have been severely affected, suffering major losses on mortgages and other credit portfolios and an industry-wide loss of short-term liquidity. In addition, bank failures have continued to occur with regularity,

through 2009 and into 2010, and are expected to persist for the foreseeable future. Many community banks, like our company, have not experienced significant losses in their loan or investment portfolios or the liquidity problems that many of our larger contemporaries have experienced, but expanding problems in commercial real estate portfolios throughout the U.S. now threaten many of these community banks (although our commercial portfolio has not experienced significant deterioration to date). The magnitude of turmoil in the markets has had an impact on the operations of all banks, including ours, during recent periods and may continue to influence our financial condition and results of operations in forthcoming periods.

***Economic Recession and Loan Quality:*** As the nationwide economic recession got underway in late 2008, our market area of northeastern New York experienced little in the way of falling real estate values or increasing unemployment, partially due to the fact that our market area had been less affected by the preceding real estate “bubble” than other areas of the U.S. As the recession became stronger and deeper in late 2009, even northeastern New York began to feel the impact of the worsening national economy, reflected in a slow-down in real estate sales and increasing unemployment rates. By year-end 2009, we had experienced a modest decline in the credit quality of our loan portfolio, although by standard measures our portfolio continued to appear stronger than the average for our peer group. In the first nine months of 2010, our loan quality held steady and in some ways actually improved. Nonperforming loans amounted to \$4.0 million at September 30, 2010, a decrease of \$703 thousand from the prior year-end. The ratio of nonperforming loans to period-end loans was .34% at September 30, 2010, a decrease from .42% at December 31, 2009. By way of comparison, the average ratio of nonperforming loans to period-end loans for our peer group was 3.67% at June 30, 2010, an increase of .16% from year-end 2009.

Our loans charged-off (net of recoveries) against our allowance for loan losses were \$157 thousand for the third quarter of 2010, as compared to \$212 thousand for the prior year period. At September 30, 2010, the allowance for loan losses was \$14.6 million, representing 1.27% of total loans. This ratio is unchanged from the prior year-end. To date, we have not experienced significant deterioration in any of our three major loan portfolio segments:

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**Commercial Loans:** We lend to small and medium sized businesses within our market place, which typically do not encounter liquidity problems, since we often also provide support for their supplementary liquidity needs. Current unemployment rates in our region are higher than in the past few years and the number of total jobs has decreased, although these trends are largely attributable to recent changes in the local operations of a small number of large corporations. Commercial property values have not shown significant deterioration in our primary market. We update the appraisals on our nonperforming commercial loans and watched commercial properties as deemed necessary, usually when the loan is downgraded or when we perceive significant market deterioration since our last appraisal. Although we may participate in loans originated by nonaffiliated financial institutions from time to time, we do not purchase whole loans to hold in our portfolio.

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**Residential Real Estate Loans:** We have not experienced a notable increase in our residential real estate foreclosure rates, primarily due to the fact that we did not originate or participate in underwriting subprime or other high-risk mortgage loans, such as so called “Alt A,” “negative amortization,” “option ARM’s” or “negative equity” loans. It is our general practice to originate residential real estate loans using conservative underwriting standards.

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**Indirect Loans (primarily automobile):** These loans comprise nearly 30% of our loan portfolio. During the first nine months of 2010, we did not experience any significant change in our delinquency rate or level of charge-offs on these loans, although both delinquencies and charge-offs did increase modestly during 2009.

***Recent Legislative Developments:***

***Financial Reform:*** In July 2010, comprehensive financial reform legislation was passed under the Dodd-Frank Act. This Act will have an impact on various aspects of our industry, many of which will not be fully known until final regulations are adopted. The impact of this act is discussed below in Part II, Item A, "Risk Factors." The Company will continue to monitor the effect of the Act.

***Health Care Reform:*** In March 2010, comprehensive federal healthcare reform legislation was passed under the Patient Protection and Affordable Care Act, as amended by the Health Care and Education Reconciliation Act of 2010 (collectively, the "Act"). Included among the major provisions of the Act, is a change in tax treatment of the federal drug subsidy paid with respect to eligible retirees. The Act contains provisions that may impact the Company's accounting for some of its benefit plans in future periods by increasing the expense associated with these plans, but at this point, we do not expect that the impact will be material. The exact extent of the Act's impact cannot be determined until final regulations are promulgated and additional interpretations become available. The Company will continue to monitor the effect of the Act.

***Liquidity and Access to Credit Markets:*** We did not experience any liquidity issues during 2009 and have not experienced any liquidity issues in 2010 through the date of this report. The terms of our lines of credit with our correspondent banks, the FHLBNY and the Federal Reserve Bank, have not changed, except for some increases in the maximum borrowing capacity (see our more detailed liquidity discussion on page 40). In general, we rely on asset-based liquidity (i.e., funds placed by us in overnight investments and regular cash flow from maturing investments and loans) with liability-based liquidity as a secondary source (overnight borrowing arrangements with our correspondent banks, arrangements for FHLBNY overnight and term advances, and access to the Federal Reserve Bank discount window, as our main sources). During the recent period of bank failures, some institutions experienced a run on deposits, even though there was no reasonable expectation that depositors would lose any of their insured deposits. We maintain, and periodically test, a contingency liquidity plan whose purpose is to ensure that we can generate an adequate amount of cash to meet a wide variety of potential liquidity crises on very short notice. Our liquidity is further discussed under the section of this report titled "Important New Capital and Liquidity Standards" on page 40.

**Acquisition of Insurance Agency:** As announced earlier, on April 1, 2010, we acquired Loomis & LaPann, Inc., a property and casualty insurance agency (“Loomis”). Loomis will be operated as a wholly-owned subsidiary of our lead bank, Glens Falls National Bank and Trust Company. All the outstanding shares of Loomis were acquired in exchange for shares of Arrow common stock. We recorded the following intangible assets as a result of the acquisition (none of which are deductible for income tax purposes): goodwill of \$514 thousand and change to intangible assets of \$126 thousand. The value of the expirations is being amortized over twenty years. Under the acquisition agreement, we issued 26,296 shares of Arrow’s common stock at closing and an additional 731 shares on May 27, 2010 in connection with a balance sheet adjustment to the purchase price as provided for in the acquisition agreement. The acquisition agreement also provides for annual contingent future payments of Arrow common stock based upon the financial performance and other results of Loomis over a three-year period. The minimum contingent payment is zero and the maximum contingent payment over the entire three-year period is \$330 thousand payable solely in shares of the Company’s common stock valued in accordance with the acquisition agreement.

**Investment Securities and Other-than-temporary Impairment:** During the last quarter of 2009, we recognized a \$375 thousand impairment charge on one inactively traded common stock which we continue to hold in our available-for-sale portfolio, with no subsequent additional impairment charge on this investment during the first nine months of 2010. We have never held and do not hold any preferred or common stock of Fannie Mae or Freddie Mac.

As of quarter-end, we had not experienced any other-than-temporary impairment issues in 2010 with regard to our holdings of mortgage-backed securities or CMO’s. Mortgage-backed securities held by the Company are comprised of pass-through securities backed by conventional residential mortgages and guaranteed by government agencies or government sponsored entities. We do not hold and have not originated any private-label mortgage-backed securities or securities backed by subprime or other high risk non-traditional mortgage loans.

**VISA Transactions in 2008 and 2009:** On March 28, 2008, VISA Inc. distributed to its member banks, including Glens Falls National Bank and Trust Company, by way of a mandatory redemption of 38.7% of the Visa Class B shares held by the member banks, some of the proceeds realized by Visa from the initial public offering and sale of its Class A shares just then completed. With another portion of the IPO proceeds, Visa established a \$3 billion escrow fund to cover certain, but not all, of its continuing litigation liabilities under various antitrust claims, which its member banks would otherwise be required to bear in full. Accordingly, during the second quarter of 2008, we recorded the following transactions:

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A gain of \$749 thousand from the mandatory redemption by Visa from us of 38.7% of our Class B Visa Inc. shares, reflected as an increase in noninterest income, and

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A reversal of \$306 thousand of the \$600 thousand accrual previously recorded by us at December 31, 2007, representing our then estimated proportional share of additional Visa litigation costs, which reversal was reflected as a reduction in other operating expense.

In October 2008, Visa announced that it had settled a lawsuit with Discover Financial Services, which was part of the covered litigation for which the Visa member banks remained contingently liable and for which Visa had established its escrow fund. Since that time, Visa has deposited additional amounts into the escrow fund for covered litigation:

\$1.1 billion in December 2008, \$700 million in July 2009, \$500 million in May 2010 and \$800 million in October 2010. These developments reduced the Company's proportionate exposure for covered litigation but also reduced the ultimate value of its remaining Class B Visa shares, as Visa's settlement of covered litigation claims directly reduced the value of member banks' Class B stock. However, the Company had not previously recognized the value of its remaining Class B shares in accordance with SEC guidance; thus the Company did not recognize any income or expense in any of the periods presented as a result of the reduced value of its Class B shares upon Visa's settlement of the litigation. The estimation of the Company's proportionate share of any potential losses related to the remaining covered litigation is extremely difficult and involves a high degree of uncertainty. Management has determined that the remaining \$294 thousand liability included in "Other Liabilities" on our September 30, 2010 consolidated balance sheet represents the fair value of our proportionate share of the remaining covered Visa litigation obligations at that date, but this value is subject to change depending upon future developments in the covered litigation.

***Sale of Merchant Bank Card Processing to TransFirst:*** As we previously reported during the first quarter of 2009, our bank subsidiaries, Glens Falls National Bank and Trust Company and Saratoga National Bank and Trust Company, sold their merchant bank card processing businesses for an initial cash payment at closing of \$3 million to TransFirst LLC (TransFirst). In connection with the sale, we entered into a relationship with TransFirst under which TransFirst will provide merchant bank card processing to merchant customers of our subsidiary banks. The gain to us from the transaction was offset, in part, by an estimated \$300 thousand cost primarily to terminate certain pre-existing agreements, for a pre-tax net gain at closing of \$2.7 million. In the second quarter of 2009, a post-closing adjustment to the purchase price substantially eliminated the termination fees related to the pre-existing agreements such that our net pre-tax gain on the sale of the business as adjusted increased by \$266 thousand to approximately \$2.97 million.

***FDIC Special Assessment & Prepayment:*** The FDIC announced during the first quarter of 2009 that the agency would levy a special assessment on all FDIC insured financial institutions to rebuild the FDIC's insurance fund which has recently been depleted by bank failures. The special assessment was set at 0.05% of the insured institution's total assets less Tier 1 capital. Institutions were instructed in the second quarter of 2009 to estimate and accrue the expense. We determined that our expense was \$787 thousand, which we accrued on September 30, 2009. The FDIC did not impose any additional special assessments in the remainder of 2009, but did generate additional much needed cash for the insurance fund by requiring insured institutions to prepay in December 2009 their projected assessments for the fourth quarter of 2009 and all of 2010, 2011 and 2012. Our prepayment amount was \$6.8 million, which is being amortized, as required by bank regulatory guidance, into expense during the relevant periods to which such assessment relates. On April 13, 2010 the FDIC Board proposed significant changes in the risk-based premiums scheme for banks, which if enacted as proposed, is not expected to have a material impact on the Company's financial condition or results of operations.

***Increase in Stockholders' Equity:*** At September 30, 2010, our tangible book value per share (calculated based on stockholders' equity reduced by intangible assets including goodwill) amounted to \$12.13, an increase of \$1.09, or 9.9%, from year-end 2009. Our total stockholders' equity at September 30, 2010 increased 9.0% over the year-end 2009 level. Major changes to stockholders' equity included \$16.7 million of net income for the period and a \$3.9 million net unrealized gain in securities available-for-sale (net of tax), offset in part by cash dividends of \$8.2 million and repurchases of our own common stock of \$2.6 million. As of September 30, 2010, our closing stock price was \$25.08, resulting in a trading multiple of 2.07 to our tangible book value. The Company and each of its subsidiary banks also continue to remain classified as "well-capitalized" under regulatory guidelines. As previously disclosed, due

to our strong capital, financial and liquidity positions, we did not participate in the U.S. Treasury's Capital Purchase Program (a component of TARP). The Board of Directors declared and paid a quarterly cash dividend of \$.24 per share for the third quarter of 2010 (as restated for the September 3% stock dividend). The recently enacted Dodd-Frank Act directs the federal bank regulators to promulgate new regulatory capital guidelines for financial institutions. It is anticipated that those guidelines may be more restrictive on banks, and will certainly be at least as restrictive as the capital guidelines presently in place. See the discussion under "Important New Capital and Liquidity Standards" on page 40 of this Report.

***New Branch Office Opened in Queensbury:*** We opened the 29<sup>th</sup> branch office for Glens Falls National Bank and Trust Company (our 35<sup>th</sup> overall) in the second quarter of 2010. The new branch expands our coverage in the Glens Falls / Queensbury market area where we now have six offices in addition to our main office in downtown Glens Falls. The new office is our fourth office located in the same building as a Stewart's Shop. Arrow leases these offices, at market rates, from Stewart's Shops Corp. The President of Stewart's Shops Corp., Gary Dake, also serves as a director of both Arrow and one of its subsidiary banks, Saratoga National Bank and Trust Company.

## CHANGE IN FINANCIAL CONDITION

### Summary of Selected Consolidated Balance Sheet Data

(Dollars in Thousands)

	<u>At Period-End</u>			<u>\$ Change From Dec</u>	<u>\$ Change From Sep</u>	<u>% Change From Dec</u>	<u>% Change From Sep</u>
	<u>Sep 2010</u>	<u>Dec 2009</u>	<u>Sep 2009</u>				
Interest-Bearing Bank							
Balances	\$ 83,122	\$ 22,730	\$ 79,375	\$ 60,392	\$ 3,747	265.7%	4.7%
Securities Available-for-Sale	468,941	437,706	402,963	31,235	65,978	7.1	16.4
Securities Held-to-Maturity	158,106	168,931	162,197	(10,825)	(4,091)	(6.4)	(2.5)
Other Investments	9,474	8,935	9,835	539	(361)	6.0	(3.7)
Loans (1)	1,154,676	1,112,150	1,106,657	42,526	48,019	3.8	4.3
Allowance for Loan Losses	14,629	14,014	13,841	615	788	4.4	5.7
Earning Assets (1)	1,874,319	1,750,452	1,761,027	123,867	113,292	7.1	6.4
Total Assets	1,960,294	1,841,627	1,836,283	118,667	124,011	6.4	6.8
Demand Deposits	\$ 217,855	\$ 198,025	\$ 197,987	\$ 19,830	\$ 19,868	10.0	10.0
NOW Accounts	578,674	516,269	494,517	62,405	84,157	12.1	17.0
Savings Deposits	367,581	336,271	323,508	31,310	44,073	9.3	13.6
Time Deposits of \$100,000 or More	129,635	148,511	163,337	(18,876)	(33,702)	(12.7)	(20.6)
Other Time Deposits	<u>252,850</u>	<u>244,490</u>	<u>253,133</u>	<u>8,360</u>	<u>(283)</u>	3.4	(0.1)
Total Deposits	<u>\$1,546,595</u>	<u>\$1,443,566</u>	<u>\$1,432,482</u>	<u>\$103,029</u>	<u>\$114,113</u>	7.1	8.0
Federal Funds Purchased and	\$ 67,336	\$ 72,020	\$ 60,592	\$(4,684)	\$ 6,744	(6.5)	11.1

Securities Sold Under

Agreements to Repurchase							
FHLB Advances	150,000	140,000	160,000	10,000	(10,000)	7.1	(6.3)
Stockholders' Equity	153,457	140,818	139,304	12,639	14,152	9.0	10.2

(1) Includes Nonaccrual Loans

Changes in Earning Assets: While our total assets increased by \$118 million, or 6.4%, from year-end 2009 to September 30, 2010, our loan portfolio increased by \$42.5 million, or 3.8%, over the same period. This is in line with management's expectations, given slackening loan demand and the general economic weakness across the U.S. economy, including our region. We experienced the following trends in our three largest portfolio segments:

1.

Commercial and commercial real estate loans – period-end balances for this segment increased slightly from year-end 2009 balances, reflecting moderating demand for commercial lending.

2.

Residential real estate loans – these loans increased by \$19.1 million from December 31, 2009 to September 30, 2010, as we closed on loans of approximately \$41.9 million, which exceeded residential real estate loan sales, prepayments and normal amortization.

3.

Indirect and other consumer loans – The balance of these loans began to increase during the second quarter and throughout the third quarter of 2010 as we introduced more aggressive rates. By September 30, 2010, the balance of these loans had increased \$25.5 million since year-end 2009.

During the nine-month period, most of the \$241.4 million of investments purchased for our securities available-for-sale portfolio represented a replacement of maturities and calls from that portfolio. Changes in our securities held-to-maturity portfolio reflected a small amount of maturities and purchases.

Changes in Sources of Funds: Total deposits increased from December 31, 2009 to September 30, 2010, by \$103.0 million, or 7.13%. Compared to September 30, 2009, our total deposits increased \$114.1 million, or 8.0%. Almost half of the increase (\$55.0 million) from September 2009 was attributable to municipal deposits (discussed in more detail below), while the remaining \$59.1 million increase was attributable to our internally generated non-municipal deposit balances with increases occurring primarily in our money market checking and savings accounts. At September 30, 2010, securities sold under agreements to repurchase were \$4.7 million below year-end balances, while FHLB advances increased \$10.0 million from the year-end balances.

*Municipal Deposits:* We experience regular seasonal fluctuations in our balances of municipal deposits. Recently, municipal deposits have ranged from 22% to over 27% of our total deposits. Municipal deposits typically are invested in NOW accounts and time deposits of short duration. Many of our municipal deposit relationships are subject to annual renewal, by formal or informal agreement.

In general, there is a seasonal pattern to municipal deposits starting with a low point beginning in June and continuing during the summer months. Municipal deposit balances tend to increase throughout the fall and into the winter months from tax deposits and receive an additional boost at the end of March from the electronic deposit of state aid to school districts. In addition to these seasonal fluctuations, the overall level of municipal deposit balances fluctuates from year-to-year as some municipalities move their accounts in and out of our banks due to competitive factors. Often, the balances of municipal deposits at the end of a quarter are not representative of the average balances for that quarter.

The recent and continuing financial crisis has had a significant negative impact on governmental tax revenues, including municipal tax revenues, and consequently on municipal budgets. This has not yet resulted in a sustained reduction in our municipal deposits levels, adjusted for seasonal fluctuations, or an elevation in the average rates we pay on such deposits, but either or both of these developments may result in the future.

*Yield Curve:* The shape of the yield curve (i.e., the line depicting interest rates being paid on low- or no-risk securities, such as U.S. Treasury bills, of different maturities, with the rate on the vertical axis and maturity on the horizontal axis) typically turns upward. Our net interest income often reflects our investment of some portion of our short-term deposits in longer-term loans and investments, and hence our net interest margin and earnings level are directly affected by the shape of the yield curve. Generally, the steeper the yield curve, the better our net interest income results. With the sharp decline in short-term interest rates, the yield curve has a more traditional upward slope, as longer-term rates have declined somewhat but not to the same degree as short-term rates.

## **Deposit Trends**

The following two tables provide information on trends in the balance and mix of our deposit portfolio by presenting, for each of the last five quarters, the quarterly average balances by deposit type and the percentage of total deposits represented by each deposit type.

### **Quarterly Average Deposit Balances**

(Dollars in Thousands)

	Quarter Ended				
	<u>Sep 2010</u>	<u>Jun 2010</u>	<u>Mar 2010</u>	<u>Dec 2009</u>	<u>Sep 2009</u>
Demand Deposits	\$ 217,017	\$ 200,547	\$ 191,950	\$ 199,116	\$ 199,611
NOW Accounts	497,981	534,157	526,137	520,161	443,841
Savings Deposits	368,565	359,094	343,078	329,400	310,991
Time Deposits of \$100,000 or More	130,471	133,737	146,874	155,588	167,681
Other Time Deposits	<u>252,507</u>	<u>249,377</u>	<u>245,332</u>	<u>248,455</u>	<u>253,359</u>
Total Deposits	<u>\$1,466,541</u>	<u>\$1,476,912</u>	<u>\$1,453,371</u>	<u>\$1,452,720</u>	<u>\$1,375,483</u>

**Percentage of Average Quarterly Deposits**

	Quarter Ended				
	<u>Sep 2010</u>	<u>Jun 2010</u>	<u>Mar 2010</u>	<u>Dec 2009</u>	<u>Sep 2009</u>
Demand Deposits	14.8%	13.5%	13.2%	13.7%	14.5%
NOW Accounts	34.0	36.2	36.2	35.8	32.3
Savings Deposits	25.1	24.3	23.6	22.7	22.6
Time Deposits of \$100,000 or More	8.9	9.1	10.1	10.7	12.2
Other Time Deposits	<u>17.2</u>	<u>16.9</u>	<u>16.9</u>	<u>17.1</u>	<u>18.4</u>
Total Deposits	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>

For a variety of reasons, including the seasonality of municipal deposits, we typically experience little net growth or a small contraction in average deposit balances in the first and third quarters of the year, versus significant growth in the second and fourth quarters. Deposit balances followed this pattern for the first three quarters of 2010 as the average balance remained essentially flat from the fourth quarter of 2009 to the first quarter of 2010 before increasing during the second quarter of 2010. During the fourth quarter of 2009, average deposits balances also increased due to the addition of a few new large municipal account relationships.

**Quarterly Cost of Deposits**

	Quarter Ended				
	<u>Sep 2010</u>	<u>Jun 2010</u>	<u>Mar 2010</u>	<u>Dec 2009</u>	<u>Sep 2009</u>
Demand Deposits	---	---	---	---	---
NOW Accounts	0.97	1.09	1.10	1.14	1.02
Savings Deposits	0.56	0.64	0.64	0.65	0.64
Time Deposits of \$100,000 or More	2.24	2.18	1.98	2.09	2.19
Other Time Deposits	2.33	2.38	2.46	2.71	2.87
Total Deposits	1.07	1.15	1.16	1.24	1.27

Average rates paid by us on deposits decreased steadily over the previous five quarters, particularly on other time deposits, in which the decrease from the 2009 third quarter to the 2010 third quarter was 49 basis points.

**Impact of Interest Rate Changes**

Our profitability is affected by the prevailing interest rate environment, both short-term rates and long-term rates, by changes in those rates, and by the relationship between short- and long-term rates (i.e., the yield curve).

*Changes in Interest Rates.* From mid-2006 to fall 2007, the Fed maintained elevated short-term rates, with a federal funds target rate of 5.25%. In September 2007, however, in response to a weakening economy and a loss of liquidity in the short-term credit market, precipitated in large part by the collapse in the housing market and resulting problems in subprime residential real estate lending, the Fed began lowering the federal funds target rate, rapidly and by significant amounts.

By the December 2007 meeting of the Board of Governors, the fed funds rate had decreased 100 basis points, to 4.25%, and in early 2008, the Fed, in response to continuing liquidity concerns in the credit markets, further lowered the targeted federal funds rate by an additional 125 basis points, to 3.00%. In the ensuing year, the Fed in a series of rate reductions lowered the target rate to the maximum extent possible; by January 2009, the fed funds target rate was at an unprecedented low of 0% to .25%, where it has remained up to the present. We saw an immediate impact in the reduced cost of our deposits when rates began to fall in 2007, and our deposit costs continued falling in 2008 and 2009 and to a much lesser extent in the first nine months of 2010. Yields on our earning assets have also fallen in the last two years, but at least initially the drop in our asset yields was not as significant as the decline in our deposit rates. As a result, our net interest margins generally increased in late 2007 and early 2008, positively impacting our net interest income.

*Changes in the Yield Curve.* An additional important development with regard to the effect of rate changes on our profitability in the mid-2005 to mid-2007 period was the “flattening” of the yield curve, especially during 2006 and the first half of 2007. After the Fed began increasing short-term interest rates in June 2004, the yield curve did not maintain its traditional upward slope (i.e., lower rates for shorter-duration debt; higher rates for longer-term debt) but flattened; that is, as short-term rates increased, longer-term rates stayed unchanged or even decreased. Therefore, the traditional spread between short-term rates and long-term rates (the upward yield curve) essentially disappeared, i.e., the curve flattened. In late 2006 and in early 2007, the yield curve actually inverted, with short-term rates exceeding long-term rates. We, like many banks, typically fund longer-duration assets with shorter-maturity liabilities, and the flattening of the yield curve directly diminishes the benefit of this strategy. The flattening of the yield curve was the most significant factor in the decrease in our net interest margin during the 2005-2007 period and consequent downward pressure on our net interest income.

At the end of the second quarter of 2007, however, the yield on longer-term securities began to increase compared to short-term investments, and the yield curve began to resume its more traditional upward sloping shape. The increase in rate spread was further enhanced when long-term rates initially held steady after the Fed began lowering short-term rates in September 2007 in response to the economic downturn. Ultimately, as the crisis deepened, long-term rates also began to decrease, while short-term rates continued to decrease, roughly in parity with each other, to the historically low levels that both short- and long-term rates presently occupy, levels that the Federal Reserve explicitly sought to perpetuate at least in the near future, through the various means at its disposal. The upward-sloping yield

curve may continue, and continue to be steep, for some time, to the benefit of banks and financial institution generally. On the other hand, all lending institutions, even those like us who have avoided subprime lending problems and continue to maintain high credit quality, have experienced some pressure on credit quality in recent periods, and this may continue if the national or regional economy continues to be weak. Any credit or asset quality erosion will reduce or possibly outweigh the benefit we may experience from the return of a more positively-sloped yield curve and a highly favorable interest rate environment generally. Thus, no assurances can be given on future improvements in our net interest income or net income generally, particularly as consumer mortgage related borrowings have diminished across the economy and the redeployment of funds from maturing loans and assets into other high-quality assets has become progressively more difficult.

*Effect of Rate Changes on Our Margin.* In September 2007, as noted above, the Fed began lowering short-term interest rates in response to the worsening economy. From the third quarter of 2007 through mid-2008 our margin steadily improved as the rates we paid on our interest-bearing liabilities began to reprice downward more rapidly than the yields on our earning assets. This had a significant positive impact on our net interest income. From mid-2008 into 2009, our net interest margin held steady at around 3.90%, but the margin began to narrow in the last three quarters of 2009 and the first three quarters of 2010 as the downward repricing of paying liabilities began to slow while interest earning assets continued to reprice downward at a steady rate. To a certain extent, further downward pricing of liabilities is approaching the absolute limit, i.e., a zero interest rate, whereas assets continue to have somewhat more room to reprice downward. If the general trend of rate reduction continues, margins, including our margin, will be under continuing pressure and slow shrinkage may continue. In this light, no assurances can be given that our net interest income will continue to grow, even if asset growth continues and earnings may be negatively impacted in future periods.

A discussion of the models we use in projecting the impact on net interest income resulting from possible changes in interest rates vis-à-vis the repricing patterns of our earning assets and interest-bearing liabilities is included later in this Report under Item 3, "Quantitative and Qualitative Disclosures About Market Risk."

### **Non-Deposit Sources of Funds**

We have typically borrowed funds from the Federal Home Loan Bank ("FHLB") under a variety of programs, including fixed and variable rate short-term borrowings and borrowings in the form of "structured advances." These structured advances have original maturities of 3 to 10 years and are callable by the FHLB at certain dates. If the advances are called, we may elect to receive replacement advances from the FHLB at the then prevailing FHLB rates of interest. Our holdings of FHLB advances ranged from \$160 million at September 30, 2009, to \$140 million at December 31, 2009, to \$150 million at September 30, 2010.

The \$20 million of Junior Subordinated Obligations Issued to Unconsolidated Subsidiary Trusts (trust preferred securities) on our consolidated balance sheet as of September 30, 2010 qualify as Tier 1 regulatory capital under capital adequacy guidelines, as discussed under "Capital Resources" beginning on page 38 of this Report. These trust preferred securities are subject to early redemption by us if the proceeds cease to qualify as Tier 1 capital of Arrow for any reason, including if bank regulatory authorities were to reverse their current position and decide that trust

preferred securities do not qualify as regulatory capital or in the event of an adverse change in tax laws that denied the Company the ability to deduct interest paid on these obligations for federal income tax purposes.

The recently-enacted Dodd-Frank Act will not significantly affect the regulatory capital status of our presently outstanding trust preferred securities, for as long as such securities remain outstanding, but our ability to issue such securities in the future may be negatively impacted by the law as the proceeds of future issuances under the law as currently in effect will not qualify as Tier 1 regulatory capital for purposes of risk-based or leverage guidelines.

## Loan Trends

The following two tables present, for each of the last five quarters, the quarterly average balances by loan type and the percentage of total loans represented by each loan type.

### Quarterly Average Loan Balances

(Dollars in Thousands)

	Quarter Ended				
	<u>Sep 2010</u>	<u>Jun 2010</u>	<u>Mar 2010</u>	<u>Dec 2009</u>	<u>Sep 2009</u>
Commercial and Commercial Real Estate	\$ 308,445	\$ 307,853	\$ 306,753	\$ 306,781	\$ 304,968
Residential Real Estate	375,262	371,482	364,974	355,292	343,948
Home Equity	73,285	70,926	68,725	66,037	61,819
Indirect Consumer Loans	351,294	338,950	328,566	337,582	343,751
Other Consumer Loans <sup>(1)</sup>	<u>39,910</u>	<u>41,427</u>	<u>42,586</u>	<u>43,803</u>	<u>45,335</u>
Total Loans	<u>\$1,148,196</u>	<u>\$1,130,638</u>	<u>\$1,111,604</u>	<u>\$1,109,495</u>	<u>\$1,099,821</u>

### Percentage of Total Quarterly Average Loans

	Quarter Ended				
	<u>Sep 2010</u>	<u>Jun 2010</u>	<u>Mar 2010</u>	<u>Dec 2009</u>	<u>Sep 2009</u>
Commercial and Commercial Real Estate	26.8%	27.2%	27.6%	27.6%	27.7%
Residential Real Estate	32.7	32.9	32.8	32.0	31.3
Home Equity	6.4	6.3	6.2	6.0	5.6
Indirect Consumer Loans	30.6	30.0	29.6	30.4	31.3
Other Consumer Loans <sup>(1)</sup>	<u>3.5</u>	<u>3.6</u>	<u>3.8</u>	<u>4.0</u>	<u>4.1</u>
Total Loans	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>

<sup>(1)</sup> The category “Other Consumer Loans”, in the tables above, includes home improvement loans secured by mortgages, which are otherwise reported with residential real estate loans in tables of period-end balances.

**Maintenance of High Quality in the Loan Portfolio:** In the second half of 2008 and throughout most of 2009, the U.S. experienced significant disruption and volatility in its financial and capital markets. A major cause of the disruption was a significant decline in residential real estate values across much of the U.S., which, in turn, triggered widespread defaults on subprime mortgage loans and steep devaluations of portfolios containing these loans and securities collateralized by them. In mid-2009, as real estate values continued to fall in most areas of the U.S., problems spread from subprime loans to better quality mortgage portfolios, and in some cases prime mortgage loans, as well as home equity and credit card loans. In addition, in mid- to late-2009, commercial real estate values also began to decline and commercial real estate mortgage portfolios began to experience the same problems that previously beset residential mortgage portfolios. Although the erosion of residential and commercial property values has in many markets begun to level off in recent periods, the damage to asset portfolios remains a serious concern. Many lending institutions have suffered sizable charge-offs and losses in their loan and investment securities portfolios in the past two years as a result of their origination or investment in these kinds of loans or securities.

Through September 2010, we have not experienced a significant deterioration in our loan or investment portfolios, except for two impaired securities discussed in our December 31, 2009 Form 10-K. We have never engaged in subprime mortgage lending as a business line and we do not extend or purchase any so-called “Alt-A,” “negative amortization,” “option ARM,” or “negative equity” mortgage loans. On occasion we have made loans to borrowers having a FICO score of 660 or below or have had extensions of credit outstanding to borrowers who have developed credit problems after origination resulting in deterioration of their FICO scores.

We also on occasion have extended community development loans to borrowers whose creditworthiness is below our normal standards as part of the community support program we have developed in fulfillment of our statutorily-mandated duty to support low- and moderate-income borrowers within our service area. However, we are a prime lender and apply prime lending standards and this, together with the fact that the service area in which we make most of our loans has not experienced as severe a decline in property values as other parts of the U.S., are the principal reasons that we have not experienced to date significant deterioration in the real estate categories of our loan portfolio.

If, however, weakness persists or worsens in the U.S. or our regional economy, we may experience elevated charge-offs, higher provisions to our loan loss reserve, and increasing expense related to asset maintenance and supervision.

**Residential Real Estate Loans:** In recent years, residential real estate and home equity loans have represented the largest segment of our loan portfolio. During the last quarter of 2008 and the first two quarters of 2009, as prevailing mortgage rates began to decline again (due primarily to the fact that the government supported entities, Fannie Mae and Freddie Mac, began to overwhelm the home mortgage market with their very low-rate mortgages), we sold most of our mortgage originations in the secondary market. During the second half of 2009 and the first two quarters of 2010, for a variety of reasons, we once again began to retain newly originated residential real estate loans in our loan portfolio, selling only a relatively small portion of the originations to Freddie Mac (with further offsets as a result of normal principal amortization and prepayments on pre-existing loans). During the third quarter of 2010, rates on conventional mortgages fell. The national average for April was 5.21%, falling to an average of 4.59% for the month of September. In response, we determined to sell most of our originations to Freddie Mac, amounting to \$11.5 million for the quarter. If the current GSE-subsidized low-rate environment for newly originated residential real estate loans

persists, we may continue to elect to sell a higher portion of our loan originations and may even experience a decrease in our outstanding balances in this segment of our portfolio. Moreover, if our local economy or real estate market suffers further major downturns, the demand for residential real estate loans in our service area may decrease, which also may negatively impact our real estate portfolio and our financial performance.

**Indirect Loans (primarily automobile loans):** In the early post-2000 years, indirect loans (primarily automobile loans originated through dealerships located primarily in the eastern region of upstate New York) were the largest segment of our loan portfolio. For much of this period, these loans were the fastest growing segment of our loan portfolio, both in terms of absolute dollar amount and as a percentage of the overall portfolio.

In the last quarter of 2007 and the first two quarters of 2008, we encountered enhanced rate competition on auto loans from other lenders, including finance affiliates of the auto manufacturers who increased their offerings of heavily subsidized, low- or zero-rate loans. This increasingly competitive environment, combined with softening demand for vehicles, especially for SUVs and light trucks, had a negative effect on our indirect originations, and we experienced decreases in these balances in the first two quarters of 2008. However during the last two quarters of 2008, our share of the local indirect auto loan market increased as some of the major lenders in the indirect market pulled back, including the auto companies' financing affiliates. Our portfolio at December 31, 2008 exceeded the balance at December 31, 2007 by \$19.5 million, or 5.7%. However, in 2009 our outstanding balances steadily declined from month to month and our ending balance at December 31, 2009 was \$28.1 million, or 7.8%, below the 2008 year-end balance.

Loan demand increased in the first nine months of 2010 as vehicle sales nationally rose nearly 17% over the very low levels experienced in the first nine months of 2009. Concurrently with the increased loan demand, we introduced more competitive financing rates in the second quarter of 2010 and as a result experienced some growth in this portfolio in both the second and third quarters of 2010.

During the first nine months of 2010, the borrowers on the newly originated indirect loans had an average credit score at origination of over 735. Our experienced lending staff not only utilizes software tools but also reviews and evaluates each loan individually. We believe our disciplined approach to evaluating risk has contributed to maintaining our strong loan quality in this portfolio. Originations of indirect loans for 2009 were approximately \$127.8 million, a decrease of \$50.0 million, or 36.7%, from 2008. Originations for the first nine months of 2010 were approximately \$143.3 million, with a weighted average yield of 4.29%. These indirect loan originations represented an increase of \$44.5 million, or 45.1%, over the originations for the first nine months of 2009.

At September 30, 2010, indirect loans represented the second largest category of loans in our portfolio and a significant component of our business. However, if weakness in auto demand persists, our portfolio is likely to experience limited, if any, overall growth, either in real terms or as a percentage of the total portfolio, regardless of whether the auto company affiliates continue or resume their offering of highly-subsidized vehicle loans. Such weakened demand for vehicle loans could negatively impact our financial performance.

**Commercial, Commercial Real Estate and Construction and Land Development Loans:** In recent years, we have experienced moderate to strong demand for commercial and commercial real estate loans. These loan balances have generally increased, both in dollar amount and as a percentage of the overall loan portfolio. However, in response to the 2008-2009 recession, demand began to ease in 2009 and our outstanding balances at the end of 2009 were essentially unchanged from year-end 2008. During the first three quarters of 2010, commercial loan balances increased by only \$2.7 million, or 0.9%. Substantially all commercial and commercial real estate loans in our portfolio are extended to businesses or borrowers located in our regional market. Many of the loans in the commercial portfolio have variable rates tied to prime, FHLB NY or U.S. Treasury indices. We have not experienced any significant weakening in the quality of our commercial loan portfolio in recent quarters, although during that period on a national scale the commercial real estate market has begun to show signs of significant weakness. It is entirely possible that we may experience a reduction in the demand for such loans and/or a weakening in the quality of our commercial and commercial real estate loan portfolio in upcoming periods.

The following table indicates the annualized tax-equivalent yield of each loan category for the past five quarters.

#### Quarterly Taxable Equivalent Yield on Loans

	Quarter Ended				
	<u>Sep 2010</u>	<u>Jun 2010</u>	<u>Mar 2010</u>	<u>Dec 2009</u>	<u>Sep 2009</u>
Commercial and Commercial Real Estate	5.92%	6.23%	6.23%	6.19%	6.23%
Residential Real Estate	5.59	5.69	5.79	5.77	5.87
Home Equity	2.96	3.04	3.11	3.14	3.22
Indirect Consumer Loans	5.64	5.94	6.19	6.26	6.34
Other Consumer Loans	7.17	7.16	7.24	7.24	7.33
Total Loans	5.58	5.80	5.92	5.94	6.03

From the third quarter of 2009 to the third quarter of 2010, the average yield on our loan portfolio declined by 50 basis points, from 6.08% to 5.58%, due to falling interest rates generally and heightened competitive rate pressure on new commercial and commercial real estate loans as well as automobile loans. The yields on new 30 year fixed-rate residential real estate loans also fell during the period, but we did sell some of those originations to the secondary market, specifically, to Freddie Mac. For the second quarter of 2010, the decrease in average yield on loans was 22 basis points while the decline in our cost of deposits during the quarter was only 8 basis points. This continued a trend in recent quarters that the yield on assets declined more rapidly than our cost of funds, as discussed in more detail on page 29 above in the section entitled "Impact of Interest Rate Changes."

In general, the yield (tax-equivalent interest income divided by average loans) on our loan portfolio and other earning assets is impacted by changes in prevailing interest rates. We expect that loan yields will continue to rise and fall with changes in prevailing market rates, although the timing and degree of responsiveness will continue to be influenced by a variety of other factors, including the extent of federal government and Federal Reserve participation in the home mortgage market, the makeup of our loan portfolio, the shape of the yield curve, consumer expectations and preferences and the rate at which the portfolio expands. Additionally, there is a significant amount of cash flow from normal amortization and prepayments in all loan categories, and this cash flow reprices at current rates as new loans are generated at the current yields.

As noted in the earlier discussion, during a period of change in prevailing rates, we generally experience a time lag between the impact of the change on our deposit portfolio (which is felt relatively quickly) and the impact of the change on our loan portfolio (which occurs more slowly). This time lag tends to have a positive impact on net interest margins during the beginning of a rate decline period and a negative impact on the margin at the beginning of a rate increase period. Conversely, the repricing time lag tends to have a negative impact on our margins when a rate decrease period matures (such has been the case in recent periods), and a positive impact on margins when a rate increase period matures.

At the present time, the prevailing expectation is that rates will remain at historically low levels for a protracted period of time, as a result of consciously adopted and pursued strategies by the Federal Reserve Board. If and when rates do increase to more normal levels, however, the repricing lag between deposits and assets may be expected to have a short-term negative effect on our net interest income and earnings.

### **Investment Portfolio Trends**

The following table presents the changes in the period-end balances for the securities available-for-sale and the securities held-to-maturity investment portfolios from December 31, 2009 to September 30, 2010 (in thousands):

	Fair Value at Period-End			Net Unrealized Gain (Loss)		
	Sep 2010	Dec 2009	Change	Sep 2010	Dec 2009	Change
Securities Available-for-Sale:						
U.S. Treasury and Agency Obligations	\$167,655	\$123,331	\$44,324	\$ 715	\$ 563	\$ 152
State and Municipal Obligations	66,148	18,913	47,235	207	70	137
Collateralized Mortgage Obligations	154,196	199,781	(45,585)	7,571	3,422	4,149
Mortgage-Backed Securities-Residential	78,154	93,017	(14,863)	3,335	1,272	2,063
Corporate and Other Debt Securities	1,390	1,331	59	(107)	(134)	27
Mutual Funds and Equity Securities	<u>1,398</u>	<u>1,333</u>	<u>65</u>	<u>19</u>	<u>25</u>	<u>(6)</u>
Total	<u>\$468,941</u>	<u>\$437,706</u>	<u>\$31,235</u>	<u>\$11,740</u>	<u>\$5,218</u>	<u>\$6,522</u>
Securities Held-to-Maturity:						
State and Municipal Obligations	\$165,070	\$171,183	\$(6,113)	\$6,964	\$2,252	\$4,712

### **Other-Than-Temporary Impairment**

Each quarter we evaluate all investment securities with a fair value less than amortized cost, both in the available-for-sale portfolio and the held-to-maturity portfolio, to determine if there exists other-than-temporary impairment as defined under generally accepted accounting principles. During the last quarter of 2009, we recognized a \$375 thousand impairment charge on one equity security which we continue to hold in our available-for-sale

portfolio. For both periods presented in the above table, other mortgage-backed securities consisted solely of U.S. agency and other government sponsored enterprises mortgage pass-through securities. Mortgage pass-through securities provide to the investor monthly portions of principal and interest pursuant to the contractual obligations of the underlying mortgages. Collateralized mortgage obligations (“CMOs”) separate the repayments into two or more components (tranches), each of which has a separate estimated life and yield. Our practice has been to purchase pass-through securities and CMOs that are guaranteed by federal agencies and government sponsored enterprises and tranches of CMOs with shorter maturities. Included in corporate and other debt securities are corporate bonds and trust preferred securities which were highly rated at the time of purchase. Mutual funds and equity securities include the other-than-temporarily impaired security discussed above.

### Investment Sales, Purchases and Maturities: Available-for-Sale Portfolio

(In Thousands)

	<u>Three Months Ended</u>		<u>Nine Months Ended</u>	
	<u>Sep 2010</u>	<u>Sep 2009</u>	<u>Sep 2010</u>	<u>Sep 2009</u>
<b>Sales</b>				
Collateralized Mortgage Obligations	\$13,909	\$ ---	\$23,747	\$12,464
Mortgage-Backed Securities-Residential	---	---	---	---
Corporate and Other Debt Securities	---	2,434	---	4,417
Mutual Funds and Equity Securities	<u>55</u>	<u>16</u>	<u>197</u>	<u>95</u>
Total Sales	13,964	2,450	23,944	16,976
Net Gains on Securities Transactions	<u>618</u>	<u>48</u>	<u>1,496</u>	<u>329</u>
Proceeds on the Sales of Securities	<u>\$14,582</u>	<u>\$2,498</u>	<u>\$25,440</u>	<u>\$17,305</u>
<b>Purchases</b>				
U.S. Agency Securities	\$ 55,000	\$32,000	\$184,175	\$151,795
Mortgage-Backed Securities-Residential	---	25,528	---	25,528
State and Municipal Obligations	50,839	9,581	56,898	12,127
Other	<u>68</u>	<u>46</u>	<u>303</u>	<u>354</u>
Total Purchases	<u>\$105,907</u>	<u>\$67,155</u>	<u>\$241,376</u>	<u>\$189,804</u>
<b><u>Maturities &amp; Calls</u></b>	<u>\$69,370</u>	<u>\$31,302</u>	<u>\$192,092</u>	<u>\$90,148</u>

Late in the second quarter of 2010, we sold two collateralized mortgage obligations from our securities available-for-sale portfolio with an amortized cost of \$9.8 million. We recognized a pre-tax gain of \$860 thousand on the sale of these two securities. For liquidity purposes, we generally are a net seller of overnight funds. Our seasonal low for municipal deposit balances traditionally occurs during at the end of June each year. Proceeds from this sale brought us back to a neutral position for overnight funds at June 30, 2010. In the third quarter of 2010, we sold an additional \$13.9 million of collateralized mortgage obligations from our securities available-for-sale portfolio to enhance our interest rate risk position.

### Asset Quality

The following table presents information related to our allowance and provision for loan losses for the past five quarters.

### Summary of the Allowance and Provision for Loan Losses

(Dollars in Thousands, Loans Stated Net of Unearned Income)

	<u>Sep 2010</u>	<u>Jun 2010</u>	<u>Mar 2010</u>	<u>Dec 2009</u>	<u>Sep 2009</u>
<b><u>Loan Balances:</u></b>					
Period-End Loans	\$1,154,676	\$1,144,959	\$1,121,147	\$1,112,150	\$1,106,657
Average Loans, Year-to-Date	1,130,280	1,121,173	1,111,604	1,101,759	1,099,153
Average Loans, Quarter-to-Date	1,148,196	1,130,638	1,111,604	1,109,496	1,099,821
Period-End Assets	1,960,294	1,846,119	1,861,295	1,841,627	1,836,283
<b><u>Allowance for Loan Losses, Year-to-Date:</u></b>					
Allowance for Loan Losses, Beginning of Period	\$14,014	\$14,014	\$14,014	\$13,272	\$13,272
Provision for Loan Losses, YTD	1,125	750	375	1,783	1,348
Loans Charged-off, YTD	(712)	(495)	(285)	(1,430)	(1,054)
Recoveries of Loans Previously Charged-off	<u>202</u>	<u>142</u>	<u>79</u>	<u>389</u>	<u>275</u>
Net Charge-offs, YTD	<u>(510)</u>	<u>(353)</u>	<u>(206)</u>	<u>(1,041)</u>	<u>(779)</u>
Allowance for Loan Losses, End of Period	<u>\$14,629</u>	<u>\$14,411</u>	<u>\$14,183</u>	<u>\$14,014</u>	<u>\$13,841</u>
<b><u>Allowance for Loan Losses, Quarter-to-Date:</u></b>					
Allowance for Loan Losses, Beginning of Period	\$14,411	\$14,183	\$14,014	\$13,841	\$13,626
Provision for Loan Losses, QTD	375	375	375	435	427
Loans Charged-off, QTD	(217)	(210)	(285)	(376)	(315)
Recoveries of Loans Previously Charged-off	<u>60</u>	<u>63</u>	<u>79</u>	<u>114</u>	<u>103</u>
Net Charge-offs, QTD	<u>(157)</u>	<u>(147)</u>	<u>(206)</u>	<u>(262)</u>	<u>(212)</u>
Allowance for Loan Losses, End of Period	<u>\$14,629</u>	<u>\$14,411</u>	<u>\$14,183</u>	<u>\$14,014</u>	<u>\$13,841</u>
<b><u>Nonperforming Assets, at Period-End:</u></b>					
Nonaccrual Loans	\$3,713	\$3,227	\$3,342	\$4,390	\$3,905
Loans Past due 90 Days or More	<u>244</u>	<u>1,219</u>	<u>263</u>	<u>270</u>	<u>723</u>
and Still Accruing Interest					
Total Nonperforming Loans	3,957	4,446	3,605	4,660	4,628
Nonaccrual Investments	---	---	---	---	---
Repossessed Assets	32	23	63	59	73
Other Real Estate Owned	<u>---</u>	<u>---</u>	<u>53</u>	<u>53</u>	<u>---</u>
Total Nonperforming Assets	<u>\$3,989</u>	<u>\$4,469</u>	<u>\$3,721</u>	<u>\$4,772</u>	<u>\$4,701</u>
<b><u>Asset Quality Ratios:</u></b>					
Allowance to Nonperforming Loans	369.69%	324.13%	393.43%	300.73%	299.07%
Allowance to Period-End Loans	1.27	1.26	1.27	1.26	1.25
Provision to Average Loans (Quarter)	0.13	0.13	0.14	0.16	0.15
Provision to Average Loans (YTD)	0.13	0.13	0.14	0.16	0.16

Net Charge-offs to Average Loans (Quarter)	0.05	0.05	0.08	0.09	0.08
Net Charge-offs to Average Loans (YTD)	0.06	0.06	0.08	0.09	0.09
Nonperforming Loans to Total Loans	0.34	0.39	0.32	0.42	0.42
Nonperforming Assets to Total Assets	0.20	0.24	0.20	0.26	0.26

### Provision for Loan Losses

Through the provision for loan losses, an allowance is maintained that reflects our best estimate of probable incurred loan losses related to specifically identified loans as well as the remaining portfolio. Loan charge-offs are recorded to this allowance when loans are deemed uncollectible, in whole or in part.

We made a provision for loan losses of \$375 thousand for each of the first three quarters of 2010, following a provision of \$435 thousand in the fourth quarter of 2009. Both the third quarter and nine-month 2010 provisions were less than the respective 2009 provisions primarily due to the improvement in overall credit quality, including net charge-offs and delinquent loans.

We consider our accounting policy relating to the allowance for loan losses to be a critical accounting policy, given the uncertainty involved in evaluating the level of the allowance required to cover credit losses inherent in the loan portfolio, and the material effect that such judgments may have on our results of operations. Through the provision for loan losses, an allowance is maintained that reflects our best estimate of probable incurred loan losses related to specifically identified loans and losses for categories of loans in the remaining portfolio. Actual loan losses are charged against this allowance when loans are deemed uncollectible.

We use a two-step process to determine the provision for loans losses and the amount of the allowance for loan losses. We evaluate impaired commercial and commercial real estate loans over \$250,000 individually, while we evaluate the remainder of the portfolio on a pooled basis as described below.

**Homogenous Loan Pools:** Under our pooled analysis, we group homogeneous loans as follows, each with its own estimated loss-rate:

i)

Secured and unsecured commercial loans,

ii)

Secured construction and development loans,

iii)

Secured commercial loans – non-owner occupied,

iv)

Secured commercial loans – owner occupied,

v)

One to four family residential real estate loans,

vi)

Home equity loans,

vii)

Indirect loans – low risk tiers (based on credit scores),

viii)

Indirect loans – high risk tiers, and

ix)

Other consumer loans.

Within the group of commercial and commercial real estate loans (listed in groups i to iv, above), we sub-group loans based on our internal system of risk-rating, which is applied to all commercial and commercial real estate loans. We establish loss rates for each of these pools.

Estimated losses reflect consideration of all significant factors that affect the collectibility of the portfolio as of September 30, 2010. In our evaluation, we do both a quantitative and qualitative analysis of the homogeneous pools.

**Quantitative Analysis:** Quantitatively, we determine the historical loss rate for each homogeneous loan pool.

During the

past five years we have had little charge-off activity on loans secured by residential real estate. Consumer lending (principally automobile loans) represents a significant component of our total loan portfolio and is the only category of loans that has a history of losses that lends itself to a trend analysis. We have had one small loss on commercial real estate loans in the past five years. Losses on commercial loans (other than those secured by real estate) are also historically low, but can vary widely from year-to-year; this is the most complex category of loans in our loss analysis.

Our net charge-offs for the past five years have been at or near historical lows for our company. Although charge-offs increased slightly in 2008 into early 2009, charge-offs have actually moderated in the past few quarters (see the preceding table on page 35). Annual net charge-offs for the past 5 years have ranged from .04% to .09% of average loans. Our charge-offs in recent years have also been far below average for our peer group. The average net charge-off ratios for bank holding companies in our peer group was 1.36% and .70% for the years ended December 31, 2009 and 2008, respectively. These peer group ratios are significantly increased from the prior five years, when the peer ratios ranged from .13% to .24%. Thus, while charge-offs for our peer group has increased markedly in the past two years, compared to prior years, our charge-offs have remained consistently at very low levels.

**Qualitative Analysis:** While historical loss experience provides a reasonable starting point for our analysis, historical losses, or even recent trends in losses, do not by themselves form a sufficient basis to determine the appropriate level for the allowance. Therefore, we have also considered and adjusted historical loss factors for qualitative and environmental factors that are likely to cause credit losses associated with our existing portfolio. These included:

- .
- Changes in the volume and severity of past due, nonaccrual and adversely classified loans
- .
- Changes in the nature and volume of the portfolio and in the terms of loans
- .
- Changes in the value of the underlying collateral for collateral dependent loans
- .
- Changes in lending policies and procedures, including changes in underwriting standards and collection, charge-off, and recovery practices not considered elsewhere in estimating credit losses
- .
- Changes in the quality of the loan review system
- .
- Changes in the experience, ability, and depth of lending management and other relevant staff
- .
- Changes in international, national, regional, and local economic and business conditions and developments that affect the collectibility of the portfolio
- .
- The existence and effect of any concentrations of credit, and changes in the level of such concentrations
- .

The effect of other external factors such as competition and legal and regulatory requirements on the level of estimated credit losses in the existing portfolio or pool

For each homogeneous loan pool, we estimate a loss factor expressed in basis points for each of the qualitative factors above, and for historical credit losses. We update and change, if necessary, the loss-rates assigned to various pools based on the analysis of loss trends and the change in qualitative and environmental factors.

Overall, our market area has not experienced in the past five quarters the degree of negative impact on lending, credit and property values that the U.S. as a whole has experienced, although this may change in upcoming periods. If our local economy does weaken, our loan losses may increase both in absolute amounts and as a percentage of our loans outstanding.

Due to the imprecise nature of the loan loss estimation process and ever changing economic conditions, the risk attributes of our portfolio may not be adequately captured in data related to the formula-based loan loss components used to determine allocations in our analysis of the adequacy of the allowance for loan losses. Management, therefore, has established and held an unallocated portion within the allowance for loan losses reflecting the uncertainty of future economic conditions within our market area. This unallocated portion of the allowance was \$585 thousand, or 4.0% of the total allowance for loan losses, at September 30, 2010 compared to \$471 thousand, or 3.4%, at September 30, 2009.

## **Risk Elements**

Our nonperforming assets at September 30, 2010 amounted to \$4.0 million, a decrease of \$783 thousand, or 16.4%, from the December 31, 2009 total, and a decrease of \$712 thousand, or 15.2%, from the September 30, 2009 total. For all periods, the amount of nonperforming assets was quite small, especially in comparison to our peer group. Our .24% ratio of nonperforming assets to total assets at June 30, 2010 was well below the 3.42% ratio for our peer group at that date (the most recent date for which peer group numbers are available). Our ratio of nonperforming assets to total assets at September 30, 2010, was an even lower .20%.

The balance of other non-current loans at period-end as to which interest income was being accrued (i.e. loans 30 to 89 days past due, as defined in bank regulatory guidelines) totaled \$7.8 million at September 30, 2010, representing 0.68% of loans outstanding on that date. This balance was down by \$744 thousand from the \$8.6 million of such loans at September 30, 2009, which represented 0.77% of loans then outstanding. These other non-current loans past due 30 to 89 days at September 30, 2010 were composed of approximately \$4.6 million of consumer loans, principally indirect automobile loans, \$1.3 million of residential real estate loans and \$1.9 million of commercial loans.

The number and dollar amount of our performing loans that demonstrate characteristics of potential weakness from time-to-time (potential problem loans, which typically is a very small percentage of our portfolio), depends principally on economic conditions in our geographic market area of northeastern New York State. In general, the economy in this area was relatively strong in the years preceding the financial crisis and has weathered the recession and the weakened U.S. economy of the past two years better than most areas. Nevertheless, continued general weakness in the U.S. economy in upcoming periods would likely have an adverse effect on the economy in our market area as well, which may negatively impact our loan portfolio.

At present, we do not anticipate significant increases in our nonperforming assets, other non-current loans as to which interest income is still being accrued or potential problem loans, but can give no assurances in this regard.

## **CAPITAL RESOURCES**

*Stockholders' Equity:* Stockholders' equity increased \$12.6 million during the first nine months of 2010, from \$140.8 million to \$153.5 million. Components of the change in stockholders' equity over the nine-month period are presented in the Consolidated Statement of Changes in Stockholders' Equity, on page 5 of this Report and discussed in more detail under the heading "Increase in Stockholder Equity" on page 27. The cash dividend was \$.243 per share for each of the first three quarters of 2010 (as adjusted for the September 2010 3% stock dividend). The Board has declared an increased cash dividend of \$.25 per share to be paid on December 15, 2010.

*Stock Repurchase Program:* At its April 2010 meeting, the Board of Directors approved a stock repurchase program authorizing the repurchase, at the discretion of senior management, of up to \$5 million of Arrow's common stock in the ensuing twelve months in open market, negotiated or private transactions. This program replaced a similar \$5 million repurchase program approved one year earlier, in April 2009, of which amount approximately \$2.6 million was used to make repurchases prior to replacement of the 2009 program with the 2010 program. See Part II, Item 2 of this Report for further information on stock repurchases and repurchase programs. Management may affect stock repurchases under the 2010 program from time-to-time in upcoming periods, to the extent that it believes the Company's stock is reasonably priced and such repurchases appear to be an attractive use of excess capital and in the best interests of stockholders.

*Regulatory Capital:* The following discussion of capital focuses on regulatory capital ratios, as defined and mandated for financial institutions by federal bank regulatory authorities. Regulatory capital, although a financial measure that is not provided for or governed by GAAP, nevertheless has been exempted by the SEC from the definition of "non-GAAP financial measures" in the SEC's Regulation G governing disclosure of non-GAAP financial measures. Thus, certain information which is generally required to be presented in connection with disclosure of non-GAAP financial measures need not be provided, and has not been provided, in connection with the disclosure on regulatory capital measures below.

*New Capital Standards to be Promulgated:* This discussion and disclosure below on regulatory capital is qualified in its entirety by referenced to the fact that the recently enacted Dodd-Frank Act, among other financial reforms, directed the federal bank regulatory authorities to promulgate new capital standards for all financial institutions, including banks like us. These standards must be at least as strict as the preexisting capital standards for financial institutions or, if greater "commonly accepted capital standards" then in effect for financial institutions in the advanced economies. The latter reference is generally understood as embracing the new, enhanced capital requirements for leading nations known as Basel III currently awaiting approval by the Group of 20 nations in November 2010. The Basel III standards, if approved and included in the new U.S. bank capital standards will require significantly higher minimum levels of capital for U.S. financial institutions when fully implemented. See the discussion under "Important New Capital and Liquidity Standards" on page 40 of this Report.

*Current Capital Standards:* Our holding company and our subsidiary banks are currently subject to two sets of regulatory capital measures, risk-based capital guidelines and a leverage ratio test. The risk-based guidelines assign risk weightings to all assets and certain off-balance sheet items of financial institutions and establish an 8% minimum ratio of qualified total capital to risk-weighted assets. At least half of total capital must consist of "Tier 1" capital, which comprises common equity and common equity equivalents, retained earnings, a limited amount of permanent preferred stock and (for holding companies) a limited amount of trust preferred securities (see the discussion below on these securities), less intangible assets, net of associated deferred tax liabilities. Up to half of total capital may consist of so-called "Tier 2" capital, comprising a limited amount of subordinated debt, other preferred stock, certain other instruments and a limited amount of the allowance for loan losses.

The second regulatory capital measure, the leverage ratio test, establishes minimum limits on the ratio of Tier 1 capital to total tangible assets, without risk weighting. For top-rated companies, the minimum leverage ratio currently is 4%, but lower-rated or rapidly expanding companies may be required by bank regulators to meet substantially higher minimum leverage ratios. Federal banking law mandates certain actions to be taken by banking regulators for financial institutions that are deemed undercapitalized as measured under regulatory capital guidelines. The law establishes five levels of capitalization for financial institutions ranging from "well-capitalized" (the highest ranking) to "critically undercapitalized" (the lowest ranking). The Gramm-Leach-Bliley Financial Modernization Act also ties the ability of banking organizations to engage in certain types of non-banking financial activities to such organizations' continuing to qualify as "well-capitalized" under these standards.

*Trust Preferred Securities Under Financial Reform Bill:* In each of 2003 and 2004 we issued \$10 million of trust preferred securities in a private placement. Under the Federal Reserve Board's pre-existing rules on regulatory capital, trust preferred securities may qualify as Tier 1 capital for bank holding companies such as ours in an amount not to exceed 25% of Tier 1 capital, net of goodwill less any associated deferred tax liability. Under the recently enacted Dodd-Frank Act, trust preferred securities outstanding at the effective date of the Act will continue to qualify as Tier 1 capital for those bank holding companies, like Arrow, that have total assets of less than \$15 billion until the redemption or maturity of such securities. Trust preferred securities issued in the future by such holding companies, however, may no longer qualify for this treatment.

As of September 30, 2010, the Tier 1 leverage and risk-based capital ratios for our holding company and our subsidiary banks were as follows:

### Summary of Capital Ratios

	Tier 1 Leverage Ratio	Tier 1 Risk-Based Capital Ratio	Total Risk-Based Capital <u>Ratio</u>
Arrow Financial Corporation	8.79%	14.16%	15.41%
Glens Falls National Bank & Trust Co.	8.64	14.25	15.49
Saratoga National Bank & Trust Co.	9.24	13.27	14.52
Regulatory Minimum	4.00	4.00	8.00
FDICIA's "Well-Capitalized" Standard	5.00	6.00	10.00

All capital ratios for our holding company and our subsidiary banks at September 30, 2010 were well above current minimum capital standards for financial institutions. Additionally, at such date our holding company and our subsidiary banks qualified as “well-capitalized” under federal banking law, based on their capital ratios on that date.

### Stock Prices and Dividends

Our common stock is traded on NasdaqGS® - AROW. The high and low stock prices for the past seven quarters listed below represent actual sales transactions, as reported by NASDAQ. On October 27, 2010, our Board of Directors declared the 2010 fourth quarter cash dividend of \$.25 payable on December 15, 2010. Per share amounts in the table below have been restated for our September 2010 3% stock dividend.

	<u>Market Price</u>		<u>Declared</u>
	<u>Low</u>	<u>High</u>	
			Cash
			Dividends
			<u>Declared</u>
<b><u>2009</u></b>			
First Quarter	\$17.67	\$24.71	\$.236
Second Quarter	19.80	26.39	.236
Third Quarter	23.57	28.88	.236
Fourth Quarter	23.20	28.20	.243
<b><u>2010</u></b>			
First Quarter	\$22.82	\$29.13	\$.243

Second Quarter	22.04	28.63	.243
Third Quarter	21.12	25.65	.243
Fourth Quarter (dividend payable December 15, 2010)			.250

<u>Selected Per Share Information:</u>	<u>Quarter Ended September 30,</u>	
	<u>2010</u>	<u>2009</u>
Dividends Per Share	\$ .24	\$ .24
Diluted Earnings Per Share	.50	.45
<b>Dividend Payout Ratio</b>	<b>48.00%</b>	<b>53.33%</b>
Total Equity (in thousands)	\$153,457	\$139,304
Shares Issued and Outstanding (in thousands)	11,234	11,244
<b>Book Value Per Share</b>	<b>\$13.66</b>	<b>\$12.39</b>
Intangible Assets (in thousands)	\$17,209	\$16,353
<b>Tangible Book Value Per Share</b>	<b>\$12.13</b>	<b>\$10.93</b>

## LIQUIDITY

Our liquidity is measured by our ability to deploy or raise cash when we need it at a reasonable cost. We must be capable of meeting expected and unexpected obligations to our customers at any time. Given the uncertain nature of customer demands as well as the need to maximize earnings, we must have available appropriate sources of funds, on- and off-balance sheet, at a reasonable cost, that can be accessed quickly in time of need. In addition, we have a liquidity contingency plan that would be followed subsequent to events placing pressure on our liquidity. Periodically we stress test that plan under increasingly severe scenarios. This stress test is not the same as the test bank regulators applied in 2009 to the 19 largest financial institutions, but the scenarios include the types of events that have led to failures of community banks, including rapid acceleration of deposit withdrawals over compacted time periods, reduction or withdrawal of our third-party borrowing facilities, reduction or a rapid increase in non-performing assets, a decline in the value of collateral for collateralized loans, and a rapid shrinkage of our net interest margin.

Cash or cash equivalents on hand, federal funds sold on an overnight basis, interest bearing bank balances at the Federal Reserve Bank, and cash flow from investment securities and loans, both from normal repayment cash-flows and the ability to quickly pledge marketable investment securities and loans to obtain funds, represent our primary sources of available liquidity. Certain investment securities are selected at purchase as available-for-sale based on their marketability and collateral value, as well as their yield and maturity. Our securities available-for-sale portfolio was \$437.7 million at September 30, 2010. Due to the volatility in market values, we are not able to assume that large quantities of such securities could be sold at short notice at their carrying value to provide needed liquidity. But if market conditions are favorable, we may pursue modest sales of such securities conducted in an orderly fashion to provide additional liquidity.

In addition to liquidity from short-term investments, investment securities and maturing loans, we have supplemented available liquidity with additional off-balance sheet sources such as federal funds lines of credit and credit lines with the Federal Home Loan Bank of New York (“FHLBNY”). We have established federal funds lines of credit with three correspondent banks totaling \$30 million, but did not draw on those lines during the first nine months of 2010. We

have established overnight and 30 day term lines of credit with the FHLBNY; each of these lines provided for a maximum borrowing line of \$125.7 million at September 30, 2010. We did not borrow from our overnight or 30-day lines of credit with the FHLBNY during 2010. If advanced, such lines of credit are collateralized by mortgage-backed securities, loans and FHLBNY stock. The balance in other short-term borrowings at September 30, 2010 consisted entirely of treasury, tax and loan balances at the Federal Reserve Bank of New York.

Both of our subsidiary banks, Glens Falls National and Saratoga National, have established a borrowing facility with the Federal Reserve Bank of New York, pledging certain consumer loans as collateral for potential “discount window” advances. At September 30, 2010, the amount available under this facility was \$273.2 million, but there were no advances then outstanding. We have also identified brokered certificates of deposit as an appropriate off-balance sheet source of funding accessible in a relatively short time period. We measure and monitor our basic liquidity as a ratio of liquid assets to short-term liabilities, both with and without the availability of these borrowing arrangements.

During the past several quarters, Arrow’s liquidity position has been strong, as depositors and investors in the wholesale funding markets have shown no hesitation in placing or maintaining their funds with our banks. The financial markets have been challenging for many financial institutions, and in the view of many, a lack or perceived lack of liquidity for many banks has been as great a problem as capital shortage. Because of Arrow’s favorable credit quality and strong balance sheet, Arrow has not experienced any significant liquidity constraints through the date of this report. Based on the level of overnight federal funds investments, available liquidity from our investment securities portfolio, cash flow from our loan portfolio, our stable core deposit base and our significant borrowing capacity, we believe that our liquidity is sufficient to meet any reasonably likely events or occurrences, including suddenly increased levels of deposit withdrawals.

### **Important New Capital and Liquidity Standards**

In December, 2009, the Basel Committee on Banking Supervision (the “Basel Committee”) released a comprehensive list of proposals for changes to capital and liquidity requirements for banks (commonly referred to as “Basel III”). In July 2010, the Basel Committee announced the design for its new capital and liquidity standards.

In September 2010, the oversight body of the Basel Committee announced minimum capital ratios and transition periods providing: (i) a new Tier 1 common equity standard requiring a minimum ratio of common equity to total risk-weighted assets of 4.5% (to be phased in by January 1, 2015); (ii) an increased minimum Tier 1 capital ratio of 6.0%, up from 4.0% (to be phased in by January 1, 2015); (iii) an additional minimum capital buffer of Tier 1 common equity equal to 2.5% of total risk-weighted assets (to be phased in between January 1, 2016 and January 1, 2019; bringing the minimum Tier 1 common equity ratio to 7.0% and the minimum Tier 1 capital ratio to 8.5%), and (iv) a minimum leverage ratio of 3.0% (to be tested starting January 1, 2013). The proposals also narrow the definition of capital, excluding instruments that no longer qualify as Tier 1 common equity as of January 1, 2013, and phasing out other instruments, including TRUPs, over several years.

The liquidity proposals under Basel III include: (i) a liquidity coverage ratio (to become effective January 1, 2015); and (ii) a net stable funding ratio (to become effective January 1, 2018).

Many of the details of Basel III's new framework related to minimum capital requirements will remain uncertain until the Committee's proposals are reviewed and possibly ratified by the Group of 20 finance ministers when they meet in Seoul in November, 2010. Implementation of the final provisions of Basel III, as thus approved, will await final implementing regulations by U.S. banking regulators.

The recently enacted Dodd-Frank Act directs U.S. Bank regulators to promulgate new capital and liquidity guidelines for banks and implicitly directs that the new guidelines should comply at a minimum with the final Basel III Standards.

Adoption and implementation of these new capital and liquidity requirements has created substantial uncertainty for financial institutions. We are not able to predict at this time the content of liquidity and capital guidelines or regulations that may be adopted by regulatory agencies or the impact that any changes in regulation may have on the Company and the Bank.

## RESULTS OF OPERATIONS:

### Three Months Ended September 30, 2010 Compared With

### Three Months Ended September 30, 2009

#### Summary of Earnings Performance

(Dollars in Thousands, Except Per Share Amounts)

(Per share amounts have been adjusted for the September 2010 3% stock dividend)

	Quarter Ended		<u>Change</u>	<u>% Change</u>
	Sep 2010	Sep 2009		
Net Income	\$5,575	\$5,062	\$513	10.1%
Diluted Earnings Per Share	\$.50	.45	\$0.05	11.1
Return on Average Assets	1.18%	1.13%	0.05%	4.4
Return on Average Equity	14.39%	14.72%	(0.33%)	(2.2)

We reported earnings (net income) of \$5.6 million for the third quarter of 2010, an increase of \$513 thousand or 10.1%, from our net income for the third quarter of 2009. Diluted earnings per share were \$.50 and \$.45 for the

respective quarters. Net interest income was virtually unchanged between the two quarters. During the third quarter of 2010, we sold \$13.9 million of securities out of our securities available-for-sale portfolio (primarily collateralized mortgage obligations) for an after tax gain of \$373 thousand versus only \$29 thousand of net gains on securities sales in the year earlier period. We also began to sell most of our newly originated residential real estate loan originations to Freddie Mac in the third quarter of 2010. We recognized net gains of \$285 thousand, net of tax, on these sales, versus only \$10 thousand of net gains on loan sales in the prior period.

The following narrative discusses the quarter-to-quarter changes in net interest income, noninterest income, noninterest expense and income taxes.

## Net Interest Income

### Summary of Net Interest Income

(Taxable Equivalent Basis, Dollars in Thousands)

	Quarter Ended		<u>Change</u>	<u>% Change</u>
	<u>Sep 2010</u>	<u>Sep 2009</u>		
Interest and Dividend Income	\$21,829	\$22,499	\$(670)	(3.0)%
Interest Expense	<u>5,829</u>	<u>6,462</u>	<u>(633)</u>	(9.8)
Net Interest Income	<u>\$16,000</u>	<u>\$16,037</u>	<u>\$(37)</u>	(0.2)
Tax-Equivalent Adjustment	\$832	\$835	\$(3)	(0.4)%
Average Earning Assets (1)	\$1,792,421	\$1,706,626	\$85,795	5.0
Average Interest-Bearing Liabilities	1,485,639	1,417,218	68,421	4.8
Yield on Earning Assets (1)	4.83%	5.23%	(0.40)%	(7.6)
Cost of Interest-Bearing Liabilities	1.56	1.81	(0.25)	(13.8)
Net Interest Spread	3.27	3.42	(0.15)	(4.4)
Net Interest Margin	3.54	3.73	(0.19)	(5.1)

(1) Includes Nonaccrual Loans

Our net interest margin (net interest income on a tax-equivalent basis divided by average earning assets, annualized) decreased from 3.73% to 3.54% between the third quarter of 2009 and the third quarter of 2010. (See the discussion under “Use of Non-GAAP Financial Measures,” on page 19, regarding our net interest margin and net interest income, which are commonly used non-GAAP financial measures.) The positive impact of an increase in our average earning assets of \$85.8 million, or 5.0%, between the periods, almost fully offset the negative impact of a 19 basis point decrease in our net interest margin. The impact of recent interest rate changes on our net interest margin and net interest income are discussed above in this Report under the sections entitled “Deposit Trends,” “Impact of Interest Rate Changes” and “Loan Trends.”

The provisions for loan losses were \$375 thousand and \$427 thousand for the quarters ended September 30, 2010 and 2009, respectively. These provisions were discussed previously under the heading "Asset Quality" beginning on page 35.

## Noninterest Income

### Summary of Noninterest Income (Dollars in Thousands)

	Quarter Ended		<u>Change</u>	<u>% Change</u>
	<u>Sep 2010</u>	<u>Sep 2009</u>		
Income From Fiduciary Activities	\$1,315	\$1,200	\$ 115	9.6%
Fees for Other Services to Customers	2,021	1,956	65	3.3
Insurance Commissions	808	727	81	11.1
Net Gains on Securities Transactions	618	48	570	N/A
Net Gain on Sale of Loans	472	16	456	N/A
Other Operating Income	<u>71</u>	<u>29</u>	<u>42</u>	144.8
Total Noninterest Income	<u>\$5,305</u>	<u>\$3,976</u>	<u>\$1,329</u>	33.4

Total noninterest income in the just completed quarter was \$5.3 million, an increase of \$1.3 million, or 33.4%, from total noninterest income of \$4.0 million for the third quarter of 2009. The increase was primarily attributable the sales of securities and loans cited on the previous page. However, we also experienced increases in our three primary categories of noninterest income: fiduciary activities, fees for other services to customers and insurance commissions.

For the just completed 2010 quarter, income from fiduciary activities increased \$115 thousand, or 9.6%, from the comparable 2009 quarter. The increase principally reflected a recovery in the dollar amount of assets under administration, which itself mirrored a general recovery in the U.S. equity and debt markets. At quarter-end 2010, the market value of assets under trust administration and investment management amounted to \$925.9 million, an increase of \$89.5 million, or 10.7%, from quarter-end 2009. A significant portion of our fiduciary fees are indexed to the market value of assets under administration.

Fees for other services to customers, primarily service charges on deposit accounts (including overdraft charges), revenues related to the sale of mutual funds to our customers by third party providers, debit card transaction fees ("interchange fees"), and servicing income on sold loans, were \$2.0 million for the third quarter of 2010, an increase of \$65 thousand, or 3.3%, from the 2009 third quarter totals. The increase was primarily attributable to interchange fees, which increased from \$503 thousand for the third quarter of 2009 to \$571 thousand for the third quarter of 2010. Beginning in 2011, the Dodd-Frank Act allows merchants the ability to charge lower prices for customers paying in cash. This provision may reduce our interchange fee income next year.

Certain provisions of the Dodd-Frank Act limited the size of interchange fees that large banks may charge on customers' debit card transactions. Although these provisions do not directly apply to smaller community banks like ours, most community banks nevertheless anticipate that the law may indirectly restrict their ability to continue to charge their current interchange fees because of the need to compete on price with larger banks. On November 12, 2009, the Federal Reserve issued amendments to Regulation E implementing certain provisions in the Electronic Fund Transfer Act. The new rules, which became effective on July 1, 2010, among other things, set limits on the ability of

banks to provide deposit customers with overdraft protection on their deposit accounts, and to charge them overdraft fees for covered overdrafts, without the customer's consent. We believe that these new laws and rules restricting interchange fees and overdraft fees are not likely to have a material adverse impact on our financial condition or results of operations in future periods. Our interchange fee percentage will not likely be materially reduced in upcoming periods, we believe, and debit card usage by our customers continues to grow. Moreover, we do not offer so-called "privilege", "bounce" or similar automated overdraft protection programs of the sort that led to substantial increases in overdraft fee income at certain other banks and provided the impetus for the new consumer protection regulations restricting the use of such programs by banks.

Insurance commissions first became a significant source of noninterest income for us following our 2004 acquisition of an insurance agency, Capital Financial Group, Inc. Capital Financial specializes in selling and servicing group health care policies. On April 1, 2010, we acquired a second insurance agency, Loomis & LaPann, Inc., which sells primarily property and casualty insurance to retail customers in our service area. We expect that noninterest income from insurance commissions, which increased in our just completed quarter compared to the prior year quarter, will continue to increase in upcoming periods as a result of our expansion of this business line.

As cited earlier, the volume of our loan sales increased during the third quarter of 2010, leading to an increase in income from that source. Other operating income also includes net gains on the sale of other real estate owned as well as other miscellaneous revenues. For the 2010 quarter, other operating income increased \$42 thousand from 2009. We are unable to predict at what rate we may continue to resell loan originations in future periods versus holding such loans and thereby augmenting our own portfolio. Much depends on the volume of originations, the rates attaching thereto, the ready availability of sales thereof into the secondary market and the pricing of such sales. We have generally retained servicing rights for loans originated and resold by us.

## Noninterest Expense

### Summary of Noninterest Expense

(Dollars in Thousands)

	Quarter Ended		<u>Change</u>	<u>% Change</u>
	<u>Sep 2010</u>	<u>Sep 2009</u>		
Salaries and Employee Benefits	\$ 7,120	\$ 6,727	\$ 393	5.8%
Occupancy Expense of Premises, Net	876	789	87	11.0
Furniture and Equipment Expense	911	819	92	11.2
FDIC and FICO Assessments	486	439	47	10.7
Amortization of Intangible Assets	67	79	(12)	(15.2)
Other Operating Expense	<u>2,646</u>	<u>2,548</u>	<u>98</u>	3.8
Total Noninterest Expense	<u>\$12,106</u>	<u>\$11,401</u>	<u>\$705</u>	6.2
Efficiency Ratio	58.20%	56.71%	1.49%	2.6

Noninterest expense for the third quarter of 2010 was \$12.1 million, an increase of \$705 thousand, or 6.2%, from noninterest expense for the third quarter of 2009. For the third quarter of 2010, our efficiency ratio was 58.20%. This ratio, for which lower is better, is a non-GAAP financial measure commonly used in the banking industry to indicate a

financial institution's operating efficiency. See the discussion on page [19] of this Report under the heading "Use of Non-GAAP Financial Measures." Our efficiency ratio is the ratio of noninterest expense (excluding intangible asset amortization) to net interest income (on a tax-equivalent basis) and noninterest income (excluding net securities gains or losses). The efficiency ratio used by the Federal Reserve Board in its "Peer Holding Company Performance Reports" excludes net securities gains or losses from the denominator (as does our calculation), but unlike our ratio does not exclude intangible asset amortization from the numerator (and thus produces a slightly higher number for most institutions). Our efficiency ratio for the 2010 second quarter was 57.08%, which compared favorably to our peer group's ratio for the 2010 second quarter of 70.73%.

Salaries and employee benefits expense increased by \$393 thousand, or 5.8%, from the third quarter of 2009 to the third quarter of 2010. The increase was primarily attributable to an increase of \$206 thousand, or 4.4%, in salaries, with the remainder of the increase in employee benefit costs. The increase in salaries was attributable to an increase of 8.4 full-time equivalent employees as well as to normal salary increases. We added 9 staff in the acquisition of the Loomis & LaPann insurance agency on April 1, 2010.

Occupancy expense increased \$87 thousand, or 11.0%, from the third quarter of 2009 to the third quarter of 2010.

The increase was primarily attributable to higher maintenance and utilities expenses. The increase in furniture and equipment expense was 11.2% quarter over quarter, and was primarily attributable to data processing expenses.

Risk-based FDIC assessments have increased over the past two years in response to the current financial crisis. We have continued to pay the lowest possible rate for insured depository institutions in recent periods, based on all criteria applied by the FDIC in determining our institution's risk.

Other operating expense increased \$98 thousand, or 3.8%, from the third quarter of 2009. The increase was spread over a variety of operating categories.

## Income Taxes

### Summary of Income Taxes

(Dollars in Thousands)

	Quarter Ended		Change % Change	
	<u>Sep 2010</u>	<u>Sep 2009</u>		
Provision for Income Taxes	\$2,417	\$2,288	\$129	5.6%
Effective Tax Rate	30.2%	31.13%	(0.9)%	(2.9)%

The provisions for federal and state income taxes amounted to \$2.4 million and \$2.3 million for the third quarters of 2010 and 2009, respectively. Most of the provision increase was attributable to increased income as opposed to increased effective tax rates. The decrease in the effective tax rate was attributable to an increase in the relative portion of tax-exempt income to total income in the 2010 period.

## RESULTS OF OPERATIONS:

### Nine Months Ended September 30, 2010 Compared With

### Nine Months Ended September 30, 2009

#### Summary of Earnings Performance

(Dollars in Thousands, Except Per Share Amounts)

(Per share amounts have been restated for the September 2010 3% stock dividend)

	Nine months Ended		<u>Change</u>	<u>% Change</u>
	Sep 2010	Sep 2009		
Net Income	\$16,704	\$16,675	\$29	0.2%
Diluted Earnings Per Share	\$1.48	1.48	\$0.00	0.0
Return on Average Assets	1.20%	1.29%	(0.09)%	(7.0)
Return on Average Equity	15.00%	16.77%	(1.77)%	(10.6)

#### Comparison of 2010 GAAP Earnings Measures to 2009 Adjusted Non-GAAP Earnings Measures:<sup>1</sup>

Net Income	\$16,704	\$14,884	\$1,820	12.2%
Diluted Earnings Per Share	\$1.48	\$1.32	\$0.16	12.1
Return on Average Assets	1.20%	1.15%	0.05%	4.3
Return on Average Equity	15.00%	14.97%	0.03%	0.2

<sup>1</sup> See "Use of Non-GAAP Financial Measures" on page 19.

#### Reconciliation of Non-GAAP to GAAP Financial Disclosures, as required by Regulation G:

Net Income and Related Ratios for the	Net Income	Diluted Per Share	Return on Average	Return on Average
	(in thousands)	Amount	Assets	Equity
Nine months Ended September 30, 2009 (GAAP)	\$16,675	\$1.48	1.29%	16.77%

## Adjustment:

## Net Gain on the Sale of our Merchant Bank Card

Processing to TransFirst LLC (\$2,966 pre-tax)	<u>(1,791)</u>	<u>(.16)</u>	<u>(0.14)%</u>	<u>(1.80)%</u>
Adjusted Net Income and Related Ratios for More				

## Meaningful Comparison, for the Nine months

Ended September 30, 2009 (non-GAAP)	<u>\$14,884</u>	<u>\$1.32</u>	<u>1.15%</u>	<u>14.97%</u>
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## Net Income and Related Ratios for the

Nine months Ended September 30, 2010 (non-GAAP)	\$16,704	\$1.48	1.20%	15.00%
Adjustment: None	<u>---</u>	<u>---</u>	<u>---</u>	<u>---</u>
Adjusted Net Income and Related Ratios for More				

## Meaningful Comparison, for the Nine months

Ended September 30, 2010	<u>\$16.704</u>	<u>\$1.48</u>	<u>1.20%</u>	<u>15.00%</u>
--------------------------	-----------------	---------------	--------------	---------------

We reported earnings (net income) of \$16.7 million for the first nine months of 2010, a virtually identical total to our earnings in the 2009 period. Diluted earnings per share was the same for the two year-to-date periods, as well, at \$1.48. As discussed in the "Overview" section of this Report on page 24, our net income for the first nine months of 2009, determined in accordance with GAAP, included the gain we recognized on the sale of our merchant bank card processing to TransFirst, a non-recurring transaction which closed in that period (the "Transaction"). Adjusting net income for the 2009 period to exclude income from this Transaction produces a non-GAAP measure, adjusted net income, as well as additional non-GAAP measures derived therefrom, i.e., adjusted diluted earnings per share, adjusted return on equity and adjusted return on assets for the 2009 period. Under SEC rules, these non-GAAP measures, if provided in a filed report such as this report, must be accompanied by a reconciliation to the nearest comparable GAAP measure. The table above presents these non-GAAP measures for the 2009 period, a reconciliation of these measures to the comparable GAAP measures for the period, and a comparison between these non-GAAP adjusted measures for the 2009 period and our GAAP measures for the 2010 period, that is, our net income, diluted earnings per share, return on average assets and return on average equity for the first nine months of 2010, prepared in accordance with GAAP. We believe the inclusion of the non-GAAP measure for the 2009 period and the comparison between the 2010 period GAAP measures and the 2009 period non-GAAP measures is meaningful and helpful, because it better reveals the earnings from our fundamental line of business, the commercial banking business, and the trend from period to period in that business. An increase in income in the 2010 period from the sales of securities and loans had a positive impact on income for that period compared to the earlier 2009 period, in which net gains from sales of securities and loans were substantially smaller.

The following narrative discusses the nine-month to nine-month changes in net interest income, noninterest income, noninterest expense and income taxes.

## Net Interest Income

### Summary of Net Interest Income

(Taxable Equivalent Basis, Dollars in Thousands)

	Nine months Ended		<u>Change</u>	<u>% Change</u>
	<u>Sep 2010</u>	<u>Sep 2009</u>		
Interest and Dividend Income	\$66,871	\$67,006	\$ (135)	(0.2)%
Interest Expense	<u>17,792</u>	<u>19,970</u>	<u>(2,178)</u>	(10.9)
Net Interest Income	<u>\$49,079</u>	<u>\$47,036</u>	<u>\$2,043</u>	4.3
Tax-Equivalent Adjustment	\$2,545	\$2,318	\$227	9.8
Average Earning Assets (1)	\$1,781,936	\$1,657,111	\$124,825	7.5
Average Interest-Bearing Liabilities	1,490,415	1,382,287	108,128	7.8
Yield on Earning Assets (1)	5.02%	5.41%	(0.39)%	(7.2)
Cost of Interest-Bearing Liabilities	1.60	1.93	(0.33)	(17.1)
Net Interest Spread	3.42	3.48	(0.06)	(1.7)
Net Interest Margin	3.68	3.79	(0.11)	(2.9)

(1) Includes Nonaccrual Loans

Our net interest margin (net interest income on a tax-equivalent basis divided by average earning assets, annualized) decreased from 3.79% to 3.68% between the first nine months of 2009 and the first nine months of 2010. (See the discussion under "Use of Non-GAAP Financial Measures," on page 19, regarding our net interest margin and net interest income, which are commonly used non-GAAP financial measures.) However, net interest income for the just completed period, on a taxable equivalent basis, increased \$2.0 million, or 4.3%, from the first nine months of 2009, due principally to the fact that our increase in average earning assets between the two periods more than compensated for the decrease in our margin. Specifically, average earning assets increased by \$124.8 million, or 7.5%, between the periods, compared to the 11 basis point decrease in our net interest margin. The impact of recent interest rate changes on our net interest margin and net interest income are discussed above in this Report under the sections entitled "Deposit Trends," "Impact of Interest Rate Changes" and "Loan Trends."

The provisions for loan losses were \$1.1 million and \$1.3 million for the nine-month periods ended September 30, 2010 and 2009, respectively. The provision for loan losses was discussed previously under the heading "Asset

Quality" beginning on page 35.

## Noninterest Income

### Summary of Noninterest Income

(Dollars in Thousands)

	Nine months Ended			
	<u>Sep 2010</u>	<u>Sep 2009</u>	<u>Change</u>	<u>% Change</u>
Income From Fiduciary Activities	\$ 4,043	\$ 3,737	\$ 306	8.2%
Fees for Other Services to Customers	5,874	5,937	(63)	(1.1)
Insurance Commissions	2,157	1,822	335	18.4
Net Gains on Securities Transactions	1,496	329	1,167	354.7
Net Gain on Sale of Merchant Bank Card Processing	---	2,966	(2,966)	(100.0)
Income from Restitution Payment	---	450	(450)	(100.0)
Net Gains on the Sale of Loans	527	326	201	61.7
Other Operating Income	<u>254</u>	<u>220</u>	<u>34</u>	15.5
Total Noninterest Income	<u>\$14.351</u>	<u>\$15.787</u>	<u>\$(1.436)</u>	(9.1)

Total noninterest income in the just completed nine-month period was \$14.4 million, down by \$1.4 million, or 9.1%, from total noninterest income of \$15.8 million for the first nine months of 2009. The primary reason for the \$1.4 million decrease was that the 2009 total included a \$2.97 million gain from the sale of our merchant bank card processing business in that period. The 2010 period reflects significantly higher net gains on securities transactions and loan sales over the comparable 2009 period.

For the just completed 2010 period, income from fiduciary activities increased \$306 thousand, or 8.2%, from the comparable 2009 period. The increase reflected a recovery in the dollar amount of assets under administration, largely a result of the general rebound in the U.S. equity and debt markets between the periods. At period-end 2010, the market value of assets under trust administration and investment management amounted to \$925.9 million, an increase of \$89.5 million, or 10.7%, from period-end 2009. A significant portion of our fiduciary fees are indexed to the market value of assets under administration.

Fees for other services to customers (primarily service charges on deposit accounts, revenues related to the sale of mutual funds to our customers by third party providers and servicing income on sold loans) were \$5.9 million for the first nine months of 2010, a decrease of \$63 thousand, or 1.1%, from the 2009 first nine months total. The decrease between the two periods in fees for other services to customers was in part the result of a modest decline in revenues derived from third-party mutual fund sales. The decrease also reflected the fact that the total for the 2009 period included income from our merchant credit card processing business prior to our sale of that business at the end of the first quarter of 2009; no income from that business was earned by us in the first nine months of 2010 (see "Sale of

Merchant Bank Card Processing to TransFirst,” in the Overview section, on page 26). Income from debit card transactions increased from \$1.4 million for the first nine months of 2009 to \$1.7 million for the first nine months of 2010. See the discussion contained in the “Noninterest Income” section of the three month-to-three-month comparison, above, relating to recent changes in law and regulation affecting interchange fees and overdraft fees that may be charged by banks, and the likely impact of such charges on our future results of operations.

Insurance commissions first became a significant source of noninterest income for us following our 2004 acquisition of an insurance agency, Capital Financial Group, Inc. Capital Financial specializes in selling and servicing group health care policies. On April 1, 2010, we acquired a second insurance agency, Loomis & LaPann, Inc., which sells primarily property and casualty insurance to retail customers in our service area. We expect that noninterest income from insurance commissions will continue to increase in upcoming periods as a result of our expansion of this line of business.

The volume of our sales of loan originations decreased after the second quarter of 2009 until the third quarter of 2010, when we began once again to resell most of our newly originated residential real estate loan originations into the secondary market (i.e., to Freddie Mac). See the discussion in the three month-to-three-month comparison, above, regarding our future resales of such loans. Other operating income includes net gains on the sale of other real estate owned as well as other miscellaneous revenues.

## Noninterest Expense

### Summary of Noninterest Expense

(Dollars in Thousands)

	Nine months Ended		<u>Change</u>	<u>% Change</u>
	<u>Sep 2010</u>	<u>Sep 2009</u>		
Salaries and Employee Benefits	\$20,775	\$19,920	\$855	4.3%
Occupancy Expense of Premises, Net	2,641	2,616	25	1.0
Furniture and Equipment Expense	2,695	2,493	202	8.1
FDIC Special Assessment	---	787	(787)	(100.0)
FDIC and FICO Assessments	1,472	1,320	152	11.5
Amortization of Intangible Assets	205	247	(42)	(17.0)
Other Operating Expense	<u>7,860</u>	<u>7,510</u>	<u>350</u>	4.7
Total Noninterest Expense	<u>\$35,648</u>	<u>\$34,893</u>	<u>\$755</u>	2.2
Efficiency Ratio	57.23%	55.44%	1.79%	3.2

Noninterest expense for the first nine months of 2010 was \$35.6 million, an increase of \$755 thousand, or 2.2%, over the expense for the first nine months of 2009. The first nine months of 2009 included a one-time FDIC insurance special assessment of \$787 thousand. For the first nine months of 2010, our efficiency ratio was 57.23%. This ratio, for which lower is better, is a non-GAAP financial measure that is commonly used in the banking industry to indicate

a financial institution's operating efficiency. See the discussion on page 19 of this Report under the heading "Use of Non-GAAP Financial Measures." Our efficiency ratio is the ratio of noninterest expense (excluding intangible asset amortization) to net interest income (on a tax-equivalent basis) and noninterest income (excluding net securities gains or losses). The efficiency ratio used by the Federal Reserve Board in its "Peer Holding Company Performance Reports" excludes net securities gains or losses from the denominator (as does our calculation), but unlike our ratio does not exclude intangible asset amortization from the numerator (and thus produces a slightly higher number for most institutions). Our efficiency ratio for the 2010 nine-month period compared favorably to the second quarter 2010 efficiency ratio of our peer group of 70.73%.

Salaries and employee benefits expense increased by \$855 thousand, or 4.3%, from the first nine months of 2009 to the first nine months of 2010. The increase was primarily in the area of salaries and was attributable to an increase of 8.4 full-time equivalent employees as well as to normal salary increases. We added 9 staff in the acquisition of Loomis & LaPann on April 1, 2010.

Occupancy expense increased by only \$25 thousand, or 1.0%, from the first nine months of 2009 to the first nine months of 2010. The increase in furniture and equipment expense was 8.1% period over period, and was primarily attributable to data processing expenses.

Risk-based FDIC assessments have increased over the past two years in response to the current financial crisis. We have continued to pay the lowest possible rate.

Other operating expense increased \$350 thousand, or 4.7%, from the first nine months of 2009. The increase was spread over a variety of operating categories.

## Income Taxes

### Summary of Income Taxes

(Dollars in Thousands)

	Nine months Ended		Change% Change	
	<u>Sep 2010</u>	<u>Sep 2009</u>	<u>\$(181)</u>	<u>(2.4)%</u>
Provision for Income Taxes	\$7,408	\$7,589		
Effective Tax Rate	30.72%	31.28%	(.56)%	(1.8)

The provisions for federal and state income taxes amounted to \$7.4 million and \$7.6 million for the first nine months of 2010 and 2009, respectively. The decrease in the effective tax rate was attributable to an increase in the relative portion of tax-exempt income to total income in the 2010 period.

**Item 3.**

**QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

In addition to credit risk in our loan portfolio and liquidity risk, discussed earlier, our business activities also generate market risk. Market risk is the possibility that changes in future market rates (interest rates) or prices (fees for products and services) will make our position less valuable. The ongoing monitoring and management of market risk, principally interest rate risk, is an important component of our asset/liability management process, which is governed by policies that are reviewed and approved annually by the Board of Directors. The Board of Directors delegates responsibility for carrying out asset/liability oversight and control to management's Asset/Liability Committee ("ALCO"). In this capacity ALCO develops guidelines and strategies impacting our asset/liability profile based upon estimated market risk sensitivity, policy limits and overall market interest rate levels and trends. We have not made use of derivatives, such as interest rate swaps, in our market risk management process.

Interest rate risk is the most significant market risk affecting us. Interest rate risk is the exposure of our net interest income to changes in interest rates. Interest rate risk is directly related to the different maturities and repricing characteristics of interest-bearing assets and liabilities, as well as to the risk of prepayment of loans and early withdrawal of time deposits, and the fact that the speed and magnitude of responses to interest rate changes varies by product.

The ALCO utilizes the results of a detailed and dynamic simulation model to quantify the estimated exposure of net interest income to sustained interest rate changes. While ALCO routinely monitors simulated net interest income sensitivity over a rolling two-year horizon, it also utilizes additional tools to monitor potential longer-term interest rate risk.

The simulation model attempts to capture the impact of changing interest rates on the interest income received and interest expense paid on all interest-sensitive assets and liabilities reflected on our consolidated balance sheet. This sensitivity analysis is compared to ALCO policy limits which specify a maximum tolerance level for net interest income exposure over a one year horizon, assuming no balance sheet growth and a 200 basis point upward and a 100 basis point downward shift in interest rates, and a repricing of interest-bearing assets and liabilities at their earliest reasonably predictable repricing date. We normally apply a parallel and pro-rata shift in rates over a 12 month period. However, at quarter-end 2010 the targeted federal funds rate was a range of 0 to .25%. For the decreasing rate simulation we applied a 100 basis point downward shift in interest rates for the long end of the yield curve with short-term rate decreases limited by an absolute floor of a zero interest rate.

Applying the simulation model analysis as of September 30, 2010, a 200 basis point increase in interest rates demonstrated a .79% decrease in net interest income over a 12-month period, and a 100 basis point decrease in interest rates produced a 1.74% decrease in net interest income over a comparable period. These amounts were well within our ALCO policy limits.

The preceding sensitivity analysis does not represent a forecast on our part and should not be relied upon as being indicative of expected operating results.

The hypothetical estimates underlying the sensitivity analysis are based upon numerous assumptions including: the nature and timing of changes in interest rates including yield curve shape, prepayments on loans and securities, deposit decay rates, pricing decisions on loans and deposits, reinvestment/replacement of asset and liability cash flows, and others. While assumptions are developed based upon current economic and local market conditions, we cannot make any assurance as to the predictive nature of these assumptions including how customer preferences or competitor influences might change.

Also, as market conditions vary from those assumed in the sensitivity analysis, actual results will differ due to: prepayment/refinancing levels likely deviating from those assumed, the varying impact of interest rate changes on caps or floors on adjustable rate assets, the potential effect of changing debt service levels on customers with adjustable rate loans, depositor early withdrawals and product preference changes, unanticipated shifts in the yield curve and other internal/external variables. Furthermore, the sensitivity analysis does not reflect actions that ALCO might take in responding to or anticipating changes in interest rates.

#### **Item 4.**

### **CONTROLS AND PROCEDURES**

Senior management, including the Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the design and operation of Arrow's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended) as of September 30, 2010. Based upon that evaluation, senior management, including the Chief Executive Officer and Chief Financial Officer, concluded that our disclosure controls and procedures were effective. Further, there were no changes made in our internal control over financial reporting that occurred during the most recent fiscal quarter that had materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

### **PART II - OTHER INFORMATION**

#### **Item 1.**

#### **Legal Proceedings**

We are not the subject of any material pending legal proceedings, other than ordinary routine litigation occurring in the normal course of our business. On an ongoing basis, we are the subject of or a party to various legal claims, which arise in the normal course of our business. The various pending legal claims against us will not, in the opinion of management based upon consultation with counsel, result in any material liability.

## **Item 1.A.**

### **Risk Factors**

Except as set forth below, there have been no material changes from the Risk Factors described in Part 1 “Item 1A. Risk Factors” of the company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2009.

***The passage of The Dodd-Frank Act and related regulations could negatively impact the company’s business, financial condition, liquidity and results of operations.***

On July 21, 2010, the Dodd-Frank Act, sweeping financial regulatory reform legislation, was signed into law. The Dodd-Frank Act implements far-reaching changes across the financial regulatory landscape, including the following provisions:

*Minimum Leverage and Capital Requirements.* Federal banking agencies are required to establish minimum leverage and risk-based capital requirements on a consolidated basis for all insured depository institutions and bank holding companies, including Arrow and its subsidiary banks, which can be no less than the currently applicable leverage and risk-based capital requirements for depository institutions.

*Interchange Fees.* 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.

*Interest on Demand Deposits.* Repeals the federal prohibitions on the payment of interest on demand deposits, thereby permitting depository institutions to pay interest on business transaction and other accounts.

*Creation of New Consumer Protection Bureau.* Creates a new Bureau of Consumer Financial Protection within the Federal Reserve with broad powers to supervise and enforce consumer protection laws. The Bureau of Consumer Financial Protection will have broad rule-making authority for a wide range of consumer protection laws that apply to all insured depository institutions. The Bureau of Consumer Financial Protection has examination and enforcement authority over all depository institutions with more than \$10 billion in assets. Depository institutions with \$10 billion or less in assets, such as the Company and its subsidiaries, will be examined by their applicable bank regulators.

*FDIC Insurance.* Makes permanent the \$250 thousand limit for federal deposit insurance and provide unlimited federal deposit insurance until January 1, 2013 for non-interest bearing demand transaction accounts at all insured depository institutions.

*Corporate Governance.* Subjects all financial institutions, along with public companies, to corporate governance revisions, including with regard to executive compensation and proxy access by shareholders.

Many provisions of the Dodd-Frank Act are subject to additional regulation and rulemaking before implementation. In addition, the Act requires multiple studies which could result in additional legislative action. At this time, it is difficult to predict the extent to which the Dodd-Frank Act or the resulting regulations and rules may adversely impact the Company. However, compliance with the Dodd-Frank Act may increase our costs, cause us to modify our strategies and business operations, and increase our capital requirements, any of which may have a material adverse impact on our financial condition.

## **Item 2.**

### **Unregistered Sales of Equity Securities and Use of Proceeds**

#### Unregistered Sales of Equity Securities

On April 1, 2010, in connection with Arrow's acquisition of Loomis & LaPann, Inc., a property and casualty insurance agency ("Loomis"), Arrow issued an aggregate of 26,296 shares of its common stock to the former Loomis shareholders, in exchange for all of the issued and outstanding common stock of Loomis. An additional 731 shares of Arrow common stock were issued to the former Loomis shareholders on May 27, 2010 in connection with a balance sheet adjustment to the purchase price provided for in the acquisition agreement. The acquisition agreement also contains a provision under which Arrow would pay to the Loomis shareholders, over the three-year period following closing, additional consideration solely in the form of additional shares of Arrow's common stock, depending on the financial performance and other results of Loomis during such period. All shares issued in connection with the acquisition have been and will be issued without registration under the Securities Act of 1933, as amended (the "1933 Act"), in reliance upon the exemption from such registration set forth in Section 3(a)(11) of the Act and Rule 147 promulgated by the Securities and Exchange Commission thereunder. This exemption is available because the acquirer (Arrow) is a New York corporation, the former shareholders of Loomis were New York residents, and the acquired company (Loomis), was a New York corporation having substantially all of its assets and business operations in the State of New York.

#### Issuer Purchases of Equity Securities

The following table (restated for the September 2010 3% stock dividend) presents information about purchases by Arrow of its own equity securities (i.e. Arrow's common stock) during the three months ended September 30, 2010:

Third Quarter 2010 <u>Calendar Month</u>	(A)	(B)	(C)	(D)
				Maximum
			Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs <sup>2</sup>	Approximate Dollar Value of Shares that May Yet be Purchased Under the Plans or Programs <sup>3</sup>
	<u>Total Number of Shares Purchased<sup>1</sup></u>	Average Price Paid Per Share <sup>1</sup>		
July	21,389	\$22.50	20,600	\$3,455,163
August	17,579	22.37	15,450	3,110,716
September	<u>16,640</u>	23.50	<u>10,300</u>	2,871,016
Total	<u>55,608</u>	22.76	<u>46,350</u>	

Issuer Purchases of Equity Securities, continued

<sup>1</sup>Share amounts and average prices listed in columns A and B (total number of shares purchased and the average price paid per share) include, in addition to shares repurchased by Arrow under the Company's publicly announced stock repurchase program, shares purchased in open market transactions under the Arrow Financial Corporation Automatic Dividend Reinvestment Plan (DRIP) by the administrator of the DRIP (who is independent of the issuer) and shares surrendered (or deemed surrendered) to Arrow by holders of options to acquire Arrow common stock in connection with the exercise of such options. In the months indicated, the total number of shares purchased listed in column A included the following numbers of shares purchased through such additional methods: July – DRIP purchases (789 shares); August – DRIP purchases (2,129 shares); September – DRIP purchases – (6,340 shares).

<sup>2</sup>Share amounts listed in column C include only those shares repurchased under the Company's publicly-announced stock repurchase program in effect during such period, which during the third quarter of 2010 was the \$5 million stock repurchase program authorized by the Board of Directors in April 2010 (the "2010 Repurchase Program"), but do not include shares purchased under the DRIP or upon exercise of outstanding stock options.

<sup>3</sup>Dollar amount of repurchase authority remaining at month-end as listed in column D represents the amount remaining under the 2010 Repurchase Program, the Company's only publicly-announced stock repurchase program in effect during the months indicated. In April 2010 the Board authorized a new \$5 million stock repurchase program, replacing the 2009 Repurchase Program.

**Item 3.**

**Defaults Upon Senior Securities - None**

**Item 4.**

**Removed and Reserved**

**Item 5.**

**Other Information - None**

**Item 6.**

**Exhibits**

(a) Exhibits:

Exhibit 15	Awareness Letter
Exhibit 31.1	Certification of Chief Executive Officer under SEC Rule 13a-14(a)/15d-14(a)
Exhibit 31.2	Certification of Chief Financial Officer under SEC Rule 13a-14(a)/15d-14(a)
Exhibit 32	Certification of Chief Executive Officer under 18 U.S.C. Section 1350 and Certification of Chief Financial Officer under 18 U.S.C. Section 1350

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**ARROW FINANCIAL CORPORATION**

Registrant

Date: November 5, 2010

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s/ Thomas L. Hoy  
Thomas L. Hoy, President,  
Chief Executive Officer and Chairman of the Board

Date: November 5, 2010

s/ Terry R. Goodemote  
Terry R. Goodemote, Senior Vice President,  
Treasurer and Chief Financial Officer  
(Principal Financial Officer and  
Principal Accounting Officer)