ARROW FINANCIAL CORP
Form 10-Q
August 08, 2017

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

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

For the Quarterly Period Ended June 30, 2017

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	22-2448962
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

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

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. x Yes
No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 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). x 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 the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

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

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standard provided pursuant to Section 13(a) of the Exchange Act. __

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

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 July 31, 2017
Common Stock, par value $1.00 per share	13,509,655

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)

	June 30, 2017	December 31, 2016	June 30, 2016
ASSETS			
Cash and Due From Banks	$39,105	$43,024	$46,139
Interest-Bearing Deposits at Banks	26,972	14,331	16,976
Investment Securities:			
Available-for-Sale	327,392	346,996	362,929
Held-to-Maturity (Approximate Fair Value of $350,355 at June 30, 2017; $343,751 at December 31, 2016; and $354,778 at June 30, 2016)	348,018	345,427	343,814
Other Investments	11,035	10,912	9,961
Loans	1,878,632	1,753,268	1,672,490
Allowance for Loan Losses	(17,442)	(17,012)	(16,798)
Net Loans	1,861,190	1,736,256	1,655,692
Premises and Equipment, Net	26,565	26,938	26,775
Goodwill	21,873	21,873	21,873
Other Intangible Assets, Net	2,482	2,696	2,885
Other Assets	57,089	56,789	53,198
Total Assets	$2,721,721	$2,605,242	$2,540,242
LIABILITIES			
Noninterest-Bearing Deposits	$433,480	$387,280	$368,378
Interest-Bearing Checking Accounts	905,624	877,988	900,974
Savings Deposits	679,320	651,965	600,513
Time Deposits over $250,000	33,630	32,878	37,297
Other Time Deposits	167,984	166,435	165,223
Total Deposits	2,220,038	2,116,546	2,072,385
Federal Funds Purchased and Securities Sold Under Agreements to Repurchase	40,892	35,836	41,497
Federal Home Loan Bank Overnight Advances	122,000	123,000	102,000
Federal Home Loan Bank Term Advances	55,000	55,000	55,000
Junior Subordinated Obligations Issued to Unconsolidated Subsidiary Trusts	20,000	20,000	20,000
Other Liabilities	23,039	22,008	23,987
Total Liabilities	2,480,969	2,372,390	2,314,869
STOCKHOLDERS' EQUITY			
Preferred Stock, $5 Par Value; 1,000,000 Shares Authorized	—	—	—
Common Stock, $1 Par Value; 20,000,000 Shares Authorized (17,943,201 Shares Issued and Outstanding at June 30, 2017; 17,943,201 at December 31, 2016 and 17,420,776 at June 30, 2016)	17,943	17,943	17,421
Additional Paid-in Capital	272,187	270,880	252,511
Retained Earnings	35,739	28,644	38,852
Unallocated ESOP Shares (19,466 Shares at June 30, 2017; 19,466 Shares at December 31, 2016 and 28,671 Shares at June 30, 2016)	(400)	(400)	(850)
Accumulated Other Comprehensive Loss	(6,200)	(6,834)	(4,742)
	(78,517)	(77,381)	(77,819)

Treasury Stock, at Cost (4,428,713 Shares at June 30, 2017; 4,441,093 Shares at December 31, 2016 and 4,380,736 Shares at June 30, 2016)			
Total Stockholders' Equity	240,752	232,852	225,373
Total Liabilities and Stockholders' Equity	$2,721,721	$2,605,242	$2,540,242

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 June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
INTEREST AND DIVIDEND INCOME				
Interest and Fees on Loans	$17,295	$15,708	$33,697	$30,732
Interest on Deposits at Banks	78	34	138	66
Interest and Dividends on Investment Securities:				
Fully Taxable	2,013	2,018	4,003	4,105
Exempt from Federal Taxes	1,540	1,477	3,085	2,960
Total Interest and Dividend Income	20,926	19,237	40,923	37,863
INTEREST EXPENSE				
Interest-Bearing Checking Accounts	381	311	712	621
Savings Deposits	316	224	607	446
Time Deposits over $250,000	66	49	121	72
Other Time Deposits	233	213	461	446
Federal Funds Purchased and Securities Sold Under Agreements to Repurchase	9	10	16	15
Federal Home Loan Bank Advances	506	314	951	623
Junior Subordinated Obligations Issued to Unconsolidated Subsidiary Trusts	188	163	367	324
Total Interest Expense	1,699	1,284	3,235	2,547
NET INTEREST INCOME	19,227	17,953	37,688	35,316
Provision for Loan Losses	422	669	780	1,070
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	18,805	17,284	36,908	34,246
NONINTEREST INCOME				
Income From Fiduciary Activities	2,150	2,000	4,168	3,931
Fees for Other Services to Customers	2,413	2,417	4,670	4,654
Insurance Commissions	2,115	2,133	4,313	4,341
Net Gain on Securities Transactions	—	144	—	144
Net Gain on Sales of Loans	204	159	250	338
Other Operating Income	175	341	351	662
Total Noninterest Income	7,057	7,194	13,752	14,070
NONINTEREST EXPENSE				
Salaries and Employee Benefits	9,084	8,408	18,092	16,530
Occupancy Expenses, Net	2,494	2,335	5,038	4,798
FDIC Assessments	228	314	454	627
Other Operating Expense	3,831	3,827	7,528	7,300
Total Noninterest Expense	15,637	14,884	31,112	29,255
INCOME BEFORE PROVISION FOR INCOME TAXES	10,225	9,594	19,548	19,061
Provision for Income Taxes	3,017	2,947	5,709	5,865
NET INCOME	$7,208	$6,647	$13,839	$13,196
Average Shares Outstanding [1]:				
Basic	13,485	13,372	13,485	13,357
Diluted	13,568	13,429	13,581	13,405

Per Common Share:				
Basic Earnings	$0.53	$0.50	$1.03	$0.99
Diluted Earnings	0.53	0.49	1.02	0.98

2016 Share and Per Share Amounts have been restated for the September 29, 2016 3% 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 June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Net Income	$7,208	$6,647	$13,839	$13,196
Other Comprehensive Income, Net of Tax:				
Net Unrealized Securities Holding Gains Arising During the Period	409	682	456	3,119
Reclassification Adjustments for Securities Gains Included in Net Income	—	(88)	—	(88)
Amortization of Net Retirement Plan Actuarial Loss	72	102	181	203
Accretion of Net Retirement Plan Prior Service Credit	(1)	(2)	(3)	(4)
Other Comprehensive Income	480	694	634	3,230
Comprehensive Income	$7,688	$7,341	$14,473	$16,426

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 Loss	Treasury Stock	Total
Balance at December 31, 2016	$ 17,943	$ 270,880	$ 28,644	$ (400)	$ (6,834)	$ (77,381)	$ 232,852
Net Income	—	—	13,839	—	—	—	13,839
Other Comprehensive Income	—	—	—	—	634	—	634
Cash Dividends Paid, $.500 per Share	—	—	(6,744)	—	—	—	(6,744)
Stock Options Exercised, Net (33,062 Shares)	—	322	—	—	—	379	701
Shares Issued Under the Directors' Stock Plan (3,927 Shares)	—	84	—	—	—	43	127
Shares Issued Under the Employee Stock Purchase Plan (7,300 Shares)	—	160	—	—	—	82	242
Shares Issued for Dividend Reinvestment Plans (24,999 Shares)	—	569	—	—	—	276	845
Stock-Based Compensation Expense	—	172	—	—	—	—	172
Purchase of Treasury Stock (56,908 Shares)	—	—	—	—	—	(1,916)	(1,916)
Balance at June 30, 2017	$ 17,943	$ 272,187	$ 35,739	$ (400)	$ (6,200)	$ (78,517)	$ 240,752
Balance at December 31, 2015	$ 17,421	$ 250,680	$ 32,139	$ (1,100)	$ (7,972)	$ (77,197)	$ 213,971
Net Income	—	—	13,196	—	—	—	13,196
Other Comprehensive Income	—	—	—	—	3,230	—	3,230
Cash Dividends Paid, $.485 per Share [1]	—	—	(6,483)	—	—	—	(6,483)
Stock Options Exercised, Net (59,711 Shares)	—	732	—	—	—	589	1,321
Shares Issued Under the Directors' Stock Plan (3,522 Shares)	—	69	—	—	—	35	104
Shares Issued Under the Employee Stock Purchase Plan (9,433 Shares)	—	157	—	—	—	93	250
Shares Issued for Dividend Reinvestment Plans (31,275 Shares)	—	565	—	—	—	309	874
Stock-Based Compensation Expense	—	145	—	—	—	—	145
Tax Benefit for Disposition of Stock Options	—	46	—	—	—	—	46
Purchase of Treasury Stock (58,605 Shares)	—	—	—	—	—	(1,648)	(1,648)
	—	117	—	250	—	—	367

Allocation of ESOP Stock (26,604 Shares)							
Balance at June 30, 2016	$ 17,421	$ 252,511	$ 38,852	$ (850)	$ (4,742)	$ (77,819)	$ 225,373

[1] Cash dividends paid per share have been adjusted for the September 29, 2016 3.0% stock dividend.
See Notes to Unaudited Interim Consolidated Financial Statements.

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

	Six Months Ended June 30,	
Cash Flows from Operating Activities:	2017	2016
Net Income	$13,839	$13,196
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Provision for Loan Losses	780	1,070
Depreciation and Amortization	2,988	3,114
Allocation of ESOP Stock	—	367
Net Gains on the Sale of Securities Available-for-Sale	—	(144)
Loans Originated and Held-for-Sale	(7,646)	(12,432)
Proceeds from the Sale of Loans Held-for-Sale	8,118	10,628
Net Gains on the Sale of Loans	(250)	(338)
Net Losses on the Sale of Premises and Equipment, Other Real Estate Owned and Repossessed Assets	122	47
Contributions to Retirement Benefit Plans	(459)	(370)
Deferred Income Tax Benefit	(94)	(403)
Shares Issued Under the Directors' Stock Plan	127	104
Stock-Based Compensation Expense	172	145
Tax Benefit from Exercise of Stock Options	112	—
Net Increase in Other Assets	(559)	(2,719)
Net Increase in Other Liabilities	1,378	2,734
Net Cash Provided By Operating Activities	18,628	14,999
Cash Flows from Investing Activities:		
Proceeds from the Sale of Securities Available-for-Sale	—	10,568
Proceeds from the Maturities and Calls of Securities Available-for-Sale	31,867	43,780
Purchases of Securities Available-for-Sale	(12,324)	(10,920)
Proceeds from the Maturities and Calls of Securities Held-to-Maturity	30,262	33,809
Purchases of Securities Held-to-Maturity	(33,435)	(57,572)
Net Increase in Loans	(126,524)	(97,100)
Proceeds from the Sales of Premises and Equipment, Other Real Estate Owned and Repossessed Assets	539	1,438
Purchase of Premises and Equipment	(867)	(527)
Proceeds from the Sale of a Subsidiary, Net	23	48
Net Decrease in Other Investments	(123)	(1,122)
Net Cash Used By Investing Activities	(110,582)	(77,598)
Cash Flows from Financing Activities:		
Net Increase in Deposits	103,492	41,962
Net (Decrease) Increase in Short-Term Federal Home Loan Bank Borrowings	(1,000)	20,000
Net Decrease in Short-Term Borrowings	5,056	18,324
Purchase of Treasury Stock	(1,916)	(1,648)
Stock Options Exercised, Net	701	1,321
Shares Issued Under the Employee Stock Purchase Plan	242	250
Tax Benefit from Exercise of Stock Options	—	46
Shares Issued for Dividend Reinvestment Plans	845	874
Cash Dividends Paid	(6,744)	(6,483)

Net Cash Provided By Financing Activities	100,676	74,646
Net Increase in Cash and Cash Equivalents	8,722	12,047
Cash and Cash Equivalents at Beginning of Period	57,355	51,068
Cash and Cash Equivalents at End of Period	$66,077	$63,115
Supplemental Disclosures to Statements of Cash Flow Information:		
Interest on Deposits and Borrowings	$3,225	$2,545
Income Taxes	5,629	6,241
Non-cash Investing and Financing Activity:		
Transfer of Loans to Other Real Estate Owned and Repossessed Assets	588	394

See Notes to Unaudited Interim Consolidated Financial Statements.

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 June 30, 2017, December 31, 2016 and June 30, 2016; the results of operations for the three- and six-month periods ended June 30, 2017 and 2016; the consolidated statements of comprehensive income for the three- and six-month periods ended June 30, 2017 and 2016; the changes in stockholders' equity for the six-month periods ended June 30, 2017 and 2016; and the cash flows for the six-month periods ended June 30, 2017 and 2016. All such adjustments are of a normal recurring nature. Certain prior period amounts have been reclassified to conform to the current presentation, including a new requirement to present time deposits with balances greater than $250,000 which were previously presented as balances of $100,000 or greater. 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, 2016, included in Arrow's 2016 Form 10-K.

New Accounting Standards Updates (ASU): Effective January 1, 2017, Arrow adopted FASB accounting standard ASU 2016-09 "Improvements to Employee Share-Based Payment Accounting," which makes several revisions to equity compensation accounting. Under the new guidance all excess tax benefits and deficiencies that occur when an award is exercised or expires are recognized in income tax expense as discrete period items. Previously, these transactions were typically recorded directly within equity. Excess tax benefits are also recognized at the time an award is exercised compared to the previous requirement to delay recognition until the deduction reduces taxes payable. All tax related cash flows recognized on stock-based compensation expense are classified as an operating activity in our consolidated statements of cash flows on a prospective basis. Accordingly, prior periods have not been adjusted. ASU 2016-09 also provides an accounting policy election to recognize forfeitures of awards as they occur when estimating stock-based compensation expense rather than the previous requirement to estimate forfeitures from inception. Further, ASU 2016-09 permits employers to use a net-settlement feature to withhold taxes on equity compensation awards up to the maximum statutory tax rate without affecting the equity classification of the award. Under previous guidance, withholding of equity awards in excess of the minimum statutory requirement resulted in liability classification for the entire award. The related cash remittance by the employer for employee taxes is treated as a financing activity in the statement of cash flows.

The annual effect of the 2017 tax provision will primarily depend upon the share price of Arrow common stock which affects the probability of exercise of certain stock options and the magnitude of windfalls upon exercise. Income tax benefits from stock options exercised in the period reduced our effective tax rate for the six months ended June 30, 2017, which resulted in an increase in earnings of approximately $112 thousand, representing earnings per share of less than $0.01.

In addition, during 2017, through the date of this report, the FASB issued 11 accounting standards updates. Some of the standards listed below did not have an immediate impact on Arrow, but could in the future.

ASU 2014-09 - Revenue from Contracts with Customers will change revenue recognition guidance under GAAP and is based on the principle that revenue is recognized to depict the transfer of goods or services to customers in an amount that reflects consideration to which the entity expects to be entitled in exchange for those goods and services. The ASU also requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. For financial reporting purposes, the standard allows for either full retrospective adoption, meaning the standard is applied to all of the periods presented, or modified retrospective adoption, meaning the standard is applied only to the most current period presented in the financial statements with the cumulative effect of initially applying the standard recognized at the date of initial application.

Initially, ASU 2014-09 was effective for Arrow on January 1, 2017; however, in August 2015, the FASB issued ASU No. 2015-14 - Revenue from Contracts with Customers - Deferral of the Effective Date, which deferred the effective date to January 1, 2018. Early adoption is not permitted. In addition, the FASB has begun to issue targeted updates to clarify specific implementation issues of ASU 2014-09. These updates include ASU No. 2016-08 - Principal versus Agent Considerations (Reporting Revenue Gross versus Net), ASU No. 2016-10 - Identifying Performance Obligations and Licensing, ASU No. 2016-12 - Narrow-Scope Improvements and Practical Expedients, and ASU No. 2016-20 - Technical Corrections and Improvements to Top 606 - Revenue from Contract with Customers. We are currently in the process of identifying and implementing required changes to the timing of our revenue recognition. We do not expect that the adoption of this change in accounting for revenue will have a material impact on our financial position or the results of operations in periods subsequent to its adoption.

ASU 2016-01 "Recognition and Measurement of Financial Assets and Financial Liabilities" will significantly change the income statement impact of equity investments. For Arrow, the standard is effective for the first quarter of 2018, and will require that equity investments be measured at fair value, with changes in fair value measured in net income. As of June 30, 2017, we hold $1.5 million of fair value in equity investments and we do not expect that the adoption of this change in accounting for equity investments will have a material impact on our financial position or the results of operations in periods subsequent to its adoption.

ASU 2016-02 "Leases" will require the recognition of operating leases. For Arrow, the standard becomes effective in the first quarter of 2019. We do not expect that the adoption of this change in accounting for operating leases will have a material impact on our financial position or the results of operations in periods subsequent to its adoption. As of June 30, 2017, we have less than $2.3 million in minimum lease payments for existing operating leases of branch and insurance locations with varying expiration dates from 2017 to 2031.

ASU 2016-13 "Financial Instruments - Credit Losses" will change the way we and other financial entities recognize losses on assets measured at amortized costs and change the method for recognizing credit losses on securities available-for-sale. Currently, loan losses are recognized using an "incurred loss" methodology. Under ASU 2016-13, the methodology will change to a current expected loss over the life of the loan. Currently, credit losses on available-for-sale securities reduce the carrying value of the instrument and cannot be reversed. Under ASU 2016-13, the amount of the credit loss is carried as a valuation allowance and can be reversed. For Arrow, the standard is effective for the first quarter of 2020 and early adoption is allowed in 2019. The Company is currently evaluating the impact of the pending adoption of the ASU on its consolidated financial statements. The initial adjustment will not be reported in earnings, but as the cumulative effect of a change in accounting principle. At this time we have not calculated the estimated impact that this Update will have on our Allowance for Loan Losses, however, we anticipate it will have a significant impact on the methodology process we utilize to calculate the allowance.

ASU 2017-01 "Business Combinations" defines when a set of assets and activities constitutes a business for the purposes of determining whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. Currently, the three elements required to be present in a business are inputs, processes, and outputs. The amendments in this Update allow for a business to consist of inputs, processes, and the ability to create output. For Arrow, the standard becomes effective in the first quarter of 2018. This Update will likely have no effect on our accounting for acquisitions and dispositions of businesses.

ASU 2017-04 "Intangibles-Goodwill and Other" changes the procedures for evaluating impairment of goodwill. Prior to this Update, entities were required to perform procedures to determine the fair value of the underlying assets and liabilities following the guidance for determining the fair value of assets and liabilities in a business combination. This additional step to impairment testing has been eliminated. Under the amendments in this Update, entities should perform goodwill impairment testing by comparing the fair value of a reporting unit to its carrying value. This amendment should reduce the cost and complexity of evaluating goodwill for impairment. For Arrow, the standard becomes effective in the first quarter of 2019, however, early adoption is permitted. This amendment will not affect our assessment of goodwill impairment since we currently perform the analysis of comparing carrying value to fair value of our reporting units that have goodwill and we have not had to perform a Step 2 Impairment Test to date.

ASU 2017-07 "Compensation-Retirement Benefits" improves the presentation of net periodic pension cost and net periodic post-retirement benefit cost by requiring that an employer disaggregate the service cost component from the other components of net benefit cost. The amendments also provide explicit guidance on how to present the service cost component and the other components of net benefit cost in the income statement and allow only the service cost component of net benefit cost to be eligible for capitalization. For Arrow, the standard becomes effective in the first quarter of 2018, however, early adoption is permitted. We do not expect that the adoption of this change in accounting for pension costs will have a material impact on our financial position or the results of operations in periods subsequent to its adoption.

ASU 2017-08 "Receivables-Nonrefundable Fees and Other Costs" amends the amortization period for certain purchased callable debt securities held at a premium. This shortens the amortization period for the premium to the earliest call date. Under current generally accepted accounting principles (GAAP), entities generally amortize the premium as an adjustment of yield over the contractual life of the instrument. For Arrow, the standard becomes effective in the first quarter of 2019, however, early adoption is permitted as early as the first quarter of 2017. We do not expect that the adoption of this change in accounting for certain callable debt securities will have a material impact on our financial position or the results of operations in periods subsequent to its adoption.

ASU 2017-09 "Compensation-Stock Compensation" provides guidance about which changes to the terms and conditions of a share-based payment award require an entity to apply modification accounting in Topic 718. The guidance highlights the requirements for applying modification accounting and the exception criteria relating to changes in share based payment terms. For Arrow, the standard becomes effective in the first quarter of 2018, however, early adoption is permitted as early as the third quarter of 2017. We do not expect that the adoption of this change in accounting for share-based payment awards will have a material impact on our financial position or the results of operations in periods subsequent to its adoption.

Note 2. INVESTMENT SECURITIES (In Thousands)

The following table is the schedule of Available-For-Sale Securities at June 30, 2017, December 31, 2016 and June 30, 2016:
Available-For-Sale Securities

	U.S. Government & 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
June 30, 2017						
Available-For-Sale Securities, at Amortized Cost	$ 146,914	$ 15,410	$ 161,324	$ 2,500	$ 1,120	$ 327,268
Available-For-Sale Securities, at Fair Value	147,085	15,441	161,077	2,299	1,490	327,392
Gross Unrealized Gains	252	31	964	—	370	1,617
Gross Unrealized Losses	81	—	1,211	201	—	1,493
Available-For-Sale Securities, Pledged as Collateral						267,912
Maturities of Debt Securities, at Amortized Cost:						
Within One Year	$ —	$ 5,482	$ 3,842	$ 1,500	$ —	$ 10,824
From 1 - 5 Years	146,914	8,966	105,663	—	—	261,543
From 5 - 10 Years	—	442	51,819	—	—	52,261
Over 10 Years	—	520	—	1,000	—	1,520
Maturities of Debt Securities, at Fair Value:						
Within One Year	$ —	$ 5,483	$ 3,893	$ 1,499	$ —	$ 10,875
From 1 - 5 Years	147,085	8,996	105,638	—	—	261,719
From 5 - 10 Years	—	442	51,546	—	—	51,988
Over 10 Years	—	520	—	800	—	1,320
Securities in a Continuous Loss Position, at Fair Value:						
Less than 12 Months	$ 49,176	$ 543	$ 97,870	$ 1,499	$ —	$ 149,088
12 Months or Longer	—	—	—	800	—	800
Total	$ 49,176	$ 543	$ 97,870	$ 2,299	$ —	$ 149,888
Number of Securities in a Continuous Loss Position	13	2	34	3	—	52
Unrealized Losses on Securities in a Continuous Loss Position:						
Less than 12 Months	$ 81	$ —	$ 1,211	$ 1	$ —	$ 1,293
12 Months or Longer	—	—	—	200	—	200
Total	$ 81	$ —	$ 1,211	$ 201	$ —	$ 1,493

Disaggregated Details:		
US Treasury Obligations, at Amortized Cost	$ 54,597	
US Treasury Obligations, at Fair Value	54,676	
US Agency Obligations, at Amortized Cost	92,317	
US Agency Obligations, at Fair Value	92,409	
US Government Agency Securities, at Amortized Cost		$ 3,740
US Government Agency Securities, at Fair Value		3,756
Government Sponsored Entity Securities, at Amortized Cost		157,584
Government Sponsored Entity Securities, at Fair Value		157,321

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Available-For-Sale Securities

	U.S. Government & 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
December 31, 2016						
Available-For-Sale Securities, at Amortized Cost	$ 147,110	$ 27,684	$ 168,189	$ 3,512	$ 1,120	$ 347,615
Available-For-Sale Securities, at Fair Value	147,377	27,690	167,239	3,308	1,382	346,996
Gross Unrealized Gains	304	24	986	—	262	1,576
Gross Unrealized Losses	37	18	1,936	204	—	2,195
Available-For-Sale Securities, Pledged as Collateral, at Fair Value						262,852
Securities in a Continuous Loss Position, at Fair Value:						
Less than 12 Months	$ 70,605	$ 12,165	$ 126,825	$ 500	$ —	$ 210,095
12 Months or Longer	—	7,377	—	2,809	—	10,186
Total	$ 70,605	$ 19,542	$ 126,825	$ 3,309	$ —	$ 220,281
Number of Securities in a Continuous Loss Position	19	84	40	4	—	147
Unrealized Losses on Securities in a Continuous Loss Position:						
Less than 12 Months	$ 37	$ 13	$ 1,936	$ 1	$ —	$ 1,987
12 Months or Longer	—	5	—	203	—	208
Total	$ 37	$ 18	$ 1,936	$ 204	$ —	$ 2,195
Disaggregated Details:						
US Treasury Obligations, at Amortized Cost	$ 54,701					
US Treasury Obligations, at Fair Value	54,706					
US Agency Obligations, at Amortized Cost	92,409					
US Agency Obligations, at Fair Value	92,671					
US Government Agency Securities, at Amortized Cost			$ 3,694			
US Government Agency Securities, at Fair Value			3,724			
Government Sponsored Entity Securities, at Amortized Cost			164,495			
Government Sponsored Entity Securities, at Fair Value			163,515			

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Available-For-Sale Securities

	U.S. Government & 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
June 30, 2016						
Available-For-Sale Securities, at Amortized Cost	$ 155,859	$ 36,256	$ 157,926	$ 5,749	$ 1,120	$ 356,910
Available-For-Sale Securities, at Fair Value	157,990	36,425	161,728	5,555	1,231	362,929
Gross Unrealized Gains	2,131	169	3,806	6	111	6,223
Gross Unrealized Losses	—	—	4	200	—	204
Available-For-Sale Securities, Pledged as Collateral						267,912
Securities in a Continuous Loss Position, at Fair Value:						
Less than 12 Months	$ —	$ —	$ 710	$ —	$ —	$ 710
12 Months or Longer	—	256	—	2,281	—	2,537
Total	$ —	$ 256	$ 710	$ 2,281	$ —	$ 3,247
Number of Securities in a Continuous Loss Position	—	1	2	3	—	6
Unrealized Losses on Securities in a Continuous Loss Position:						
Less than 12 Months	$ —	$ —	$ 4	$ —	$ —	$ 4
12 Months or Longer	—	—	—	200	—	200
Total	$ —	$ —	$ 4	$ 200	$ —	$ 204
Disaggregated Details:						
US Agency Obligations, at Amortized Cost	$ 155,859					
US Agency Obligations, at Fair Value	157,990					
US Government Agency Securities, at Amortized Cost			$ 10,318			
US Government Agency Securities, at Fair Value			10,401			
Government Sponsored Entity Securities, at Amortized Cost			147,608			
Government Sponsored Entity Securities, at Fair Value			151,327			

The following table is the schedule of Held-To-Maturity Securities at June 30, 2017, December 31, 2016 and June 30, 2016:

Held-To-Maturity Securities

	State and Municipal Obligations	Mortgage-Backed Securities - Residential	Corporate and Other Debt Securities	Total Held-To Maturity Securities
June 30, 2017				
Held-To-Maturity Securities, at Amortized Cost	$ 280,485	$ 67,533	$ —	$ 348,018
Held-To-Maturity Securities, at Fair Value	282,157	68,198	—	350,355
Gross Unrealized Gains	3,208	677	—	3,885
Gross Unrealized Losses	1,536	12	—	1,548
Held-To-Maturity Securities, Pledged as Collateral				327,820
Maturities of Debt Securities, at Amortized Cost:				
Within One Year	$ 13,986	$ —	$ —	$ 13,986
From 1 - 5 Years	91,072	61,506	—	152,578
From 5 - 10 Years	164,161	6,027	—	170,188
Over 10 Years	11,266	—	—	11,266
Maturities of Debt Securities, at Fair Value:				
Within One Year	$ 14,006	$ —	$ —	$ 14,006
From 1 - 5 Years	92,549	62,078	—	154,627
From 5 - 10 Years	164,399	6,120	—	170,519
Over 10 Years	11,203	—	—	11,203
Securities in a Continuous Loss Position, at Fair Value:				
Less than 12 Months	$ 93,046	$ 4,338	$ —	$ 97,384
12 Months or Longer	403	—	—	403
Total	$ 93,449	$ 4,338	$ —	$ 97,787
Number of Securities in a Continuous Loss Position	263	9	—	272
Unrealized Losses on Securities in a Continuous Loss Position:				
Less than 12 Months	$ 1,534	$ 12	$ —	$ 1,546
12 Months or Longer	2	—	—	2
Total	$ 1,536	$ 12	$ —	$ 1,548
Disaggregated Details:				
US Government Agency		$ 3,106		

Securities, at Amortized Cost	
US Government Agency Securities, at Fair Value	3,121
Government Sponsored Entity Securities, at Amortized Cost	64,427
Government Sponsored Entity Securities, at Fair Value	65,077

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Held-To-Maturity Securities

	State and Municipal Obligations	Mortgage-Backed Securities - Residential	Corporate and Other Debt Securities	Total Held-To Maturity Securities
December 31, 2016				
Held-To-Maturity Securities, at Amortized Cost	$ 268,892	$ 75,535	$ 1,000	$ 345,427
Held-To-Maturity Securities, at Fair Value	267,127	75,624	1,000	343,751
Gross Unrealized Gains	2,058	258	—	2,316
Gross Unrealized Losses	3,823	169	—	3,992
Held-To-Maturity Securities, Pledged as Collateral				321,202
Securities in a Continuous Loss Position, at Fair Value:				
Less than 12 Months	$ 107,255	$ 13,306	$ —	$ 120,561
12 Months or Longer	12,363	—	—	12,363
Total	$ 119,618	$ 13,306	$ —	$ 132,924
Number of Securities in a Continuous Loss Position	347	13	—	360
Unrealized Losses on Securities in a Continuous Loss Position:				
Less than 12 Months	$ 3,129	$ 169	$ —	$ 3,298
12 Months or Longer	694	—	—	694
Total	$ 3,823	$ 169	$ —	$ 3,992
Disaggregated Details:				
US Government Agency Securities, at Amortized Cost		$ 3,206		
US Government Agency Securities, at Fair Value		3,222		
Government Sponsored Entity Securities, at Amortized Cost		72,329		
Government Sponsored Entity Securities, at Fair Value		72,402		
June 30, 2016				
Held-To-Maturity Securities, at Amortized Cost	$ 257,982	$ 84,832	$ 1,000	$ 343,814
Held-To-Maturity Securities, at Fair Value	265,983	87,795	1,000	354,778
Gross Unrealized Gains	8,002	2,963	—	10,965
Gross Unrealized Losses	1	—	—	1
Held-To-Maturity Securities, Pledged as Collateral				327,820

Securities in a Continuous Loss Position, at Fair Value:				
Less than 12 Months	$ —	$ —	$ —	$—
12 Months or Longer	659	—	—	659
Total	$ 659	$ —	$ —	$659
Number of Securities in a Continuous Loss Position	3	—	—	3
Unrealized Losses on Securities in a Continuous Loss Position:				
Less than 12 Months	$ —	$ —	$ —	$—
12 Months or Longer	1	—	—	1
Total	$ 1	$ —	$ —	$1

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Held-To-Maturity Securities

	State and Municipal Obligations	Mortgage-Backed Securities - Residential	Corporate and Other Debt Securities	Total Held-To Maturity Securities
June 30, 2016				
Disaggregated Details:				
US Government Agency Securities, at Amortized Cost		$ 3,497		
US Government Agency Securities, at Fair Value		3,622		
Government Sponsored Entity Securities, at Amortized Cost		81,335		
Government Sponsored Entity Securities, at Fair Value		84,173		

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 above because issuers may have the right to call or prepay obligations with, or without, prepayment penalties.

Securities in a continuous loss position, in the tables above for June 30, 2017, December 31, 2016 and June 30, 2016, 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 reflects satisfactory credit worthiness of the municipalities. Corporate and other debt securities continue to be rated above investment grade according to Moody's and Standard and Poor's. Subsequent to June 30, 2017, and through the date of filing this report, 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 June 30, 2017, December 31, 2016 and June 30, 2016 and an analysis of the recorded investment in loans that are past due at these dates. Generally, Arrow considers an amortizing loan past due 30 or more days when the borrower is two payments past due. Loans held-for-sale of $261, $483 and $2,440 as of June 30, 2017, December 31, 2016 and June 30, 2016, respectively, are included in the residential real estate balances for current loans.

	Commercial	Commercial Real Estate	Consumer	Residential	Total
June 30, 2017					
Loans Past Due 30-59 Days	$ 138	$ —	$ 4,123	$ 122	$ 4,383
Loans Past Due 60-89 Days	40	865	1,265	2,591	4,761
Loans Past Due 90 or more Days	249	357	391	2,115	3,112
Total Loans Past Due	427	1,222	5,779	4,828	12,256
Current Loans	125,832	440,587	572,975	726,982	1,866,376
Total Loans	$ 126,259	$ 441,809	$ 578,754	$ 731,810	$ 1,878,632
Loans 90 or More Days Past Due and Still Accruing Interest	$ 120	$ 357	$ 75	$ 1,269	$ 1,821
Nonaccrual Loans	653	1,343	419	2,807	5,222
December 31, 2016					
Loans Past Due 30-59 Days	$ 112	$ 121	$ 5,593	$ 2,368	$ 8,194
Loans Past Due 60-89 Days	29	—	898	142	1,069
Loans Past Due 90 or more Days	148	—	513	1,975	2,636
Total Loans Past Due	289	121	7,004	4,485	11,899
Current Loans	104,866	431,525	530,357	674,621	1,741,369
Total Loans	$ 105,155	$ 431,646	$ 537,361	$ 679,106	$ 1,753,268
Loans 90 or More Days Past Due and Still Accruing Interest	$ —	$ —	$ 158	$ 1,043	$ 1,201
Nonaccrual Loans	$ 155	$ 875	$ 589	$ 2,574	4,193
June 30, 2016					
Loans Past Due 30-59 Days	$ 61	$ —	$ 3,362	$ 101	$ 3,524
Loans Past Due 60-89 Days	25	168	1,393	1,750	3,336
Loans Past Due 90 or more Days	194	938	283	1,780	3,195
Total Loans Past Due	280	1,106	5,038	3,631	10,055
Current Loans	106,371	416,506	503,500	636,058	1,662,435
Total Loans	$ 106,651	$ 417,612	$ 508,538	$ 639,689	$ 1,672,490
Loans 90 or More Days Past Due and Still Accruing Interest	$ —	$ —	$ 53	$ 403	$ 456
Nonaccrual Loans	$ 194	$ 3,525	$ 451	$ 2,535	6,705

The Company disaggregates its loan portfolio into the following four 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 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. However, the Company also offers commercial construction and land development loans to finance projects, primarily within the communities that we serve. Many projects will ultimately be used by the borrowers' businesses, while others are developed for resale. These real estate loans are also secured by first liens on the real estate, which may include apartments, commercial structures, housing business, healthcare facilities and both owner-occupied and non-owner-occupied facilities. There is enhanced risk during the construction period, since the loan is secured by an incomplete project.

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. Also included in this category are automobile loans. 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. 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 an existing 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. It is our general practice to underwrite our residential real estate loans to secondary market standards. 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%, although periodically higher advances are allowed. 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 Real Estate	Consumer	Residential	Unallocated	Total
Roll-forward of the Allowance for Loan Losses for the Quarterly Periods:						

March 31, 2017	$ 939	$ 5,449	$ 6,702	$ 4,126	$ —	$ 17,216
Charge-offs	(23)	—	(277)	(5)	—	(305)
Recoveries	5	—	104	—	—	109
Provision	4	(466)	776	108	—	422
June 30, 2017	$ 925	$ 4,983	$ 7,305	$ 4,229	$ —	$ 17,442
March 31, 2016	$ 1,437	$ 4,950	$ 5,912	$ 3,798	$ 190	$ 16,287
Charge-offs	(11)	—	(189)	—	—	(200)
Recoveries	2	—	40	—	—	42
Provision	(300)	866	(21)	228	(104)	669
June 30, 2016	$ 1,128	$ 5,816	$ 5,742	$ 4,026	$ 86	$ 16,798

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Allowance for Loan Losses

	Commercial	Commercial Real Estate	Consumer	Residential	Unallocated	Total
Roll-forward of the Allowance for Loan Losses for the Year-to-Date Periods:						
December 31, 2016	$ 1,017	$ 5,677	$ 6,120	$ 4,198	$ —	$ 17,012
Charge-offs	(39)	—	(530)	(6)	—	(575)
Recoveries	12	—	213	—	—	225
Provision	(65)	(694)	1,502	37	—	780
June 30, 2017	$ 925	$ 4,983	$ 7,305	$ 4,229	$ —	$ 17,442
December 31, 2015	$ 1,827	$ 4,520	$ 5,554	$ 3,790	$ 347	$ 16,038
Charge-offs	(52)	—	(349)	(16)	—	(417)
Recoveries	15	—	92	—	—	107
Provision	(662)	1,296	445	252	(261)	1,070
June 30, 2016	$ 1,128	$ 5,816	$ 5,742	$ 4,026	$ 86	$ 16,798
June 30, 2017						
Allowance for loan losses - Loans Individually Evaluated for Impairment	$ 112	$ —	$ —	$ 34	$ —	$ 146
Allowance for loan losses - Loans Collectively Evaluated for Impairment	813	4,983	7,305	4,195	—	17,296
Ending Loan Balance - Individually Evaluated for Impairment	503	1,178	88	1,090	—	2,859
Ending Loan Balance - Collectively Evaluated for Impairment	$ 125,756	$ 440,631	$ 578,666	$ 730,720	$ —	$ 1,875,773
December 31, 2016						
Allowance for loan losses - Loans Individually Evaluated for Impairment	$ —	$ —	$ —	$ —	$ —	$ —
Allowance for loan losses - Loans Collectively Evaluated for Impairment	1,017	5,677	6,120	4,198	—	17,012
Ending Loan Balance - Individually Evaluated for Impairment	—	890	91	1,098	—	2,079
Ending Loan Balance - Collectively Evaluated for Impairment	$ 105,155	$ 430,756	$ 537,270	$ 678,008	$ —	$ 1,751,189
June 30, 2016						
Allowance for loan losses - Loans Individually Evaluated for Impairment	$ —	$ 250	$ —	$ —	$ —	$ 250
Allowance for loan losses - Loans Collectively Evaluated for Impairment	1,128	5,566	5,742	4,026	86	16,548
Ending Loan Balance - Individually Evaluated for Impairment	—	3,542	93	640	—	4,275
Ending Loan Balance - Collectively Evaluated for Impairment	$ 106,651	$ 414,070	$ 508,445	$ 639,049	$ —	$ 1,668,215

Through the provision for loan losses, an allowance for loan losses is maintained that reflects our best estimate of the inherent risk of loss in the Company's loan portfolio as of the balance sheet date. Additions are made to the allowance for loan losses through a periodic provision for loan losses. Actual loan losses are charged against the allowance for loan losses when loans are deemed uncollectible and recoveries of amounts previously charged off are recorded as credits to the allowance for loan losses.

Our loan officers and risk managers meet at least quarterly to discuss and review the conditions and risks associated with certain criticized and classified commercial-related relationships. In addition, our independent internal loan review department performs periodic reviews of the risk ratings on individual loans in our commercial loan portfolio.

We use a two-step process to determine the provision for loan losses and the amount of the allowance for loan losses. We measure impairment on our impaired loans on a quarterly basis. Our impaired loans are generally nonaccrual loans over $250 thousand and all troubled debt restructured loans. Our impaired loans are generally considered to be collateral dependent with the specific reserve, if any, determined based on the value of the collateral less estimated costs to sell.

The remainder of the portfolio is evaluated on a pooled basis. For each homogeneous loan pool, we estimate a total loss factor based on the historical net loss rates adjusted for applicable qualitative factors. We update the total loss factors assigned to each loan category on a quarterly basis. For the commercial and commercial real estate categories, we further segregate the loan categories by credit risk profile (pools of loans graded satisfactory, special mention and substandard). Additional description of the credit risk classifications is detailed in the Credit Quality Indicators section of this note.

We determine the annualized historical net loss rate for each loan category using a trailing three-year net charge-off average. We then apply a loss emergence period factor to the historical net loss rate to account for the time it takes to identify the loss after a loss-causing event. While historical net loss experience provides a reasonable starting point for our analysis, historical net losses, or even recent trends in net losses, do not by themselves form a sufficient basis to determine the appropriate level of the allowance for loan losses. Therefore, we also consider and adjust historical net loss factors for qualitative factors that impact the inherent risk of loss associated with our loan categories within our total loan portfolio. These include:

- 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

While not a significant part of the allowance for loan losses methodology, in 2016, we maintained an unallocated portion of the total allowance for loan losses related to the overall level of imprecision inherent in the estimation of the appropriate level of allowance for loan losses.

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Credit Quality Indicators

The following table presents the credit quality indicators by loan category at June 30, 2017, December 31, 2016 and June 30, 2016:
Loan Credit Quality Indicators

	Commercial	Commercial Real Estate	Consumer	Residential	Total
June 30, 2017					
Credit Risk Profile by Creditworthiness Category:					
Satisfactory	$ 120,388	$ 412,423			$532,811
Special Mention	1,269	1,414			2,683
Substandard	4,602	27,973			32,575
Doubtful	—	—			—
Credit Risk Profile Based on Payment Activity:					
Performing			$578,317	$ 727,733	$1,306,050
Nonperforming			437	4,076	4,513
December 31, 2016					
Credit Risk Profile by Creditworthiness Category:					
Satisfactory	$ 95,722	$ 396,907			$492,629
Special Mention	1,359	7,008			8,367
Substandard	8,074	27,731			35,805
Doubtful	—	—			—
Credit Risk Profile Based on Payment Activity:					
Performing			$536,614	$ 675,489	$1,212,103
Nonperforming			747	3,617	4,364
June 30, 2016					
Credit Risk Profile by Creditworthiness Category:					
Satisfactory	$ 96,703	$ 377,039			$473,742
Special Mention	1,290	10,429			11,719
Substandard	8,658	30,144			38,802
Doubtful	—	—			—
Credit Risk Profile Based on Payment Activity:					
Performing			$508,014	$ 636,751	$1,144,765
Nonperforming			524	2,938	3,462

We use an internally developed system of five credit quality indicators to rate the credit worthiness of each commercial loan defined as follows: 1) Satisfactory - "Satisfactory" borrowers have acceptable financial condition with satisfactory record of earnings and sufficient historical and projected cash flow to service the debt. Borrowers have satisfactory repayment histories and primary and secondary sources of repayment can be clearly identified; 2) Special Mention - Loans in this category have potential weaknesses that deserve management’s close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in the institution’s credit position at some future date. "Special mention" assets are not adversely classified and do not expose an institution to sufficient risk to warrant adverse classification. Loans which might be assigned this risk rating include loans to borrowers with deteriorating financial strength and/or earnings record and loans with potential for problems due to weakening economic or market conditions; 3) Substandard - Loans classified as “substandard” are inadequately protected by the current sound net worth or paying capacity of the borrower or the collateral pledged, if any. Loans in this category have well defined weaknesses that jeopardize the repayment. They are characterized by the distinct possibility that the bank will sustain some loss if the deficiencies are not corrected. “Substandard” loans may include loans which are likely to require liquidation of collateral to effect repayment, and other loans where character or ability to repay has become suspect. Loss potential, while existing in the aggregate amount of substandard assets, does not have to exist in individual assets classified substandard; 4) Doubtful - Loans classified as “doubtful” have all of the weaknesses inherent in those classified as “substandard” with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of current existing facts, conditions, and values highly questionable and improbable. Although possibility of loss is extremely high, classification of these loans as “loss” has been deferred due to specific pending factors or events which may strengthen the value (i.e. possibility of additional collateral, injection of capital, collateral liquidation, debt restructure, economic recovery, etc). Loans classified as “doubtful” need to be placed on

non-accrual; and 5) Loss - Loans classified as “loss” are considered uncollectible and of such little value that their continuance as bankable assets is not warranted. As of the date of the balance sheet, all loans in this category have been charged-off to the allowance for loan losses. Large commercial loans are evaluated on an annual basis, unless the credit quality indicator falls to a level of "special mention" or below, when the loan is evaluated quarterly. The credit quality indicator is one of the factors used to determine any loss, as further described in this footnote.
For the purposes of the table above, nonperforming consumer and residential loans are those loans on nonaccrual status or are 90 days or more past due and still accruing interest.

Impaired Loans

The following table presents information on impaired loans based on whether the impaired loan has a recorded related allowance or has no recorded related allowance:
Impaired Loans

	Commercial	Commercial Real Estate	Consumer	Residential	Total
June 30, 2017					
Recorded Investment:					
With No Related Allowance	$ —	$ 1,178	$ 88	$ 802	$2,068
With a Related Allowance	503	—	—	288	791
Unpaid Principal Balance:					
With No Related Allowance	—	1,178	88	802	2,068
With a Related Allowance	503	—	—	288	791
December 31, 2016					
Recorded Investment:					
With No Related Allowance	$ —	$ 890	$ 91	$ 1,098	$2,079
With a Related Allowance	—	—	—	—	—
Unpaid Principal Balance:					
With No Related Allowance	—	890	91	1,098	2,079
With a Related Allowance	—	—	—	—	—
June 30, 2016					
Recorded Investment:					
With No Related Allowance	$ —	$ 1,850	$ 93	$ 640	$2,583
With a Related Allowance	—	1,692	—	—	1,692
Unpaid Principal Balance:					
With No Related Allowance	—	1,850	93	640	$2,583
With a Related Allowance	—	1,692	—	—	1,692
For the Quarter Ended:					
June 30, 2017					
Average Recorded Balance:					
With No Related Allowance	$ —	$ 1,031	$ 88	$ 804	$1,923
With a Related Allowance	252	—	—	288	540
Interest Income Recognized:					
With No Related Allowance	—	—	2	4	6
With a Related Allowance	—	—	—	—	—
Cash Basis Income:					
With No Related Allowance	—	—	—	—	—

With a Related Allowance	—	—	—	—	—
June 30, 2016					
Average Recorded Balance:					
With No Related Allowance	$ —	$ 2,111	$ 106	$ 641	$2,858
With a Related Allowance	—	1,698	—	—	1,698
Interest Income Recognized:					
With No Related Allowance	—	2	1	—	3
With a Related Allowance	—	—	—	—	—
Cash Basis Income:					
With No Related Allowance	—	—	—	—	—
With a Related Allowance	—	—	—	—	—

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Impaired Loans

	Commercial	Commercial Real Estate	Consumer	Residential	Total
For the Year-To-Date Period Ended:					
June 30, 2017					
Average Recorded Balance:					
With No Related Allowance	$ —	$ 1,034	$ 90	$ 950	$2,074
With a Related Allowance	252	—	—	144	396
Interest Income Recognized:					
With No Related Allowance	—	—	3	4	7
With a Related Allowance	—	—	—	—	—
Cash Basis Income:					
With No Related Allowance	—	—	—	—	—
With a Related Allowance	—	—	—	—	—
June 30, 2016					
Average Recorded Balance:					
With No Related Allowance	$ 78	$ 2,111	$ 104	$ 643	$2,936
With a Related Allowance	—	846	—	—	846
Interest Income Recognized:					
With No Related Allowance	—	11	2	—	13
With a Related Allowance	—	—	—	—	—
Cash Basis Income:					
With No Related Allowance	—	—	—	—	—
With a Related Allowance	—	—	—	—	—

At June 30, 2017, December 31, 2016 and June 30, 2016, all impaired loans were considered to be collateral dependent and were therefore evaluated for impairment based on the fair value of collateral less estimated cost to sell. Interest income recognized in the table above, represents income earned after the loans became impaired and includes restructured loans in compliance with their modified terms and nonaccrual loans where we have recognized interest income on a cash basis.

Loans Modified in Trouble Debt Restructurings

The following table presents information on loans modified in trouble debt restructurings during the periods indicated. All loans were modified under Arrow's own programs. The principal modification, for all the modifications in the table below, involved payment deferrals.

Loans Modified in Trouble Debt Restructurings During the Period

	Commercial	Commercial Real Estate	Consumer	Residential	Total
For the Quarter Ended:					
June 30, 2017					
Number of Loans	1	—	2	—	3
Pre-Modification Outstanding Recorded Investment	$ 503	$ —	$ 10	$ —	$ 513
Post-Modification Outstanding Recorded Investment	503	—	10	—	513
Subsequent Default, Number of Contracts	—	—	—	—	—
Subsequent Default, Recorded Investment	—	—	—	—	—
June 30, 2016					
Number of Loans	—	—	1	—	1
Pre-Modification Outstanding Recorded Investment	$ —	$ —	$ 8	$ —	$ 8
Post-Modification Outstanding Recorded Investment	—	—	8	—	8
Subsequent Default, Number of Contracts	—	—	—	—	—
Subsequent Default, Recorded Investment	—	—	—	—	—
For the Year-To-Date Period Ended:					
June 30, 2017					
Number of Loans	1	—	4	—	5
Pre-Modification Outstanding Recorded Investment	$ 503	$ —	$ 26	$ —	$ 529
Post-Modification Outstanding Recorded Investment	503	—	26	—	529
Subsequent Default, Number of Contracts	—	—	—	—	—
Subsequent Default, Recorded Investment	—	—	—	—	—
June 30, 2016					
Number of Loans	—	—	1	—	1
Pre-Modification Outstanding Recorded Investment	$ —	$ —	$ 8	$ —	$ 8
Post-Modification Outstanding Recorded Investment	—	—	8	—	8
Subsequent Default, Number of Contracts	—	—	—	—	—
Subsequent Default, Recorded Investment	—	—	—	—	—

In general, loans requiring modification are restructured to accommodate the projected cashflows of the borrower. No loans modified during the preceding twelve months subsequently defaulted as of June 30, 2017. In addition, no commitments have been made to extend credit to borrowers whose loans have been modified in a troubled debt restructuring.

Note 4. GUARANTEES (In Thousands)

The following table presents the balance for commitments to extend credit and standby letters of credit for the periods ended June 30, 2017, December 31, 2016 and June 30, 2016:

Commitments to Extend Credit and Letters of Credit

	June 30, 2017	December 31, 2016	June 30, 2016
Notional Amount:			
Commitments to Extend Credit	$290,818	$ 296,442	$292,839
Standby Letters of Credit	3,373	3,445	3,137
Fair Value:			
Commitments to Extend Credit	$—	$ —	$—
Standby Letters of Credit	25	30	24

Arrow is party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. Commitments to extend credit include home equity lines of credit, commitments for residential and commercial construction loans and other personal and commercial lines of credit. These instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheets. The contract or notional amounts of those instruments reflect the extent of the involvement Arrow has in particular classes of financial instruments.

Arrow's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual notional amount of those instruments. Arrow uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Arrow evaluates each customer's creditworthiness on a case-by-case basis. Home equity lines of credit are secured by residential real estate. Construction commitments are secured by underlying real estate. For other lines of credit, the amount of collateral obtained, if deemed necessary by Arrow upon extension of credit, is based on management's credit evaluation of the counterparty. Collateral held varies, but may include accounts receivable, inventory, property, plant and equipment, and income-producing commercial properties. Most of the commitments are variable rate instruments.

Arrow has issued conditional commitments in the form of standby letters of credit to guarantee payment on behalf of a customer and guarantee the performance of a customer to a third party. Standby letters of credit generally arise in connection with lending relationships. The credit risk involved in issuing these instruments is essentially the same as that involved in extending loans to customers. Contingent obligations under standby letters of credit at June 30, 2017, December 31, 2016 and June 30, 2016 represent the maximum potential future payments Arrow could be required to make. Typically, these instruments have terms of 12 months or less and expire unused; therefore, the total amounts do not necessarily represent future cash requirements. Each customer is evaluated individually for creditworthiness under the same underwriting standards used for commitments to extend credit and on-balance sheet instruments. Company policies governing loan collateral apply to standby letters of credit at the time of credit extension. Loan-to-value ratios generally range from 50% for movable assets, such as inventory, to 100% for liquid assets, such as bank CD's. Fees for standby letters of credit typically range from 1% to 3% of the notional amount. Fees are collected upfront and are amortized over the life of the commitment. The fair values of Arrow's standby letters of credit at June 30, 2017, December 31, 2016 and June 30, 2016, in the table above, were the same as the carrying amounts. The fair value of standby letters of credit is based on the fees currently charged for similar agreements or the cost to terminate the arrangement with the counterparties.

The fair value of commitments to extend credit is determined by estimating the fees to enter into similar agreements, taking into account the remaining terms and present creditworthiness of the counterparties, and for fixed rate loan commitments, the difference between the current and committed interest rates. Arrow provides several types of commercial lines of credit and standby letters of credit to its commercial customers. The pricing of these services is not isolated, as Arrow considers the customer's complete deposit and borrowing relationship in pricing individual products and services. The commitments to extend credit also include commitments under home equity lines of credit, for which Arrow charges no fee. The carrying value and fair value of commitments to extend credit are not material and Arrow does not expect to incur any material loss as a result of these commitments.

Note 5. COMPREHENSIVE INCOME (In Thousands)

The following table presents the components of other comprehensive income for the three-month period ended June 30, 2017 and 2016:

Schedule of Comprehensive Income

	Three Months Ended June 30,			Six Months Ended June 30,		
	Before-Tax Amount	Tax (Expense) Benefit	Net-of-Tax Amount	Before-Tax Amount	Tax (Expense) Benefit	Net-of-Tax Amount
2017						
Net Unrealized Securities Holding (Losses) Gains Arising During the Period	$666	$ (257)	$ 409	$743	$(287)	$ 456
Amortization of Net Retirement Plan Actuarial Loss	181	(109)	72	359	(178)	181
Accretion of Net Retirement Plan Prior Service Credit	(3)	2	(1)	(6)	3	(3)
Other Comprehensive Income	$844	$ (364)	$ 480	$1,096	$(462)	$ 634
2016						
Net Unrealized Securities Holding Gains (Losses) Arising During the Period	$1,123	$ (441)	$ 682	$5,132	$(2,013)	$ 3,119
Reclassification Adjustment for Securities Gains Included in Net Income	(144)	56	(88)	(144)	56	(88)
Amortization of Net Retirement Plan Actuarial Loss	168	(66)	102	334	(131)	203
Accretion of Net Retirement Plan Prior Service Credit	(4)	2	(2)	(7)	3	(4)
Other Comprehensive Income	$1,143	$ (449)	$ 694	$5,315	$(2,085)	$ 3,230

The following table presents the changes in accumulated other comprehensive income by component:
Changes in Accumulated Other Comprehensive Income (Loss) by Component [(1)]

	Unrealized Gains and Losses on Available-for-Sale Securities	Defined Benefit Plan Items Net Gain (Loss)	Defined Benefit Plan Items Net Prior Service (Cost) Credit	Total
For the Quarter-To-Date periods ended:				
March 31, 2017	$ (335)	$(5,628)	$(717)	$(6,680)
Other comprehensive income or loss before reclassifications	409	—	—	409
Amounts reclassified from accumulated other comprehensive income	—	72	(1)	71
Net current-period other comprehensive income	409	72	(1)	480
June 30, 2017	$ 74	$(5,556)	$(718)	$(6,200)
March 31, 2016	$ 3,066	$(7,792)	$(710)	$(5,436)
Other comprehensive income or loss before reclassifications	682	—	—	682
Amounts reclassified from accumulated other comprehensive income	(88)	102	(2)	12
Net current-period other comprehensive income	594	102	(2)	694
June 30, 2016	$ 3,660	$(7,690)	$(712)	$(4,742)
For the Year-To-Date periods ended:				
December 31, 2016	$ (382)	$(5,737)	$(715)	$(6,834)
Other comprehensive income or loss before reclassifications	456	—	—	456
Amounts reclassified from accumulated other comprehensive income	—	181	(3)	178
Net current-period other comprehensive income	456	181	(3)	634
June 30, 2017	$ 74	$(5,556)	$(718)	$(6,200)
December 31, 2015	$ 629	$(7,893)	$(708)	$(7,972)
Other comprehensive income or loss before reclassifications	3,119	—	—	3,119
Amounts reclassified from accumulated other comprehensive income	(88)	203	(4)	111
Net current-period other comprehensive income	3,031	203	(4)	3,230
June 30, 2016	$ 3,660	$(7,690)	$(712)	$(4,742)

(1) All amounts are net of tax. Amounts in parentheses indicate debits.

The following table presents the reclassifications out of accumulated other comprehensive income:
Reclassifications Out of Accumulated Other Comprehensive Income [1]

Details about Accumulated Other Comprehensive Income (Loss) Components	Amounts Reclassified from Accumulated Other Comprehensive Income		Affected Line Item in the Statement Where Net Income Is Presented
For the Quarter-to-date periods ended:			
June 30, 2017			
Unrealized gains and losses on available-for-sale securities	$ —		Gain on Securities Transactions
	—		Total before Tax
	—		Provision for Income Taxes
	$ —		Net of Tax
Amortization of defined benefit pension items:			
Prior-service costs	$ 3	(2)	Salaries and Employee Benefits
Actuarial gains/(losses)	(181)	(2)	Salaries and Employee Benefits
	(178)		Total before Tax
	107		Provision for Income Taxes
	$ (71)		Net of Tax
Total reclassifications for the period	$ (71)		Net of Tax
June 30, 2016			
Unrealized gains and losses on available-for-sale securities	$ 144		Gain on Securities Transactions
	144		Total before Tax
	(56)		Provision for Income Taxes
	$ 88		Net of Tax
Amortization of defined benefit pension items:			
Prior-service costs	$ 4	(2)	Salaries and Employee Benefits
Actuarial gains/(losses)	(168)	(2)	Salaries and Employee Benefits
	(164)		Total before Tax
	64		Provision for Income Taxes
	$ (100)		Net of Tax
Total reclassifications for the period	$ (12)		Net of Tax
For the Year-to-date periods ended:			
June 30, 2017			
Unrealized gains and losses on available-for-sale securities	$ —		Gain on Securities Transactions
	—		Total before Tax

	—		Provision for Income Taxes
	$ —		Net of Tax
Amortization of defined benefit pension items:			
Prior-service costs	$ 6	(2)	Salaries and Employee Benefits
Actuarial gains/(losses)	(359)	(2)	Salaries and Employee Benefits
	(353)		Total before Tax
	175		Provision for Income Taxes
	$ (178)		Net of Tax
Total reclassifications for the period	$ (178)		Net of Tax

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Reclassifications Out of Accumulated Other Comprehensive Income [1]

Details about Accumulated Other Comprehensive Income (Loss) Components	Amounts Reclassified from Accumulated Other Comprehensive Income		Affected Line Item in the Statement Where Net Income Is Presented
June 30, 2016			
Unrealized gains and losses on available-for-sale securities	$ 144		Gain on Securities Transactions
	144		Total before Tax
	(56)		Provision for Income Taxes
	$ 88		Net of Tax
Amortization of defined benefit pension items:			
Prior-service costs	7	(2)	Salaries and Employee Benefits
Actuarial gains/(losses)	$ (334)	(2)	Salaries and Employee Benefits
	(327)		Total before Tax
	128		Provision for Income Taxes
	$ (199)		Net of Tax
Total reclassifications for the period	$ (111)		Net of Tax

(1) Amounts in parentheses indicate debits to profit/loss.
(2) These accumulated other comprehensive income components are included in the computation of net periodic pension cost.

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Note 6. STOCK BASED COMPENSATION PLANS

Under our 2013 Long-Term Incentive Plan, we granted options in the first quarter of 2017 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 following table presents a roll-forward of our stock option plans and grants issued during 2017:
Schedule of Share-based Compensation Arrangements

	Stock Option Plans	
Roll-Forward of Shares Outstanding:		
Outstanding at January 1, 2017	355,651	
Granted	54,000	
Exercised	(33,062)	
Forfeited	—	
Outstanding at June 30, 2017	376,589	
Exercisable at Period-End	237,443	
Vested and Expected to Vest	139,146	
Roll-Forward of Shares Outstanding - Weighted Average Exercise Price:		
Outstanding at January 1, 2017	$22.52	
Granted	37.20	
Exercised	21.22	
Forfeited	—	
Outstanding at June 30, 2017	24.74	
Exercisable at Period-End	21.96	
Vested and Expected to Vest	29.49	
Grants Issued During 2017 - Weighted Average Information:		
Fair Value	$6.44	
Fair Value Assumptions:		
Dividend Yield	2.72	%
Expected Volatility	21.40	%
Risk Free Interest Rate	2.25	%
Expected Lives (in years)	6.88	

The following table presents information on the amounts expensed for the periods ended June 30, 2017 and 2016:
Share-Based Compensation Expense

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2017	2016	2017	2016
Share-Based Compensation Expense	$89	$71	$172	$145

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.

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Note 7. RETIREMENT PLANS (Dollars in Thousands)

The following tables provide the components of net periodic benefit costs for the three and six-month periods ended June 30, 2017 and 2016.

	Employees' Pension Plan	Select Executive Retirement Plan	Postretirement Benefit Plans
Net Periodic Benefit Cost			
For the Three Months Ended June 30, 2017:			
Service Cost	$ 350	$ 10	$ 37
Interest Cost	373	59	63
Expected Return on Plan Assets	(800)	—	—
Amortization of Prior Service (Credit) Cost	(14)	14	(3)
Amortization of Net Loss	148	33	—
Net Periodic Benefit Cost	$ 57	$ 116	$ 97