

ARROW FINANCIAL CORP
Form 10-Q
November 12, 2013

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the Quarterly Period Ended September 30, 2013

or
 TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

Commission File Number: 0-12507

ARROW FINANCIAL CORPORATION

(Exact name of registrant as specified in its charter)

New York
(State or other jurisdiction of
incorporation or organization)
250 GLEN STREET, GLENS FALLS, NEW YORK 12801
(Address of principal executive offices) (Zip Code)
Registrant's telephone number, including area code: (518) 745-1000

22-2448962
(I.R.S. Employer
Identification No.)

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

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

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Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding as of October 31, 2013
Common Stock, par value \$1.00 per share	12,330,466

ARROW FINANCIAL CORPORATION
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PART I - Financial Information

ARROW FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

(In Thousands, Except Share and Per Share Amounts)

(Unaudited)

	September 30, 2013	December 31, 2012	September 30, 2012
ASSETS			
Cash and Due From Banks	\$47,513	\$37,076	\$43,990
Interest-Bearing Deposits at Banks	24,539	11,756	92,428
Investment Securities:			
Available-for-Sale	486,888	478,698	425,416
Held-to-Maturity (Approximate Fair Value of \$278,390 at September 30, 2013, \$248,252 at December 31, 2012, and \$254,936 at September 30, 2012)	273,626	239,803	244,949
Federal Home Loan Bank and Federal Reserve Bank Stock	3,896	5,792	4,487
Loans	1,243,370	1,172,341	1,152,951
Allowance for Loan Losses	(14,584)	(15,298)	(15,247)
Net Loans	1,228,786	1,157,043	1,137,704
Premises and Equipment, Net	29,386	28,897	26,645
Other Real Estate and Repossessed Assets, Net	499	1,034	834
Goodwill	22,003	22,003	22,003
Other Intangible Assets, Net	4,270	4,492	4,543
Accrued Interest Receivable	6,614	5,486	6,510
Other Assets	28,838	30,716	31,006
Total Assets	\$2,156,858	\$2,022,796	\$2,040,515
LIABILITIES			
Noninterest-Bearing Deposits	\$280,326	\$247,232	\$259,943
NOW Accounts	839,213	758,287	769,107
Savings Deposits	516,010	442,363	443,053
Time Deposits of \$100,000 or More	83,702	93,375	98,215
Other Time Deposits	176,124	189,898	201,143
Total Deposits	1,895,375	1,731,155	1,771,461
Federal Funds Purchased and Securities Sold Under Agreements to Repurchase	15,977	12,678	18,042
Federal Home Loan Bank Overnight Advances	—	29,000	—
Federal Home Loan Bank Term Advances	20,000	30,000	30,000
Junior Subordinated Obligations Issued to Unconsolidated Subsidiary Trusts	20,000	20,000	20,000
Accrued Interest Payable	472	584	676
Other Liabilities	22,351	23,554	24,022
Total Liabilities	1,974,175	1,846,971	1,864,201
STOCKHOLDERS' EQUITY			
Preferred Stock, \$5 Par Value; 1,000,000 Shares Authorized	—	—	—
Common Stock, \$1 Par Value; 20,000,000 Shares Authorized (16,744,486 Shares Issued at September 30, 2013, 16,416,163 Shares Issued at December 31, 2012 and 16,416,163 Shares Issued at	16,744	16,416	16,416

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September 30, 2012)			
Additional Paid-in Capital	228,622	218,650	217,756
Retained Earnings	24,755	26,251	23,697
Unallocated ESOP Shares (87,641 Shares at September 30, 2013, 102,890 Shares at December 31, 2012 and 107,315 Shares at September 30, 2012)	(1,800)	(2,150)	(2,150)
Accumulated Other Comprehensive Loss	(10,293)	(8,462)	(5,693)
Treasury Stock, at Cost (4,327,741 Shares at September 30, 2013, 4,288,617 Shares at December 31, 2012, and 4,274,972 Shares at September 30, 2012)	(75,345)	(74,880)	(73,712)
Total Stockholders' Equity	182,683	175,825	176,314
Total Liabilities and Stockholders' Equity	\$2,156,858	\$2,022,796	\$2,040,515
See Notes to Unaudited Interim Consolidated Financial Statements.			

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ARROW FINANCIAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

(In Thousands, Except Per Share Amounts)

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
INTEREST AND DIVIDEND INCOME				
Interest and Fees on Loans	\$ 12,846	\$ 13,569	\$ 38,279	\$ 41,155
Interest on Deposits at Banks	11	23	57	80
Interest and Dividends on Investment Securities:				
Fully Taxable	1,556	2,191	4,991	7,309
Exempt from Federal Taxes	1,461	1,385	4,352	4,095
Total Interest and Dividend Income	15,874	17,168	47,679	52,639
INTEREST EXPENSE				
NOW Accounts	423	675	1,987	2,710
Savings Deposits	240	319	785	1,005
Time Deposits of \$100,000 or More	297	459	921	1,636
Other Time Deposits	470	855	1,529	3,075
Federal Funds Purchased and Securities Sold Under Agreements to Repurchase	5	6	14	17
Federal Home Loan Bank Advances	167	174	539	543
Junior Subordinated Obligations Issued to Unconsolidated Subsidiary Trusts	145	155	434	468
Total Interest Expense	1,747	2,643	6,209	9,454
NET INTEREST INCOME	14,127	14,525	41,470	43,185
Provision for Loan Losses	—	150	200	670
NET INTEREST INCOME AFTER PROVISION FOR	14,127	14,375	41,270	42,515
LOAN LOSSES				
NONINTEREST INCOME				
Income From Fiduciary Activities	1,688	1,563	5,020	4,786
Fees for Other Services to Customers	2,403	2,097	7,056	6,111
Insurance Commissions	2,404	2,223	6,608	6,219
Net Gain on Securities Transactions	—	64	540	709
Net Gain on Sales of Loans	166	600	1,271	1,494
Other Operating Income	278	288	689	883
Total Noninterest Income	6,939	6,835	21,184	20,202
NONINTEREST EXPENSE				
Salaries and Employee Benefits	7,856	7,964	23,114	23,661
Occupancy Expenses, Net	1,882	1,779	6,277	5,773
FDIC Assessments	269	255	800	766
Other Operating Expense	3,126	2,924	9,627	8,519
Total Noninterest Expense	13,133	12,922	39,818	38,719
INCOME BEFORE PROVISION FOR INCOME TAXES	7,933	8,288	22,636	23,998
Provision for Income Taxes	2,310	2,540	6,625	7,368
NET INCOME	\$ 5,623	\$ 5,748	\$ 16,011	\$ 16,630
Average Shares Outstanding:				

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Basic	12,308	12,252	12,282	12,244
Diluted	12,344	12,273	12,302	12,262
Per Common Share:				
Basic Earnings	\$0.46	\$0.47	\$1.30	\$1.36
Diluted Earnings	0.46	0.47	1.30	1.36

Share and Per Share Amounts have been restated for the September 2013 2% stock dividend.
See Notes to Unaudited Interim Consolidated Financial Statements.

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ARROW FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In Thousands)

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Net Income	\$5,623	\$5,748	\$16,011	\$16,630
Other Comprehensive Income (Loss), Net of Tax:				
Net Unrealized Securities Holding (Losses) Gains Arising During the Period	1,210	411	(2,213)	758
Reclassification Adjustment for Securities Gains Included in Net Income	—	(39)	(326)	(428)
Amortization of Net Retirement Plan Actuarial Loss	235	228	707	685
Accretion of Net Retirement Plan Prior Service Credit	1	(4)	1	(13)
Other Comprehensive Income (Loss)	1,446	596	(1,831)	1,002
Comprehensive Income	\$7,069	\$6,344	\$14,180	\$17,632

See Notes to Unaudited Interim Consolidated Financial Statements.

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ARROW FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
(In Thousands, Except Share and Per Share Amounts)
(Unaudited)

	Common Stock	Additional Paid-In Capital	Retained Earnings	Unallo- cated ESOP Shares	Accumu- lated Other Com- prehensive Income (Loss)	Treasury Stock	Total
Balance at December 31, 2012	\$ 16,416	\$ 218,650	\$ 26,251	\$ (2,150)	\$ (8,462)	\$ (74,880)	\$ 175,825
Net Income	—	—	16,011	—	—	—	16,011
Other Comprehensive (Loss) Income	—	—	—	—	(1,831)	—	(1,831)
2% Stock Dividend (328,323 Shares)	328	8,152	(8,480)	—	—	—	—
Cash Dividends Paid, \$.74 per Share ¹	—	—	(9,027)	—	—	—	(9,027)
Stock Options Exercised, Net (44,849 Shares)	—	524	—	—	—	441	965
Shares Issued Under the Directors' Stock Plan (4,255 Shares)	—	64	—	—	—	42	106
Shares Issued Under the Employee Stock Purchase Plan (14,668 Shares)	—	204	—	—	—	144	348
Shares Issued for Dividend Reinvestment Plans (33,539 Shares)	—	525	—	—	—	326	851
Stock-Based Compensation Expense	—	281	—	—	—	—	281
Tax Benefit for Disposition of Stock Options	—	17	—	—	—	—	17
Purchase of Treasury Stock (61,075 Shares)	—	—	—	—	—	(1,512)	(1,512)
Acquisition of Subsidiaries (9,503 Shares)	—	139	—	—	—	94	233
Allocation of ESOP Stock (16,969 Shares)	—	66	—	350	—	—	416
Balance at September 30, 2013	\$ 16,744	\$ 228,622	\$ 24,755	\$ (1,800)	\$ (10,293)	\$ (75,345)	\$ 182,683
Balance at December 31, 2011	\$ 16,094	\$ 207,600	\$ 23,947	\$ (2,500)	\$ (6,695)	\$ (72,061)	\$ 166,385
Net Income	—	—	16,630	—	—	—	16,630
Other Comprehensive (Loss) Income	—	—	—	—	1,002	—	1,002
2% Stock Dividend (321,886 Shares)	322	7,738	(8,060)	—	—	—	—

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Cash Dividends Paid, \$.72 per Share ¹	—	—	(8,820)	—	—	—	(8,820)
Stock Options Exercised, Net (66,498 Shares)	—	789	—	—	—	661	1,450
Shares Issued Under the Directors' Stock Plan (3,667 Shares)	—	52	—	—	—	36	88
Shares Issued Under the Employee Stock Purchase Plan (14,913 Shares)	—	199	—	—	—	148	347
Shares Issued for Dividend Reinvestment Plans (55,870 Shares)	—	813	—	—	—	556	1,369
Stock-Based Compensation Expense	—	315	—	—	—	—	315
Tax Benefit for Disposition of Stock Options	—	53	—	—	—	—	53
Purchase of Treasury Stock (127,983 Shares)	—	—	—	—	—	(3,145)	(3,145)
Acquisition of Subsidiaries (9,356 Shares)	—	140	—	—	—	93	233
Allocation of ESOP Stock (12,291 Shares)	—	57	—	350	—	—	407
Balance at September 30, 2012	\$16,416	\$217,756	\$23,697	\$(2,150)	\$(5,693)	\$(73,712)	\$176,314

¹ Cash dividends paid per share have been adjusted for the September 2013 2% stock dividend.

See Notes to Unaudited Interim Consolidated Financial Statements.

ARROW FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in Thousands)
(Unaudited)

	Nine Months Ended September	
	30,	
	2013	2012
Cash Flows from Operating Activities:		
Net Income	\$16,011	\$16,630
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Provision for Loan Losses	200	670
Depreciation and Amortization	6,908	6,555
Allocation of ESOP Stock	416	407
Gains on the Sale of Securities Available-for-Sale	(527)	(719)
Gains on the Sale of Securities Held-to-Maturity	(18)	—
Losses on the Sale of Securities Held-to-Maturity	5	—
Losses on the Sale of Securities Available-for-Sale	—	10
Loans Originated and Held-for-Sale	(41,545)	(40,991)
Proceeds from the Sale of Loans Held-for-Sale	44,057	42,561
Net Gains on the Sale of Loans	(1,271)	(1,494)
Net Losses (Gains) on the Sale of Premises and Equipment, Other Real Estate Owned and Repossessed Assets	87	(50)
Contributions to Pension Plans	(354)	(244)
Deferred Income Tax Benefit	(83)	(547)
Shares Issued Under the Directors' Stock Plan	106	88
Stock-Based Compensation Expense	281	315
Net Decrease in Other Assets	2,611	943
Net (Decrease) Increase in Other Liabilities	(653)	1,837
Net Cash Provided By Operating Activities	26,231	25,971
Cash Flows from Investing Activities:		
Proceeds from the Sale of Securities Available-for-Sale	16,284	17,015
Proceeds from the Maturities and Calls of Securities Available-for-Sale	89,857	175,193
Purchases of Securities Available-for-Sale	(121,287)	(63,383)
Proceeds from the Sale of Securities Held-to-Maturity	1,181	—
Proceeds from the Maturities and Calls of Securities Held-to-Maturity	35,214	35,483
Purchases of Securities Held-to-Maturity	(71,573)	(130,769)
Net Increase in Loans	(73,948)	(23,080)
Proceeds from the Sales of Premises and Equipment, Other Real Estate Owned and Repossessed Assets	1,214	827
Purchase of Premises and Equipment	(1,935)	(5,153)
Cash Paid for Subsidiaries, Net	(75)	(75)
Net Decrease in Other Investments	1,896	2,235
Net Cash (Used In) Provided By Investing Activities	(123,172)	8,293
Cash Flows from Financing Activities:		
Net Increase in Deposits	164,220	127,415
Net Decrease in Short-Term Borrowings	(25,701)	(50,251)
Repayments of Federal Home Loan Bank Term Advances	(10,000)	(10,000)
Purchase of Treasury Stock	(1,512)	(3,145)
Stock Options Exercised, Net	965	1,450
Shares Issued Under the Employee Stock Purchase Plan	348	347

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Tax Benefit from Exercise of Stock Options	17	53
Shares Issued for Dividend Reinvestment Plans	851	1,369
Cash Dividends Paid	(9,027)	(8,820)
Net Cash Provided By Financing Activities	120,161	58,418
Net Increase in Cash and Cash Equivalents	23,220	92,682
Cash and Cash Equivalents at Beginning of Period	48,832	43,736
Cash and Cash Equivalents at End of Period	\$72,052	\$136,418
Supplemental Disclosures to Statements of Cash Flow Information:		
Interest on Deposits and Borrowings	\$6,318	\$9,922
Income Taxes	6,086	5,991
Non-cash Investing and Financing Activity:		
Transfer of Loans to Other Real Estate Owned and Repossessed Assets	764	1,084
Acquisition of Subsidiaries	233	233

See Notes to Unaudited Interim Consolidated Financial Statements.

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NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 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, 2013, December 31, 2012 and September 30, 2012; the results of operations for the three and nine-month periods ended September 30, 2013 and 2012; the consolidated statements of comprehensive income for the three and nine-month periods ended September 30, 2013 and 2012; the changes in stockholders' equity for the nine-month periods ended September 30, 2013 and 2012; and the cash flows for the nine-month periods ended September 30, 2013 and 2012. All such adjustments are of a normal recurring nature. The preparation of financial statements requires the use of management estimates. 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, 2012, included in Arrow's 2012 Form 10-K.

New Accounting Standards Updates (ASU): During 2013, through the date of this report, the FASB issued eleven accounting standards updates. Nine did not apply to Arrow. ASU 2013-02 "Comprehensive Income" requires additional disclosures relating to reclassifications out of accumulated other comprehensive income. Since the ASU was effective for this Form 10-Q, the new disclosures are included in Note 5 - Comprehensive Income. ASU 2013-10 "Derivatives and Hedging" now allows the federal funds effective swap rate as a benchmark interest rate for hedge accounting. While this has no current impact on Arrow, it may provide us an option for future swaps that we did not have before the ASU.

Note 2. INVESTMENT SECURITIES (In Thousands)

The following table is the schedule of Available-For-Sale Securities at September 30, 2013, December 31, 2012 and September 30, 2012:

Available-For-Sale Securities

	U.S. Agency Obligations	State and Municipal Obligations	Mortgage- Backed Securities - Residential	Corporate and Other Debt Securities	Mutual Funds and Equity Securities	Total Available- For-Sale Securities
September 30, 2013						
Available-For-Sale Securities, at Amortized Cost	\$ 150,184	\$ 134,059	\$ 179,235	\$ 17,180	\$ 1,120	\$ 481,778
Available-For-Sale Securities, at Fair Value	149,774	133,919	185,215	16,798	1,182	486,888
Gross Unrealized Gains	2	175	6,041	—	62	6,280
Gross Unrealized Losses	412	315	61	382	—	1,170
Available-For-Sale Securities, Pledged as Collateral						314,693
Maturities of Debt Securities, at Amortized Cost:						
Within One Year	—	53,557	20,825	—		74,382
From 1 - 5 Years	150,184	77,849	149,147	16,180		393,360
From 5 - 10 Years	—	1,973	9,263	—		11,236

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Over 10 Years	—	680	—	1,000		1,680
Maturities of Debt Securities, at Fair Value:						
Within One Year	—	53,590	21,390	—		74,980
From 1 - 5 Years	149,774	77,644	153,984	15,998		397,400
From 5 - 10 Years	—	2,005	9,841	—		11,846
Over 10 Years	—	680	—	800		1,480
Securities in a Continuous Loss Position, at Fair Value:						
Less than 12 Months	\$105,517	\$58,710	\$8,482	\$15,998	\$—	\$188,707
12 Months or Longer	4,992	3,513	—	800	—	9,305
Total	\$110,509	\$62,223	\$8,482	\$16,798	\$—	\$198,012
Number of Securities in a Continuous Loss Position	30	230	4	22	—	286

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Available-For-Sale Securities

	U.S. Agency Obligations	State and Municipal Obligations	Mortgage- Backed Securities - Residential	Corporate and Other Debt Securities	Mutual Funds and Equity Securities	Total Available- For-Sale Securities
Unrealized Losses on Securities in a Continuous Loss Position:						
Less than 12 Months	\$405	\$304	\$61	\$182	\$—	\$952
12 Months or Longer	7	11	—	200	—	218
Total	\$412	\$315	\$61	\$382	\$—	\$1,170

December 31, 2012

Available-For-Sale Securities, at Amortized Cost	\$122,297	\$84,798	\$252,480	\$8,689	\$1,120	\$469,384
Available-For-Sale Securities, at Fair Value	122,457	84,838	261,804	8,451	1,148	478,698
Gross Unrealized Gains	204	206	9,405	—	28	9,843
Gross Unrealized Losses	44	166	81	238	—	529
Available-For-Sale Securities, Pledged as Collateral						260,292

 Securities in a Continuous
Loss Position, at Fair Value:

Less than 12 Months	\$72,531	\$46,627	\$10,230	\$8,451	\$—	\$137,839
12 Months or Longer	—	2,149	4,968	—	—	7,117
Total	\$72,531	\$48,776	\$15,198	\$8,451	\$—	\$144,956
Number of Securities in a Continuous Loss Position	22	198	7	11	—	238

 Unrealized Losses on
Securities in a Continuous
Loss Position:

Less than 12 Months	\$44	\$160	\$50	\$238	\$—	\$492
12 Months or Longer	—	6	31	—	—	37
Total	\$44	\$166	\$81	\$238	\$—	\$529

September 30, 2012

Available-For-Sale Securities, at Amortized Cost	\$56,054	\$62,706	\$292,716	\$1,000	\$1,120	\$413,596
Available-For-Sale Securities, at Fair Value	56,391	62,965	304,085	800	1,175	425,416
Gross Unrealized Gains	337	285	11,549	—	55	12,226
Gross Unrealized Losses	—	26	180	200	—	406
Available-For-Sale Securities, Pledged as Collateral						277,357

 Securities in a Continuous
Loss Position, at Fair Value:

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Less than 12 Months	\$4,999	\$17,432	\$18,825	\$800	\$—	\$42,056
12 Months or Longer	—	—	—	—	—	—
Total	\$4,999	\$17,432	\$18,825	\$800	\$—	\$42,056
Number of Securities in a Continuous Loss Position	1	73	7	1	—	82
Unrealized Losses on Securities in a Continuous Loss Position:						
Less than 12 Months	\$—	\$26	\$180	\$200	\$—	\$406
12 Months or Longer	—	—	—	—	—	—
Total	\$—	\$26	\$180	\$200	\$—	\$406

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The following table is the schedule of Held-To-Maturity Securities at September 30, 2013, December 31, 2012 and September 30, 2012:

Held-To-Maturity Securities

	State and Municipal Obligations	Mortgage- Backed Securities - Residential	Corporate and Other Debt Securities	Total Held-To- Maturity Securities
September 30, 2013				
Held-To-Maturity Securities, at Amortized Cost	\$ 194,065	\$ 78,561	\$ 1,000	\$ 273,626
Held-To-Maturity Securities, at Fair Value	198,548	78,842	1,000	278,390
Gross Unrealized Gains	5,018	314	—	5,332
Gross Unrealized Losses	535	33	—	568
Held-To-Maturity Securities, Pledged as Collateral				272,626
Maturities of Debt Securities, at Amortized Cost:				
Within One Year	45,615	—	—	45,615
From 1 - 5 Years	80,848	44,388	—	125,236
From 5 - 10 Years	64,057	34,173	—	98,230
Over 10 Years	3,545	—	1,000	4,545
Maturities of Debt Securities, at Fair Value:				
Within One Year	45,665	—	—	45,665
From 1 - 5 Years	82,492	44,669	—	127,161
From 5 - 10 Years	66,734	34,173	—	100,907
Over 10 Years	3,657	—	1,000	4,657
Securities in a Continuous Loss Position, at Fair Value:				
Less than 12 Months	\$ 27,814	\$ 29,714	\$ —	\$ 57,528
12 Months or Longer	171	—	—	171
Total	\$ 27,985	\$ 29,714	\$ —	\$ 57,699
Number of Securities in a Continuous Loss Position	97	13	—	110
Unrealized Losses on Securities in a Continuous Loss Position:				
Less than 12 Months	\$ 532	\$ 33	\$ —	\$ 565
12 Months or Longer	2	—	—	2
Total	\$ 534	\$ 33	\$ —	\$ 567

Held-To-Maturity Securities

	State and Municipal Obligations	Mortgage- Backed Securities - Residential	Corporate and Other Debt Securities	Total Held-To- Maturity Securities
December 31, 2012				
Held-To-Maturity Securities, at Amortized Cost	\$ 183,373	\$ 55,430	\$ 1,000	\$ 239,803
Held-To-Maturity Securities, at Fair Value	191,196	56,056	1,000	248,252
Gross Unrealized Gains	7,886	626	—	8,512
Gross Unrealized Losses	63	—	—	63
Held-To-Maturity Securities, Pledged as Collateral				238,803

Securities in a Continuous
Loss Position, at Fair Value:

Less than 12 Months	\$ 21,583	\$ —	\$ —	\$ 21,583
12 Months or Longer	503	—	—	503
Total	\$ 22,086	\$ —	\$ —	\$ 22,086
Number of Securities in a Continuous Loss Position	61	—	—	61

Unrealized Losses on
Securities in a Continuous
Loss Position:

Less than 12 Months	\$ 62	\$ —	\$ —	\$ 62
12 Months or Longer	1	—	—	1
Total	\$ 63	\$ —	\$ —	\$ 63

September 30, 2012

Held-To-Maturity Securities, at Amortized Cost	\$ 179,412	\$ 64,537	\$ 1,000	\$ 244,949
Held-To-Maturity Securities, at Fair Value	188,127	65,809	1,000	254,936
Gross Unrealized Gains	8,718	1,272	—	9,990
Gross Unrealized Losses	3	—	—	3
Held-To-Maturity Securities, Pledged as Collateral				243,949

Securities in a Continuous
Loss Position, at Fair Value:

Less than 12 Months	\$ 3,165	\$ —	\$ —	\$ 3,165
12 Months or Longer	—	—	—	—
Total	\$ 3,165	\$ —	\$ —	\$ 3,165
Number of Securities in a Continuous Loss Position	9	—	—	9

Unrealized Losses on

Securities in a Continuous

Loss Position:

Less than 12 Months	\$3	\$—	\$—	\$3
12 Months or Longer	—	—	—	—
Total	\$3	\$—	\$—	\$3

In the tables above, maturities of mortgage-backed-securities - residential are included 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.

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In the available-for-sale category at September 30, 2013, U.S. agency obligations consisted solely of U.S. Government Agency securities with an amortized cost of \$150.2 million and a fair value of \$149.8 million. Mortgage-backed securities-residential consisted of U.S. Government Agency securities with an amortized cost of \$32.5 million and a fair value of \$33.6 million and GSE securities with an amortized cost of \$146.7 million and a fair value of \$151.6 million. In the held-to-maturity category at September 30, 2013, mortgage-backed securities-residential consisted of U.S. Government Agency securities with an amortized cost of \$5.0 million and a fair value of \$4.9 million and GSE securities with an amortized cost of \$73.6 million and a fair value of \$73.9 million.

In the available-for-sale category at September 30, 2012, U.S. agency obligations consisted solely of U.S. Government Agency securities with an amortized cost of \$56.1 million and a fair value of \$56.4 million. Mortgage-backed securities-residential consisted of US Government Agency securities with an amortized cost of \$40.6 million and a fair value of \$42.1 million and GSE securities with an amortized cost of \$262.0 million and a fair value of \$252.1 million. In the held-to-maturity category at September 30, 2012, mortgage-backed securities-residential consisted of GSE securities with an amortized cost of \$64.5 million and a fair value of \$65.8 million.

Securities in a continuous loss position, in the tables above for September 30, 2013, December 31, 2012 and September 30, 2012 do not reflect any deterioration of the credit worthiness of the issuing entities. U.S. Agency issues, including agency-backed collateralized mortgage obligations and mortgage-backed securities, are all rated at least Aaa by Moody's or AA+ by Standard and Poor's. 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 is performed in-house based upon data that has been submitted by the issuers to the NY State Comptroller. That analysis shows no deterioration in the credit worthiness of the municipalities. Subsequent to September 30, 2013, 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 that we would be required to sell the securities prior to recovery, the impairment is considered temporary.

Note 3. LOANS (In Thousands)

Loan Categories and Past Due Loans

The following table presents loan balances outstanding as of September 30, 2013, December 31, 2012 and September 30, 2012 and an analysis of the recorded investment in loans that are past due at these dates. Generally, Arrow considers a loan past due 30 or more days if the borrower is two or more payments past due. Loans held-for-sale of \$1,561, \$2,801 and \$816 as of September 30, 2013, December 31, 2012 and September 30, 2012, respectively, are included in the residential real estate loan balances.

Past Due Loans

	Commercial	Commercial Construction	Commercial Real Estate	Other Consumer	Automobile	Residential	Total
September 30, 2013							
Loans Past Due 30-59 Days	\$595	\$—	\$—	\$50	\$2,230	\$200	\$3,075
Loans Past Due 60-89 Days	750	—	1,173	4	654	1,999	4,580
Loans Past Due 90 or more Days	53	—	1,847	—	133	2,721	4,754
Total Loans Past Due	1,398	—	3,020	54	3,017	4,920	12,409
Current Loans	85,719	33,960	260,084	7,516	389,335	454,347	1,230,961
Total Loans	\$87,117	\$33,960	\$263,104	\$7,570	\$392,352	\$459,267	\$1,243,370
Loans 90 or More Days							
Past Due and Still Accruing Interest	\$—	\$—	\$—	\$—	\$11	\$916	\$927
Nonaccrual Loans	\$269	\$—	\$1,930	\$3	\$240	\$3,729	\$6,171
December 31, 2012							
Loans Past Due 30-59 Days	\$1,045	\$—	\$534	\$43	\$2,427	\$407	\$4,456
Loans Past Due 60-89 Days	1,588	—	1,332	17	793	2,466	6,196
Loans Past Due 90 or more Days	494	—	1,871	—	185	1,462	4,012
Total Loans Past Due	3,127	—	3,737	60	3,405	4,335	14,664
Current Loans	102,409	29,149	241,440	6,624	345,695	432,360	1,157,677
Total Loans	\$105,536	\$29,149	\$245,177	\$6,684	\$349,100	\$436,695	\$1,172,341
Loans 90 or More Days							
Past Due and Still Accruing Interest	\$126	\$—	\$378	\$—	\$42	\$374	\$920
Nonaccrual Loans	\$1,787	\$—	\$2,026	\$1	\$419	\$2,400	\$6,633
September 30, 2012							
Loans Past Due 30-59 Days	\$831	\$—	\$271	\$20	\$2,675	\$2,245	\$6,042
Loans Past Due 60-89 Days	1,764	—	1,051	—	485	822	4,122
Loans Past Due 90 or more Days	216	—	621	—	148	1,278	2,263
Total Loans Past Due	2,811	—	1,943	20	3,308	4,345	12,427
Current Loans	97,612	27,265	233,238	6,837	339,922	435,650	1,140,524
Total Loans	\$100,423	\$27,265	\$235,181	\$6,857	\$343,230	\$439,995	\$1,152,951

Loans 90 or More Days Past Due and Still Accruing Interest	\$—	\$—	\$—	\$—	\$—	\$150	\$150
Nonaccrual Loans	\$1,750	\$—	\$1,156	\$1	\$419	\$2,762	\$6,088

The Company disaggregates its loan portfolio into the following six categories:

Commercial - The Company offers a variety of loan options to meet the specific needs of our commercial customers including term loans, time notes and lines of credit. Such loans are made available to businesses for working capital needs such as inventory and receivables, business expansion and equipment purchases. Generally, a collateral lien is placed on equipment or other assets owned by the borrower. These loans carry a higher risk than commercial real estate loans due to the nature of the underlying collateral, which can be business assets such as equipment and accounts receivable and generally have a lower liquidation value than real estate. In the event of default by the borrower, the Company may be required to liquidate collateral at deeply discounted values. To reduce the risk, management usually obtains personal guarantees of the borrowers.

Commercial Construction - The Company offers commercial construction and land development loans to finance projects within the communities that we serve. Many projects will ultimately be used by the borrowers' businesses, while others are developed for resale.

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These real estate loans are secured by first liens on the real estate, which may include apartments, commercial structures, housing businesses, healthcare facilities, and both owner-occupied and nonowner-occupied facilities. There is enhanced risk during the construction period, since the loan is secured by an incomplete project.

Commercial Real Estate - The Company offers commercial real estate loans to finance real estate purchases, refinancings, expansions and improvements to commercial properties. Commercial real estate loans are made to finance the purchases of real property which generally consists of real estate with completed structures. These commercial real estate loans are secured by first liens on the real estate, which may include apartments, commercial structures, housing businesses, healthcare facilities, and both owner and non owner-occupied facilities. These loans are typically less risky than commercial loans, since they are secured by real estate and buildings, and are generally originated in amounts of no more than 80% of the appraised value of the property.

Other Consumer Loans - The Company offers a variety of consumer installment loans to finance personal expenditures. Most of these loans carry a fixed rate of interest with principal repayment terms typically ranging from one to five years, based upon the nature of the collateral and the size of the loan. In addition to installment loans, the Company also offers personal lines of credit and overdraft protection. Several loans are unsecured, which carry a higher risk of loss.

Automobile - The Company primarily finances the purchases of automobiles indirectly through dealer relationships located throughout upstate New York and Vermont. Most of these loans carry a fixed rate of interest with principal repayment terms typically ranging from three to seven years. The majority of indirect consumer loans are underwritten on a secured basis using the underlying collateral being financed.

Residential Real Estate Mortgages - Residential real estate loans consist primarily of loans secured by first or second mortgages on primary residences. We originate adjustable-rate and fixed-rate, one-to-four-family residential real estate loans for the construction, purchase or refinancing of a mortgage. These loans are collateralized primarily by owner-occupied properties generally located in the Company's market area. Loans on one-to-four-family residential real estate are generally originated in amounts of no more than 85% of the purchase price or appraised value (whichever is lower), or have private mortgage insurance. The Company's underwriting analysis for residential mortgage loans typically includes credit verification, independent appraisals, and a review of the borrower's financial condition. Mortgage title insurance and hazard insurance are normally required. Construction loans have a unique risk, because they are secured by an incomplete dwelling. This risk is reduced through periodic site inspections, including one at each loan draw period. In addition, the Company offers fixed home equity loans as well as home equity lines of credit to consumers to finance home improvements, debt consolidation, education and other uses. Our policy allows for a maximum loan to value ratio of 80%. The Company originates home equity lines of credit and second mortgage loans (loans secured by a second junior lien position on one-to-four-family residential real estate). Risk is generally reduced through underwriting criteria, which include credit verification, appraisals, a review of the borrower's financial condition, and personal cash flows. A security interest, with title insurance when necessary, is taken in the underlying real estate.

Allowance for Loan Losses

The following table presents a roll-forward of the allowance for loan losses and other information pertaining to the allowance for loan losses:

Allowance for Loan Losses

Commercial	Commercial	Other				
Commercial	Construction	Real Estate	Consumer	Automobile	Residential	Unallocated Total

Roll-forward of
the Allowance for
Loan Losses for
the Quarterly
Periods:

June 30, 2013	\$ 1,552	\$ 646	\$ 3,293	\$ 299	\$ 4,357	\$ 3,408	\$ 1,123	\$ 14,678	
Charge-offs	(62) —	—	(7) (114) —	—	(183)
Recoveries	8	—	—	2	79	—	—	89	
Provision	209	4	15	(29) (14) (159) (26) —	
September 30, 2013	\$ 1,707	\$ 650	\$ 3,308	\$ 265	\$ 4,308	\$ 3,249	\$ 1,097	\$ 14,584	
June 30, 2012	\$ 2,098	\$ 528	\$ 3,295	\$ 355	\$ 4,571	\$ 3,451	\$ 913	\$ 15,211	
Charge-offs	—	—	(39) (27) (105) —	—	(171)
Recoveries	2	—	—	8	47	—	—	57	
Provision	22	19	(82) (11) 119	38	45	150	
September 30, 2012	\$ 2,122	\$ 547	\$ 3,174	\$ 325	\$ 4,632	\$ 3,489	\$ 958	\$ 15,247	

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Allowance for Loan Losses

	Commercial	Commercial	Commercial	Other	Automobile	Residential	Unallocated	Total
	Commercial	Construction	Real Estate	Consumer	Automobile	Residential	Unallocated	Total
Roll-forward of the Allowance for Loan Losses for the Year-to-Date Periods:								
December 31, 2012	\$2,344	\$601	\$3,050	\$304	\$4,536	\$3,405	\$1,058	\$15,298
Charge-offs	(850)	—	(11)	(20)	(284)	—	—	(1,165)
Recoveries	48	—	—	2	201	—	—	251
Provision	165	49	269	(21)	(145)	(156)	39	200
September 30, 2013	\$1,707	\$650	\$3,308	\$265	\$4,308	\$3,249	\$1,097	\$14,584
December 31, 2011	\$1,927	\$602	\$3,136	\$350	\$4,496	\$3,414	\$1,078	\$15,003
Charge-offs	(15)	—	(206)	(69)	(281)	(33)	—	(604)
Recoveries	5	—	—	17	156	—	—	178
Provision	205	(55)	244	27	261	108	(120)	670
September 30, 2012	\$2,122	\$547	\$3,174	\$325	\$4,632	\$3,489	\$958	\$15,247
September 30, 2013								
Allowance for loan losses - Loans Individually Evaluated for Impairment	\$—	\$—	\$—	\$—	\$—	\$—	\$—	\$—
Allowance for loan losses - Loans Collectively Evaluated for Impairment	\$1,707	\$650	\$3,308	\$265	\$4,308	\$3,249	\$1,097	\$14,584
Ending Loan Balance - Loans Individually Evaluated for Impairment	\$25	\$—	\$1,497	\$—	\$169	\$1,720	\$—	\$3,411
Ending Loan Balance - Loans Collectively Evaluated for Impairment	\$87,092	\$33,960	\$261,607	\$7,570	\$392,183	\$457,547	\$—	\$1,239,959

December 31,
2012

Allowance for
loan losses -

Loans

Individually

Evaluated for

Impairment

\$ 853

\$—

\$—

\$—

\$—

\$—

\$—

\$ 853

Allowance for
loan losses -

Loans

Collectively

Evaluated for

Impairment

\$ 1,491

\$ 601

\$ 3,050

\$ 304

\$ 4,536

\$ 3,405

\$ 1,058

\$ 14,445