ARROW FINANCIAL CORP
Form 10-Q/A
October 13, 2006

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**
Washington, D.C. 20549

**FORM 10-Q/A**
**Amendment No. 1**
[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

**For the Quarterly Period Ended June 30, 2005**

[ ] 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) | (IRS Employer Identification Number) |

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 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 __X__ No ____

Indicate by checkmark whether the registrant is an accelerated filer (as defined in Exchange Act 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 29, 2005 |
|---|---|
| Common Stock, par value $1.00 per share | 10,114,219 |

**ARROW FINANCIAL CORPORATION**

FORM 10-Q/A

June 30, 2005

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Explanatory Note

This Amendment No. 1 on Form 10-Q/A ("Form 10-Q/A") to the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2005 is being filed with the U.S. Securities and Exchange Commission to restate the Registrant s consolidated financial statements as of and for the quarterly period ended June 30, 2005 for the purpose of providing a corrected Consolidated Statement of Cash Flows. The restatement of the Registrant s consolidated financial statements in this Form 10-Q/A primarily corrects and reclassifies the presentation of the cash flow for acquisitions from financing activities to investing activities. Except as set forth in this Form 10-Q/A, all other Items included in the Registrant s Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2005 are unaffected by the changes described above and have been omitted from this amendment. The information in this Form 10-Q/A is stated as of June 30, 2005 and except as specifically noted herein, does not reflect any subsequent information or events.

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**ARROW FINANCIAL CORPORATION AND SUBSIDIARIES**

**CONSOLIDATED BALANCE SHEETS**

(Dollars in Thousands) (Unaudited)

| | June 30, 2005 | December 31, 2004 |
|---|---|---|
| **ASSETS** | | |
| Cash and Due from Banks | $ 33,541 | $ 29,805 |
| Federal Funds Sold | --- | 7,000 |
| Cash and Cash Equivalents | 33,541 | 36,805 |
| Securities Available-for-Sale | 321,101 | 325,248 |
| Securities Held-to-Maturity (Approximate Fair Value of $108,524 at June 30, 2005 and $110,341 at December 31, 2004) | 106,478 | 108,117 |
| Loans | 952,938 | 875,311 |
| Allowance for Loan Losses | (12,168) | (12,046) |
| Net Loans | 940,770 | 863,265 |
| Premises and Equipment, Net | 15,422 | 14,939 |
| Other Real Estate and Repossessed Assets, Net | 29 | 136 |
| Goodwill | 14,355 | 10,717 |
| Other Intangible Assets, Net | 3,106 | 1,019 |
| Other Assets | 19,503 | 17,703 |
| Total Assets | $1,454,305 | $1,377,949 |
| **LIABILITIES** | | |
| Deposits: | | |
| Demand | $ 178,708 | $ 167,667 |
| Regular Savings, N.O.W. & Money Market Deposit Accounts | 612,543 | 607,820 |
| Time Deposits of $100,000 or More | 113,062 | 85,906 |
| Other Time Deposits | 200,925 | 170,887 |
| Total Deposits | 1,105,238 | 1,032,280 |
| Short-Term Borrowings: | | |
| Federal Funds Purchased and Securities Sold Under Agreements to Repurchase | 49,164 | 42,256 |
| Other Short-Term Borrowings | 1,755 | 1,720 |
| Federal Home Loan Bank Advances | 145,000 | 150,000 |
| Junior Subordinated Obligations Issued to Unconsolidated Subsidiary Trusts | 20,000 | 20,000 |

| | | |
|---|---|---|
| Other Liabilities | 15,281 | 13,659 |
| Total Liabilities | 1,336,438 | 1,259,915 |
| **SHAREHOLDERS EQUITY** | | |
| Preferred Stock, $5 Par Value; 1,000,000 Shares Authorized | --- | --- |
| Common Stock, $1 Par Value; 20,000,000 Shares Authorized | | |
| (13,478,703 Shares Issued at June 30, 2005 and December 31, 2004) | 13,479 | 13,479 |
| Surplus | 128,266 | 127,312 |
| Undivided Profits | 27,799 | 23,356 |
| Unallocated ESOP Shares (81,185 Shares at June 30, 2005 | | |
| and 93,273 Shares at December 31, 2004) | (1,182) | (1,358) |
| Accumulated Other Comprehensive (Loss) Income | (1,540) | 429 |
| Treasury Stock, at Cost (3,274,798 Shares at June 30, | | |
| 2005 and 3,189,485 Shares at December 31, 2004) | (48,955) | (45,184) |
| Total Shareholders Equity | 117,867 | 118,034 |
| Total Liabilities and Shareholders Equity | $1,454,305 | $1,377,949 |

See Notes to Unaudited Consolidated Interim Financial Statements.

**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, | |
|---|---|---|---|---|
| | 2005 | 2004 | 2005 | 2004 |
| **INTEREST AND DIVIDEND INCOME** | | | | |
| Interest and Fees on Loans | $13,248 | $12,523 | $25,707 | $25,278 |
| Interest on Federal Funds Sold | 35 | 42 | 44 | 62 |
| Interest and Dividends on Securities Available-for-Sale | 3,489 | 3,491 | 6,907 | 7,038 |
| Interest on Securities Held-to-Maturity | 1,004 | 1,006 | 1,985 | 1,986 |
| Total Interest and Dividend Income | 17,776 | 17,062 | 34,643 | 34,364 |
| **INTEREST EXPENSE** | | | | |
| Interest on Deposits: | | | | |
| Time Deposits of $100,000 or More | 975 | 345 | 1,666 | 699 |
| Other Deposits | 2,787 | 2,671 | 5,123 | 5,396 |
| Interest on Short-Term Borrowings: | | | | |
| Federal Funds Purchased and Securities Sold | | | | |
| Under Agreements to Repurchase | 144 | 69 | 261 | 124 |
| Other Short-Term Borrowings | 5 | 2 | 8 | 4 |
| Federal Home Loan Bank Advances | 1,416 | 1,580 | 3,055 | 3,158 |
| Junior Subordinated Obligations Issued to Unconsolidated | | | | |
| Subsidiary Trusts | 294 | 284 | 571 | 568 |
| Total Interest Expense | 5,621 | 4,951 | 10,684 | 9,949 |
| **NET INTEREST INCOME** | 12,155 | 12,111 | 23,959 | 24,415 |
| Provision for Loan Losses | 176 | 254 | 408 | 539 |
| **NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES** | 11,979 | 11,857 | 23,551 | 23,876 |
| **OTHER INCOME** | | | | |
| Income from Fiduciary Activities | 1,181 | 1,060 | 2,288 | 2,116 |
| Fees for Other Services to Customers | 1,948 | 1,904 | 3,548 | 3,584 |
| Net Gains on Securities Transactions | 125 | --- | 189 | 210 |

| | | | | |
|---|---|---|---|---|
| Insurance Commissions | 488 | 6 | 883 | 11 |
| Other Operating Income | 140 | 165 | 268 | 438 |
| Total Other Income | 3,882 | 3,135 | 7,176 | 6,359 |
| | | | | |
| **OTHER EXPENSE** | | | | |
| Salaries and Employee Benefits | 5,288 | 4,778 | 10,343 | 9,583 |
| Occupancy Expense of Premises, Net | 757 | 699 | 1,464 | 1,394 |
| Furniture and Equipment Expense | 746 | 695 | 1,511 | 1,389 |
| Other Operating Expense | 2,384 | 2,001 | 4,342 | 3,933 |
| Total Other Expense | 9,175 | 8,173 | 17,660 | 16,299 |
| | | | | |
| **INCOME BEFORE PROVISION FOR INCOME TAXES** | 6,686 | 6,819 | 13,067 | 13,936 |
| Provision for Income Taxes | 2,006 | 2,121 | 3,957 | 4,373 |
| **NET INCOME** | $ 4,680 | $ 4,698 | $ 9,110 | $ 9,563 |
| | | | | |
| Average Shares Outstanding: | | | | |
| Basic | 10,131 | 10,123 | 10,160 | 10,120 |
| Diluted | 10,304 | 10,358 | 10,348 | 10,358 |
| | | | | |
| Per Common Share: | | | | |
| Basic Earnings | $ .46 | $ .46 | $ .90 | $ .94 |
| Diluted Earnings | .45 | .45 | .88 | .92 |

Share and Per Share amounts have been restated for the September 2004 3% stock dividend.

See Notes to Unaudited Consolidated Interim Financial Statements.

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**ARROW FINANCIAL CORPORATION AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY**

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

| | Shares Issued | Common Stock | Surplus | Undivided Profits | Unallo-cated ESOP Shares | Accumulated Other Com-prehensive (Loss) Income | Treasury Stock | Total |
|---|---|---|---|---|---|---|---|---|
| Balance at December 31, 2004 | 13,478,703 | $13,479 | $127,312 | $23,356 | $(1,358) | $ 429 | $(45,184) | $118,034 |
| Comprehensive Income, Net of Tax: | | | | | | | | |
| Net Income | --- | --- | --- | 9,110 | --- | --- | --- | 9,110 |
| Increase in Additional Pension Liability Over Unrecognized Prior Service Cost (Pre-tax $570) | --- | --- | --- | --- | --- | (343) | --- | (343) |
| Net Unrealized Securities Holding Losses Arising During the Period, Net of Tax (Pre-tax $2,515) | --- | --- | --- | --- | --- | (1,512) | --- | (1,512) |
| Reclassification Adjustment for Net Securities Gains Included in | --- | --- | --- | --- | --- | (114) | --- | (114) |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Net Income, Net of Tax | | | | | | | | |
| (Pre-tax $189) | | | | | | | | |
| Other Comprehensive Loss | | | | | | | | (1,969) |
| Comprehensive Income | | | | | | | | 7,141 |
| Cash Dividends Declared, | | | | | | | | |
| $.46 per Share | --- | --- | --- | (4,667) | --- | --- | --- | (4,667) |
| Stock Options Exercised | | | | | | | | |
| (64,320 Shares) | --- | --- | 149 | --- | --- | --- | 565 | 714 |
| Shares Issued Under the Directors | | | | | | | | |
| Stock Purchase Plan (2,264 | | | | | | | | |
| Shares) | --- | --- | 40 | --- | --- | --- | 20 | 60 |
| Shares Issued Under the Employee | | | | | | | | |
| Stock Purchase Plan (12,105 | | | | | | | | |
| Shares) | --- | --- | 202 | --- | --- | --- | 147 | 349 |
| Tax Benefit for Exercise of | | | | | | | | |
| Stock Options | --- | --- | 397 | --- | --- | --- | --- | 397 |
| Allocation of ESOP Stock | | | | | | | | |
| (12,088 Shares) | --- | --- | 166 | --- | 176 | --- | --- | 342 |
| Purchase of Treasury Stock | | | | | | | | |
| (164,035 Shares) | --- | --- | --- | --- | --- | --- | (4,503) | (4,503) |
| Balance at June 30, 2005 | 13,478,703 | $13,479 | $128,266 | $27,799 | $(1,182) | $(1,540) | $(48,955) | $117,867 |

See Notes to Unaudited Consolidated Interim Financial Statements.

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**ARROW FINANCIAL CORPORATION AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY**

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

| | Shares Issued | Common Stock | Surplus | Undivided Profits | Unallo-cated ESOP Shares | Accumulated Other Com-prehensive (Loss) Income | Treasury Stock | Total |
|---|---|---|---|---|---|---|---|---|
| Balance at December 31, 2003 | 13,086,119 | $13,086 | $113,335 | $24,303 | $(1,769) | $ 1,084 | $(44,174) | $105,865 |
| Comprehensive Income, Net of Tax: | | | | | | | | |
| Net Income | --- | --- | --- | 9,563 | --- | --- | --- | 9,563 |
| Increase in Additional Pension Liability Over Unrecognized Prior Service Cost (Pre-tax $40) | | | | | | (24) | | (24) |
| Net Unrealized Securities Holding Losses Arising During the Period, Net of Tax (Pre-tax $4,923) | --- | --- | --- | --- | --- | (2,960) | --- | (2,960) |
| Reclassification Adjustment for Net Securities Gains Included in | --- | --- | --- | --- | --- | (126) | --- | (126) |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Net Income, Net of Tax | | | | | | | | |
| (Pre-tax $210) | | | | | | | | |
| Other Comprehensive Loss | | | | | | | | (3,110) |
| Comprehensive Income | | | | | | | | 6,453 |
| Cash Dividends Declared, | | | | | | | | |
| $.44 per Share | --- | --- | --- | (4,412) | --- | --- | --- | (4,412) |
| Stock Options Exercised | | | | | | | | |
| (60,138 Shares) | --- | --- | 106 | --- | --- | --- | 467 | 573 |
| Shares Issued Under the Employee | | | | | | | | |
| Stock Purchase Plan (12,357 | | | | | | | | |
| Shares) | --- | --- | 206 | --- | --- | --- | 97 | 303 |
| Shares Issued Under the Directors | | | | | | | | |
| Stock Plan (1,206 Shares) | --- | --- | 26 | --- | --- | --- | 10 | 36 |
| Tax Benefit for Exercise of | | | | | | | | |
| Stock Options | --- | --- | 158 | --- | --- | --- | --- | 158 |
| Allocation of ESOP Stock | | | | | | | | |
| (18,339 Shares) | --- | --- | 257 | --- | 267 | --- | --- | 524 |
| Purchase of Treasury Stock | | | | | | | | |
| (44,370 Shares) | --- | --- | --- | --- | --- | --- | (1,260) | (1,260) |
| Balance at June 30, 2004 | 13,086,119 | $13,086 | $114,088 | $29,454 | $(1,502) | $(2,026) | $(44,860) | $108,240 |

Share and Per Share amounts have been restated for the September 2004 3% stock dividend.

See Notes to Unaudited Consolidated Interim 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, 2005 (Restated) | 2004 |
|---|---|---|
| **Operating Activities:** | | |
| Net Income | $ 9,110 | $ 9,563 |
| Adjustments to Reconcile Net Income to Net Cash | | |
| Provided by Operating Activities: | | |
| Provision for Loan Losses | 408 | 539 |
| Depreciation and Amortization | 1,113 | 1,618 |
| Compensation Expense for Allocated ESOP Shares | 166 | 257 |
| Net Gains on the Sale of Securities Available-for-Sale | (195) | (210) |
| Losses on the Sale of Securities Available-for-Sale | 6 | --- |
| Loans Originated and Held-for-Sale | (1,381) | (7,497) |
| Proceeds from the Sale of Loans Held-for-Sale | 2,312 | 7,609 |
| Net Losses (Gains) on the Sale of Loans, Premises and Equipment, | | |
| Other Real Estate Owned and Repossessed Assets | 9 | (64) |
| (Increase) Decrease in Deferred Tax Assets | (181) | 45 |
| Shares Issued Under the Directors Stock Plan | 60 | 36 |
| Net Increase in Other Assets | (799) | (1,994) |
| Net Increase (Decrease) in Other Liabilities | 1,854 | (1,238) |
| **Net Cash Provided By Operating Activities** | 12,482 | 8,664 |
| **Investing Activities:** | | |
| Proceeds from the Sale of Securities Available-for-Sale | 28,178 | 20,226 |
| Proceeds from the Maturities and Calls of Securities Available-for-Sale | 19,361 | 36,714 |
| Purchases of Securities Available-for-Sale | (46,455) | (56,162) |
| Proceeds from the Maturities of Securities Held-to-Maturity | 6,916 | 2,957 |
| Purchases of Securities Held-to-Maturity | (5,375) | (5,335) |
| Net Increase in Loans | (70,853) | (11,839) |
| Proceeds from the Sales of Premises and Equipment, | 470 | 431 |

| | | |
|---|---|---|
| Other Real Estate Owned and Repossessed Assets | | |
| Purchases of Premises and Equipment | (226) | (1,052) |
| Net Increase from Branch Acquisitions | 47,083 | --- |
| **Net Cash Used In Investing Activities** | (20,901) | (14,060) |
| **Financing Activities:** | | |
| Net Increase (Decrease) in Deposits | 10,746 | (8,949) |
| Net Increase in Short-Term Borrowings | 6,943 | 6,531 |
| Federal Home Loan Bank Advances | 75,000 | 20,000 |
| Federal Home Loan Bank Repayments | (80,000) | (12,500) |
| Tax Benefit from Exercise of Stock Options | 397 | 158 |
| Purchases of Treasury Stock | (4,503) | (1,260) |
| Treasury Stock Issued for Stock-Based Plans | 1,063 | 876 |
| Allocation of ESOP Shares | 176 | 267 |
| Cash Dividends Paid | (4,667) | (4,412) |
| **Net Cash Provided By Financing Activities** | 5,155 | 711 |
| **Net Decrease in Cash and Cash Equivalents** | (3,264) | (4,685) |
| Cash and Cash Equivalents at Beginning of Period | 36,805 | 33,326 |
| **Cash and Cash Equivalents at End of Period** | $33,541 | $28,641 |
| **Supplemental Cash Flow Information:** | | |
| Interest Paid | $10,416 | $10,076 |
| Income Taxes Paid | 2,866 | 5,244 |
| Transfer of Loans to Other Real Estate Owned and Repossessed Assets | 403 | 493 |

See Notes to Unaudited Consolidated Interim Financial Statements.

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ARROW FINANCIAL CORPORATION AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

June 30, 2005

(Dollars in Thousands)

1. Financial Statement Presentation

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, 2005 and December 31, 2004; the results of operations for the three-month and six-month periods ended June 30, 2005 and 2004; the changes in shareholders equity for the six-month periods ended June 30, 2005 and 2004; and the cash flows for the six-month periods ended June 30, 2005 (restated) and 2004. All such adjustments are of a normal recurring nature. The unaudited consolidated interim financial statements should be read in conjunction with the annual consolidated financial statements of Arrow for the year ended December 31, 2004, included in Arrow s 2004 Form 10-K.

Restatement of the Consolidated Statement of Cash Flows: During the third quarter of 2006, Arrow determined that it was necessary to restate our previously issued financial statements for the quarterly period ended June 30, 2005 to correct certain misclassifications in the Consolidated Statement of Cash Flows.

The restatement principally involves the reclassification of certain cash flows related to Arrow s acquisition of three HSBC Bank U.S.A., N.A. branches in the second quarter of 2005. Those cash flows, totaling $47,083, should have been presented as investing activities as opposed to financing activities in the Consolidated Statement of Cash Flows for the six months ended June 30, 2005. The reclassification of these cash flows affects the subtotals of cash flows from investing and financing activities but does not affect the total amount of net increase (decrease) in cash and cash equivalents as presented in the Consolidated Statement of Cash Flows.

In addition to the foregoing, in the previously filed Consolidated Statement of Cash Flows for the six months ended June 30, 2005, under operating activities, the line item (Increase) Decrease in Other Liabilities incorrectly excluded $231 as a result of a typographical error. However, this change did not affect the total for Net Cash Provided by Operating Activities.

In order to conform to common industry presentation practice, and more readily correspond to changes in balance sheet captions, Arrow has combined in the restated Consolidated Statements of Cash Flows, and will combine in future filed Consolidated Statements of Cash Flows, the line item (Increase) Decrease in Interest Receivable and Increase in Other Assets into a single line item, Net Increase in Other Assets and will combine the line items Increase (Decrease) in Interest Payable and Increase (Decrease) in Other Liabilities into a single line item Net Increase (Decrease) in Other Liabilities. The combination of these line items, for all periods presented, has no effect on the amount of net cash provided by operating activities as disclosed in the previously filed Consolidated Statements of Cash Flows.

The restatement does not affect Arrow s Consolidated Statements of Income, Consolidated Balance Sheets or Consolidated Statements of Changes in Stockholders Equity for the affected period. Accordingly, Arrow s previously reported net income, earnings per share, total assets and regulatory capital as of and for the six-month period ended June 30, 2005 remain unchanged.

The Consolidated Statement of Cash Flows for the six-month period ended June 30, 2005, as previously reported and as restated, is reflected on the following page.

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**1. Financial Statement Presentation (Continued)**

**ARROW FINANCIAL CORPORATION AND SUBSIDIARIES**

**CONSOLIDATED STATEMENT OF CASH FLOWS**

(Dollars in Thousands)(Unaudited)

| | Six Months Ended June 30, | |
|---|---|---|
| | 2005 (As Previously Reported) | 2005 (Restated) |
| **Operating Activities:** | | |
| Net Income | $ 9,110 | $ 9,110 |
| Adjustments to Reconcile Net Income to Net Cash | | |
| Provided by Operating Activities: | | |
| Provision for Loan Losses | 408 | 408 |
| Depreciation and Amortization | 1,113 | 1,113 |
| Compensation Expense for Allocated ESOP Shares | 166 | 166 |
| Net Gains on the Sale of Securities Available-for-Sale | (195) | (195) |
| Losses on the Sale of Securities Available-for-Sale | 6 | 6 |
| Loans Originated and Held-for-Sale | (1,381) | (1,381) |
| Proceeds from the Sale of Loans Held-for-Sale | 2,312 | 2,312 |
| Net Losses (Gains) on the Sale of Loans, Premises and Equipment, | | |
| Other Real Estate Owned and Repossessed Assets | 9 | 9 |
| (Increase) Decrease in Deferred Tax Assets | (181) | (181) |
| Shares Issued Under the Directors Stock Plan | 60 | 60 |
| | (532) | --- |
| (Increase) Decrease in Interest Receivable | | |
| | 267 | --- |
| Increase (Decrease) in Interest Payable | | |
| | (268) | --- |
| Increase in Other Assets | | |
| | 1,356 | --- |

| | | |
|---|---|---|
| Increase (Decrease) in Other Liabilities | --- | (799) |
| Net Increase in Other Assets | --- | 1,854 |
| Net Increase (Decrease) in Other Liabilities | | |
| **Net Cash Provided By Operating Activities** | 12,481 | 12,482 |
| **Investing Activities:** | | |
| Proceeds from the Sale of Securities Available-for-Sale | 28,178 | 28,178 |
| Proceeds from the Maturities and Calls of Securities Available-for-Sale | 19,361 | 19,361 |
| Purchases of Securities Available-for-Sale | (46,455) | (46,455) |
| Proceeds from the Maturities of Securities Held-to-Maturity | 6,916 | 6,916 |
| Purchases of Securities Held-to-Maturity | (5,375) | (5,375) |
| Net Increase in Loans | (70,853) | (70,853) |
| Proceeds from the Sales of Premises and Equipment, | | |
| Other Real Estate Owned and Repossessed Assets | 470 | 470 |
| Purchases of Premises and Equipment | (226) | (226) |
| Net Increase from Branch Acquisitions | --- | 47,083 |
| **Net Cash Used In Investing Activities** | (67,984) | (20,901) |
| **Financing Activities:** | | |
| Net Increase (Decrease) in Deposits | 10,746 | 10,746 |
| Net Increase in Short-Term Borrowings | 6,943 | 6,943 |
| Federal Home Loan Bank Advances | 75,000 | 75,000 |
| Federal Home Loan Bank Repayments | (80,000) | (80,000) |
| Net Increase from Branch Acquisitions | 47,084 | --- |
| Tax Benefit from Exercise of Stock Options | 397 | 397 |
| Purchases of Treasury Stock | (4,503) | (4,503) |
| Treasury Stock Issued for Stock-Based Plans | 1,063 | 1,063 |
| Allocation of ESOP Shares | 176 | 176 |
| Cash Dividends Paid | (4,667) | (4,667) |
| **Net Cash Provided By Financing Activities** | 52,239 | 5,155 |
| **Net Decrease in Cash and Cash Equivalents** | (3,264) | (3,264) |
| Cash and Cash Equivalents at Beginning of Period | 36,805 | 36,805 |
| **Cash and Cash Equivalents at End of Period** | $33,541 | $33,541 |
| **Supplemental Cash Flow Information:** | | |
| Interest Paid | $10,416 | $10,416 |
| Income Taxes Paid | 2,866 | 2,866 |
| Transfer of Loans to Other Real Estate Owned and Repossessed Assets | 403 | 403 |

2. Accumulated Other Comprehensive (Loss) Income (In Thousands)

The following table presents the components, net of tax, of accumulated other comprehensive (loss) income as of June 30, 2005 and December 31, 2004:

| | 2005 | 2004 |
|---|---|---|
| Excess of Additional Pension Liability Over Unrecognized Prior Service Cost | $ (693) | $(351) |
| Net Unrealized Holding (Losses) Gains on Securities Available-for-Sale | (847) | 780 |
| Total Accumulated Other Comprehensive (Loss) Income | $(1,540) | $ 429 |

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

The following table presents a reconciliation of the numerator and denominator used in the calculation of basic and diluted earnings per common share (EPS) for the three-month and six-month periods ended June 30, 2005 and 2004:

| | Income (Numerator) | Shares (Denominator) | Per Share Amount |
|---|---|---|---|
| For the Three Months Ended June 30, 2005: | | | |
| Basic EPS | $4,680 | 10,131 | $.46 |
| Dilutive Effect of Stock Options | --- | 173 | |
| Diluted EPS | $4,680 | 10,304 | $.45 |
| For the Three Months Ended June 30, 2004: | | | |
| Basic EPS | $4,698 | 10,123 | $.46 |
| Dilutive Effect of Stock Options | --- | 235 | |
| Diluted EPS | $4,698 | 10,358 | $.45 |

| | Income | Shares | Per Share |
|---|---|---|---|

| | (Numerator) | (Denominator) | Amount |
|---|---|---|---|
| For the Six Months Ended June 30, 2005: | | | |
| Basic EPS | $9,110 | 10,160 | $.90 |
| Dilutive Effect of Stock Options | --- | 188 | |
| Diluted EPS | $9,110 | 10,348 | $.88 |
| For the Six Months Ended June 30, 2004: | | | |
| Basic EPS | $9,563 | 10,120 | $.94 |
| Dilutive Effect of Stock Options | --- | 238 | |
| Diluted EPS | $9,563 | 10,358 | $.92 |

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4. Stock-Based Compensation Plans

Arrow accounts for its stock-based compensation plans under the recognition and measurement principles of APB Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations. No stock-based employee compensation cost has been reflected in net income for stock awards granted under these plans (other than for certain stock appreciation rights attached to options granted in 1992 and earlier, all of which have been exercised as of January 2002), as all awards granted under these plans have been options having an exercise price equal to the market value of the underlying common stock on the date of grant. However, options granted do generally impact diluted earnings per share by increasing the weighted average diluted shares outstanding and thereby decreasing diluted earnings per share as compared to basic earnings per share.

There were no options granted in the first six months of 2005. The weighted-average fair value of options granted during 2004 was $6.49 per option. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions used for grants in 2004: dividend yield of 3.28%; expected volatility of 27.2%; risk free interest rate of 3.76%; and expected lives of 7.0 years. Arrow also sponsors an Employee Stock Purchase Plan (ESPP) under which employees purchased Arrow s common stock at a 15% discount below market price at the time of purchase for the first two months of 2005, but at a 5% discount below market price for all subsequent purchases. Under APB 25, a plan with a discount of 15% or less is not considered compensatory and expense is not recognized. Under SFAS No. 123, however, a stock purchase plan with a discount in excess of 5% is considered a compensatory plan and thus the ESPP was considered a compensatory plan for the first two months of 2005, and the entire discount for that period was considered compensation expense in the pro forma disclosures set forth below. The effects of applying SFAS No. 123 on pro forma net income in the recently completed period may not be representative of the effects on pro forma net income for future periods.

The following table illustrates the effect on net income and earnings per share if we had applied the fair value recognition provisions of SFAS No. 123, Accounting for Stock-Based Compensation, to stock-based employee compensation plans.

| | Quarter Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | 2005 | 2004 | 2005 | 2004 |
| Net Income, as Reported | $4,680 | $4,698 | $9,110 | $9,563 |
| Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects | (134) | (137) | (285) | (271) |
| Pro Forma Net Income | $4,546 | $4,561 | $8,825 | $9,292 |

| | | | | |
|---|---|---|---|---|
| Earnings per Share: | | | | |
| Basic - as Reported | $.46 | $.46 | $.90 | $.94 |
| Basic - Pro Forma | .45 | .45 | .87 | .92 |
| Diluted - as Reported | .45 | .45 | .88 | .92 |
| Diluted - Pro Forma | .44 | .44 | .85 | .90 |

In December 2004, the FASB issued a revised Statement of Financial Accounting Standards No. 123 (SFAS No. 123R), Share-Based Payment. SFAS No. 123R requires that we measure the cost of employee services received in exchange for an award of equity instruments based on the fair value of the award on the grant date. That cost will be recognized over the period during which an employee is required to provide service in exchange for the award (i.e. the vesting period), which is typically four years for Arrow. In a press release dated April 14, 2005, the SEC delayed the effective date of SFAS No. 123R to the first quarter of 2006.

5. Guarantees

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

For letters of credit, the amount of the collateral obtained, if any, is based on management s credit evaluation of the counter-party. Arrow had approximately $3.0 million of standby letters of credit on June 30, 2005, most of which will expire within one year and some of which were not collateralized. At that date, all the letters of credit were for private borrowing arrangements. The fair value of the Arrow s standby letters of credit at June 30, 2005 was insignificant.

6. Retirement Plans (In Thousands)

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

| | Pension Benefits | | Postretirement Benefits | |
|---|---|---|---|---|
| | 2005 | 2004 | 2005 | 2004 |
| Service Cost | $465 | $246 | $ 46 | $ 44 |
| Interest Cost | 639 | 346 | 115 | 97 |
| Expected Return on Plan Assets | (963) | (527) | --- | --- |
| Amortization of Prior Service Cost (Credit) | (57) | 32 | (6) | (17) |
| Amortization of Transition Obligation | --- | --- | 26 | 10 |
| Amortization of Net Loss (Gain) | 150 | 16 | 42 | 46 |
| Net Periodic Benefit Cost | $234 | $113 | $223 | $180 |

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

| | Pension Benefits | | Postretirement Benefits | |
|---|---|---|---|---|
| | 2005 | 2004 | 2005 | 2004 |
| Service Cost | $ 797 | $ 492 | $ 89 | $ 88 |
| Interest Cost | 1,095 | 692 | 221 | 194 |
| Expected Return on Plan Assets | (1,651) | (1,054) | --- | --- |
| Amortization of Prior Service Cost (Credit) | (97) | 64 | (11) | (34) |
| Amortization of Transition Obligation | --- | --- | 50 | 20 |
| Amortization of Net Loss (Gain) | 257 | 32 | 81 | 92 |
| Net Periodic Benefit Cost | $ 401 | $ 226 | $430 | $360 |

We previously disclosed in our financial statements for the year ended December 31, 2004 that we do not expect to make a contribution to the qualified defined benefit pension plan during 2005. However, we recently determined that it was appropriate to contribute approximately $792 thousand to the plan, the maximum actuarially recommended contribution for the 2005 plan year.

In December 2003, the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the Act) became law in the United States, however, final regulations were not issued until January 2005. The Act introduced a prescription drug benefit under Medicare as well as a federal subsidy to sponsors of retiree health care benefit plans that provide a benefit that is at least actuarially equivalent to Medicare Part D under the Act. The measures of the accumulated non-pension postretirement benefit obligation and net periodic non-pension postretirement benefit cost do not reflect any amount associated with the subsidy at June 30, 2005, because we were unable to conclude whether the benefits provided by the plan are actuarially equivalent to Medicare Part D under the Act.

7. Recently Issued Accounting Pronouncements

In January 2003, the FASB issued FASB Interpretation No. 46 ( FIN 46 ), Consolidation of Variable Interest Entities . The objective of this interpretation was to provide guidance on how to identify a variable interest entity ( VIE ) and determine when the assets, liabilities, non-controlling interests, and results of operations of a VIE need to be included in a company s consolidated financial statements. FIN 46 was effective for all VIE s created after January 31, 2003. However, the FASB postponed that effective date to December 31, 2003. In December 2003, the FASB issued a revised FIN 46 (FIN 46 R), which further delayed this effective date until March 31, 2004 for VIE s created prior to February 1, 2003, except for special purpose entities, which were required to adopt either FIN 46 or FIN 46 R as of December 31, 2003. The requirements of FIN 46 R resulted in the deconsolidation of our wholly-owned subsidiary trusts, formed to issue redeemable preferred securities ( trust preferred securities ) to the public, the proceeds of which are used by the trust to acquire subordinated debt of Arrow. Under final rules issued February 28, 2005 by the Federal Reserve Board, trust preferred securities may continue to qualify as Tier 1 capital for bank regulatory purposes, in an amount not to exceed 25% of Tier 1 capital. The final rule limits restricted core capital elements to a percentage of the sum of core capital elements, net of goodwill less any associated deferred tax liability. We have issued trust preferred securities in 2003 and 2004 totaling $20 million. Up to half of total capital may consist of so-called "Tier 2" capital, comprising a limited amount of subordinated debt, preferred stock not qualifying as Tier 1 capital, certain other instruments and a limited amount of the allowance for loan losses.

## Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders

Arrow Financial Corporation:

We have reviewed the consolidated balance sheet of Arrow Financial Corporation and subsidiaries (the Company ) as of June 30, 2005, and the related consolidated statements of income for the three-month and six-month periods ended June 30, 2005 and 2004, and the consolidated statements of changes in shareholders equity and cash flows for the six-month periods ended June 30, 2005 and 2004. These consolidated financial statements are the responsibility of the Company s management.

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

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

We have previously audited, in accordance with standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of Arrow Financial Corporation and subsidiaries as of December 31, 2004, and the related consolidated statements of income, changes in shareholders equity and cash flows for the year then ended (not presented herein); and in our report dated March 7, 2005, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying consolidated balance sheet as of December 31, 2004, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

As discussed in Note 1 to the consolidated financial statements, the Company has restated its financial statements for the six-month period ended June 30, 2005.

/s/ KPMG LLP

Albany, New York

August 5, 2005, except for Note 1, as to which

the date is October 12, 2006

**Item 4: Controls and Procedures**

Senior management, including the Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the design and operation of Arrow's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended) as of June 30, 2005. Based upon that evaluation, including the effects of the restatement of the Consolidated Statement of Cash Flows as described in Note 1 to the Consolidated Financial Statements, senior management, including the Chief Executive Officer and Chief Financial Officer, concluded that our disclosure controls and procedures were effective. Further, there were no changes made in our internal control over financial reporting that occurred during the most recent fiscal quarter that had materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**Part II**

**Item 6.**

**Exhibits**

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

**SIGNATURES**

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

ARROW FINANCIAL CORPORATION

Registrant

| | |
|---|---|
| Date: October 12, 2006 | s/Thomas L. Hoy<br>Thomas L. Hoy, President and<br>Chief Executive Officer and Chairman of the Board |
| Date: October 12, 2006 | s/John J. Murphy<br>John J. Murphy, Executive Vice President,<br>Treasurer and Chief Financial Officer<br>(Principal Financial Officer and<br>Principal Accounting Officer) |

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