

ARROW FINANCIAL CORP  
Form 10-Q  
May 09, 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 March 31, 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 April 30, 2013
Common Stock, par value \$1.00 per share	12,107,397

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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)

	March 31, 2013	December 31, 2012	March 31, 2012
<b>ASSETS</b>			
Cash and Due From Banks	\$23,943	\$37,076	\$31,128
Interest-Bearing Deposits at Banks	113,231	11,756	106,380
Investment Securities:			
Available-for-Sale	478,775	478,698	466,785
Held-to-Maturity (Approximate Fair Value of \$259,562 at March 31, 2013, \$248,252 at December 31, 2012, and \$207,779 at March 31, 2012)	251,456	239,803	200,607
Federal Home Loan Bank and Federal Reserve Bank Stock	4,493	5,792	4,382
Loans	1,164,759	1,172,341	1,137,547
Allowance for Loan Losses	(14,603)	(15,298)	(15,053)
Net Loans	1,150,156	1,157,043	1,122,494
Premises and Equipment, Net	29,363	28,897	23,217
Other Real Estate and Repossessed Assets, Net	1,194	1,034	555
Goodwill	22,003	22,003	22,003
Other Intangible Assets, Net	4,457	4,492	4,650
Accrued Interest Receivable	6,481	5,486	6,380
Other Assets	30,410	30,716	31,788
Total Assets	\$2,115,962	\$2,022,796	\$2,020,369
<b>LIABILITIES</b>			
Noninterest-Bearing Deposits	\$254,308	\$247,232	\$230,289
NOW Accounts	845,531	758,287	758,114
Savings Deposits	476,115	442,363	432,854
Time Deposits of \$100,000 or More	89,797	93,375	115,161
Other Time Deposits	185,455	189,898	224,460
Total Deposits	1,851,206	1,731,155	1,760,878
Federal Funds Purchased and Securities Sold Under Agreements to Repurchase	12,166	12,678	16,652
Federal Home Loan Bank Overnight Advances	—	29,000	—
Federal Home Loan Bank Term Advances	30,000	30,000	30,000
Junior Subordinated Obligations Issued to Unconsolidated Subsidiary Trusts	20,000	20,000	20,000
Accrued Interest Payable	523	584	974
Other Liabilities	24,264	23,554	23,399
Total Liabilities	1,938,159	1,846,971	1,851,903
<b>STOCKHOLDERS' EQUITY</b>			
Preferred Stock, \$5 Par Value; 1,000,000 Shares Authorized	—	—	—
Common Stock, \$1 Par Value; 20,000,000 Shares Authorized (16,416,163 Shares Issued at March 31, 2013 and December 31, 2012 and	16,416	16,416	16,094

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16,094,277 Shares Issued at March 31, 2012)			
Additional Paid-in Capital	219,178	218,650	208,808
Retained Earnings	28,423	26,251	26,291
Unallocated ESOP Shares (95,172 Shares at March 31, 2013, 102,890 Shares at December 31, 2012 and 109,939 Shares at March 31, 2012)	(2,000 )	(2,150 )	(2,350 )
Accumulated Other Comprehensive Loss	(8,324 )	(8,462 )	(6,872 )
Treasury Stock, at Cost (4,310,578 Shares at March 31, 2013, 4,288,617 Shares at December 31, 2012, and 4,223,687 Shares at March 31, 2012)	(75,890 )	(74,880 )	(73,505 )
Total Stockholders' Equity	177,803	175,825	168,466
Total Liabilities and Stockholders' Equity	\$2,115,962	\$2,022,796	\$2,020,369
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 March	
	31,	
	2013	2012
<b>INTEREST AND DIVIDEND INCOME</b>		
Interest and Fees on Loans	\$12,783	\$13,958
Interest on Deposits at Banks	27	21
Interest and Dividends on Investment Securities:		
Fully Taxable	1,796	2,638
Exempt from Federal Taxes	1,390	1,321
Total Interest and Dividend Income	15,996	17,938
<b>INTEREST EXPENSE</b>		
NOW Accounts	778	1,059
Savings Deposits	268	357
Time Deposits of \$100,000 or More	319	608
Other Time Deposits	554	1,146
Federal Funds Purchased and Securities Sold Under Agreements to Repurchase	3	6
Federal Home Loan Bank Advances	173	197
Junior Subordinated Obligations Issued to Unconsolidated Subsidiary Trusts	144	159
Total Interest Expense	2,239	3,532
NET INTEREST INCOME	13,757	14,406
Provision for Loan Losses	100	280
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	13,657	14,126
<b>NONINTEREST INCOME</b>		
Income From Fiduciary Activities	1,574	1,622
Fees for Other Services to Customers	2,282	1,960
Insurance Commissions	2,028	1,889
Gain on Securities Transactions	527	502
Net Gain on Sales of Loans	607	357
Other Operating Income	156	229
Total Noninterest Income	7,174	6,559
<b>NONINTEREST EXPENSE</b>		
Salaries and Employee Benefits	7,621	7,903
Occupancy Expenses, Net	2,276	2,024
FDIC Assessments	264	255
Other Operating Expense	3,250	2,964
Total Noninterest Expense	13,411	13,146
INCOME BEFORE PROVISION FOR INCOME TAXES	7,420	7,539
Provision for Income Taxes	2,239	2,251
NET INCOME	\$5,181	\$5,288
Average Shares Outstanding:		
Basic	12,031	12,005

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Diluted	12,049	12,030
Per Common Share:		
Basic Earnings	\$0.43	\$0.44
Diluted Earnings	0.43	0.44

Share and Per Share Amounts have been restated for the September 2012 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 March 31,	
	2013	2012
Net Income	\$5,181	\$5,288
Other Comprehensive Income (Loss), Net of Tax:		
Net Unrealized Securities Holding Gains Arising		
During the Period	220	(98 )
Reclassification Adjustment for Securities Gains		
Included in Net Income	(318 )	(303 )
Amortization of Net Retirement Plan Actuarial Loss	236	228
Accretion of Net Retirement Plan Prior Service Credit	—	(4 )
Other Comprehensive Income (Loss)	138	(177 )
Comprehensive Income	\$5,319	\$5,111

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	—	—	5,181	—	—	—	5,181
Other Comprehensive (Loss) Income	—	—	—	—	138	—	138
Cash Dividends Paid, \$.25 per Share <sup>1</sup>	—	—	(3,009 )	—	—	—	(3,009 )
Stock Options Exercised (23,434 Shares)	—	259	—	—	—	231	490
Shares Issued Under the Directors' Stock Plan (396 Shares)	—	6	—	—	—	4	10
Shares Issued Under the Employee Stock Purchase Plan (4,683 Shares)	—	64	—	—	—	46	110
Stock-Based Compensation Expense	—	97	—	—	—	—	97
Tax Benefit for Disposition of Stock Options	—	8	—	—	—	—	8
Purchase of Treasury Stock (54,231 Shares)	—	—	—	—	—	(1,328 )	(1,328 )
Acquisition of Subsidiaries (3,757 Shares)	—	54	—	—	—	37	91
Allocation of ESOP Stock (7,718 Shares)	—	40	—	150	—	—	190
Balance at March 31, 2013	\$ 16,416	\$ 219,178	\$ 28,423	\$ (2,000 )	\$ (8,324 )	\$(75,890 )	\$ 177,803
Balance at December 31, 2011	\$ 16,094	\$ 207,600	\$ 23,947	\$ (2,500 )	\$ (6,695 )	\$(72,061 )	\$ 166,385
Net Income	—	—	5,288	—	—	—	5,288
Other Comprehensive (Loss) Income	—	—	—	—	(177 )	—	(177 )
Cash Dividends Paid, \$.245 per Share <sup>1</sup>	—	—	(2,944 )	—	—	—	(2,944 )
Stock Options Exercised (52,502 Shares)	—	627	—	—	—	522	1,149
Shares Issued Under the Employee Stock Purchase Plan (4,542 Shares)	—	62	—	—	—	45	107

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Shares Issued for Dividend							
Reinvestment Plans (19,032 Shares)	—	275	—	—	—	189	464
Stock-Based Compensation Expense	—	99	—	—	—	—	99
Tax Benefit for Disposition of Stock Options	—	53	—	—	—	—	53
Purchase of Treasury Stock (90,017 Shares)	—	—	—	—	—	(2,237 )	(2,237 )
Acquisition of Subsidiaries (3,724 Shares)	—	54	—	—	—	37	91
Allocation of ESOP Stock (7,563 Shares)	—	38	—	150	—	—	188
Balance at March 31, 2012	\$16,094	\$208,808	\$26,291	\$ (2,350 )	\$ (6,872 )	\$(73,505 )	\$168,466

<sup>1</sup> Cash dividends paid per share have been adjusted for the September 2012 2% 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)

	Three Months Ended March	
	31,	
	2013	2012
Cash Flows from Operating Activities:		
Net Income	\$5,181	\$5,288
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Provision for Loan Losses	100	280
Depreciation and Amortization	2,373	2,043
Allocation of ESOP Stock	190	188
Gains on the Sale of Securities Available-for-Sale	(527 )	(502 )
Loans Originated and Held-for-Sale	(18,842 )	(10,469 )
Proceeds from the Sale of Loans Held-for-Sale	21,385	10,630
Net Gains on the Sale of Loans	(607 )	(357 )
Net Gains on the Sale of Premises and Equipment, Other Real Estate Owned and Repossessed Assets	105	30
Contributions to Pension Plans	(111 )	(80 )
Deferred Income Tax Expense (Benefit)	358	(288 )
Shares Issued Under the Directors' Stock Plan	10	—
Stock-Based Compensation Expense	97	99
Net (Increase) Decrease in Other Assets	(991 )	1,064
Net Increase in Other Liabilities	926	659
Net Cash Provided By Operating Activities	9,647	8,585
Cash Flows from Investing Activities:		
Proceeds from the Sale of Securities Available-for-Sale	16,261	10,851
Proceeds from the Maturities and Calls of Securities Available-for-Sale	22,846	77,782
Purchases of Securities Available-for-Sale	(39,928 )	(288 )
Proceeds from the Maturities and Calls of Securities Held-to-Maturity	6,815	8,987
Purchases of Securities Held-to-Maturity	(18,930 )	(59,043 )
Net Decrease (Increase) in Loans	4,247	(6,355 )
Proceeds from the Sales of Premises and Equipment, Other Real Estate Owned and Repossessed Assets	341	230
Purchase of Premises and Equipment	(991 )	(1,025 )
Cash Paid for Subsidiaries, Net	(75 )	(75 )
Net Decrease in Other Investments	1,299	2,340
Net Cash (Used In) Provided By Investing Activities	(8,115 )	33,404
Cash Flows from Financing Activities:		
Net Increase in Deposits	120,051	116,832
Net Decrease in Short-Term Borrowings	(29,512 )	(51,641 )
Repayments of Federal Home Loan Bank Term Advances	—	(10,000 )
Purchase of Treasury Stock	(1,328 )	(2,237 )
Stock Options Exercised	490	1,149
Shares Issued Under the Employee Stock Purchase Plan	110	107
Tax Benefit from Exercise of Stock Options	8	53
Shares Issued for Dividend Reinvestment Plans	—	464
Cash Dividends Paid	(3,009 )	(2,944 )
Net Cash Provided By Financing Activities	86,810	51,783

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Net Increase in Cash and Cash Equivalents	88,342	93,772
Cash and Cash Equivalents at Beginning of Period	48,832	43,736
Cash and Cash Equivalents at End of Period	\$137,174	\$137,508

Supplemental Disclosures to Statements of Cash Flow Information:

Interest on Deposits and Borrowings	\$2,299	\$3,704
Income Taxes	511	191
Non-cash Investing and Financing Activity:		
Transfer of Loans to Other Real Estate Owned and Repossessed Assets	604	232
Acquisition of Subsidiaries	91	91

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 March 31, 2013, December 31, 2012 and March 31, 2012; the results of operations for the three-month periods ended March 31, 2013 and 2012; the consolidated statements of comprehensive income for the three-month periods ended March 31, 2013 and 2012; the changes in stockholders' equity for the three-month periods ended March 31, 2013 and 2012; and the cash flows for the three-month periods ended March 31, 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 five accounting standards updates. Four 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 the Consolidating Statements of Income and Note 5 - Comprehensive Income.

## Note 2. INVESTMENT SECURITIES (In Thousands)

The following table is the schedule of Available-For-Sale Securities at March 31, 2013, December 31, 2012 and March 31, 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
March 31, 2013						
Available-For-Sale Securities, at Amortized Cost	\$ 132,217	\$ 104,304	\$ 219,067	\$ 12,913	\$ 1,120	\$ 469,621
Available-For-Sale Securities, at Fair Value	132,153	104,469	228,323	12,691	1,139	478,775
Gross Unrealized Gains	23	228	9,256	2	19	9,528
Gross Unrealized Losses	87	63	—	224	—	374
Available-For-Sale Securities, Pledged as Collateral						274,433
Maturities of Debt Securities, at Amortized Cost:						
Within One Year	—	29,880	14,955	—		44,835
From 1 - 5 Years	132,217	69,269	193,002	11,913		406,401
From 5 - 10 Years	—	4,235	11,110	—		15,345
Over 10 Years	—	920	—	1,000		1,920

Maturities of Debt Securities,  
at Fair Value:

Within One Year	—	29,925	15,367	—		45,292
From 1 - 5 Years	132,153	69,340	200,956	11,891		414,340
From 5 - 10 Years	—	4,284	12,000	—		16,284
Over 10 Years	—	920	—	800		1,720

Securities in a Continuous

Loss Position, at Fair Value:

Less than 12 Months	\$94,909	\$31,325	\$3	\$8,452	\$—	\$134,689
12 Months or Longer	—	1,481	—	—	—	1,481
Total	\$94,909	\$32,806	\$3	\$8,452	\$—	\$136,170

Number of Securities in a  
Continuous Loss Position

28	154	1	11	—	194
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Unrealized Losses on  
Securities in a Continuous  
Loss Position:

Less than 12 Months	\$87	\$61	\$—	\$224	\$—	\$372
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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
12 Months or Longer	—	2	—	—	—	2
Total	\$87	\$63	\$—	\$224	\$—	\$374
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

March 31, 2012

Available-For-Sale Securities, at Amortized Cost	\$65,303	\$43,186	\$345,294	\$1,028	\$1,365	\$456,176
Available-For-Sale Securities, at Fair Value	65,660	43,482	355,382	828	1,433	466,785
Gross Unrealized Gains	357	308	10,240	—	74	10,979
Gross Unrealized Losses	—	12	152	200	6	370
Available-For-Sale Securities, Pledged as Collateral						304,303

Securities in a Continuous

Loss Position, at Fair Value:

Less than 12 Months	\$—	\$2,831	\$14,205	\$800	\$39	\$17,875
12 Months or Longer	—	—	—	—	—	—
Total	\$—	\$2,831	\$14,205	\$800	\$39	\$17,875
Number of Securities in a Continuous Loss Position	—	7	4	1	1	13

Unrealized Losses on  
 Securities in a Continuous  
 Loss Position:

Less than 12 Months	\$—	\$12	\$152	\$200	\$6	\$370
12 Months or Longer	—	—	—	—	—	—
Total						