NBT BANCORP INC
Form 10-Q
August 08, 2013

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

(Mark One)
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2013.
OR
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from ________ to ________.

COMMISSION FILE NUMBER 0-14703

NBT BANCORP INC.
(Exact Name of Registrant as Specified in its Charter)

DELAWARE	16-1268674
(State of Incorporation)	(I.R.S. Employer Identification No.)

52 SOUTH BROAD STREET, NORWICH, NEW YORK 13815
(Address of Principal Executive Offices) (Zip Code)

Registrant's Telephone Number, Including Area Code: (607) 337-2265

None
(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

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 x No o

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 (Section 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 x No o

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. (Check One):

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

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

As of July 31, 2013, there were 43,587,942 shares outstanding of the Registrant's common stock, $0.01 par value per share.

NBT BANCORP INC.
FORM 10-Q--Quarter Ended June 30, 2013

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Item 1 – FINANCIAL STATEMENTS

NBT Bancorp Inc. and Subsidiaries
Consolidated Balance Sheets (unaudited)

(In thousands, except share and per share data)	June 30, 2013	December 31, 2012
Assets		
Cash and due from banks	$142,570	$157,094
Short-term interest bearing accounts	1,117	6,574
Securities available for sale, at fair value	1,390,403	1,147,999
Securities held to maturity (fair value $121,069 and $61,535, respectively)	122,302	60,563
Trading securities	5,092	3,918
Federal Reserve and Federal Home Loan Bank stock	43,491	29,920
Loans	5,290,710	4,277,616
Less allowance for loan losses	71,184	69,334
Net loans	5,219,526	4,208,282
Premises and equipment, net	87,811	77,875
Goodwill	264,376	152,373
Intangible assets, net	28,204	16,962
Bank owned life insurance	112,907	80,702
Other assets	116,719	99,997
Total assets	$7,534,518	$6,042,259
Liabilities		
Demand (noninterest bearing)	$1,516,385	$1,242,712
Savings, NOW, and money market	3,256,753	2,558,376
Time	1,105,038	983,261
Total deposits	5,878,176	4,784,349
Short-term borrowings	385,611	162,941
Long-term debt	309,111	367,492
Trust preferred debentures	101,196	75,422
Other liabilities	68,849	69,782
Total liabilities	6,742,943	5,459,986
Stockholders’ equity		
Preferred stock, $0.01 par value. Authorized 2,500,000 shares at June 30, 2013 and December 31, 2012	-	-
Common stock, $0.01 par value. Authorized 100,000,000 shares at June 30, 2013 and December 31, 2012; issued 49,651,494 at June 30, 2013 and 39,305,131 at December 31, 2012	497	393
Additional paid-in-capital	572,359	346,692
Retained earnings	366,555	357,558
Accumulated other comprehensive loss	(21,586)	(5,880)
Common stock in treasury, at cost, 6,116,825 and 5,529,781 shares at June 30, 2013 and December 31, 2012, respectively	(126,250)	(116,490)
Total stockholders’ equity	791,575	582,273
Total liabilities and stockholders’ equity	$7,534,518	$6,042,259

See accompanying notes to unaudited interim consolidated financial statements.

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NBT Bancorp Inc. and Subsidiaries Consolidated Statements of Income (unaudited) (In thousands, except per share data)	Three months ended June 30, 2013	2012	Six months ended June 30, 2013	2012
Interest, fee, and dividend income				
Interest and fees on loans	$62,031	$50,509	$115,726	$100,717
Securities available for sale	6,537	7,108	12,283	14,474
Securities held to maturity	548	617	1,073	1,257
Other	488	413	891	805
Total interest, fee, and dividend income	69,604	58,647	129,973	117,253
Interest expense				
Deposits	4,296	4,834	8,446	9,977
Short-term borrowings	67	48	109	89
Long-term debt	3,026	3,580	6,635	7,161
Trust preferred debentures	560	434	988	883
Total interest expense	7,949	8,896	16,178	18,110
Net interest income	61,655	49,751	113,795	99,143
Provision for loan losses	6,402	4,103	12,060	8,574
Net interest income after provision for loan losses	55,253	45,648	101,735	90,569
Noninterest income				
Insurance and other financial services revenue	5,755	5,279	12,648	11,433
Service charges on deposit accounts	4,933	4,571	9,256	8,912
ATM and debit card fees	4,044	3,063	7,286	6,025
Retirement plan administration fees	2,957	2,411	5,639	4,744
Trust	4,699	2,312	7,612	4,441
Bank owned life insurance	886	618	1,735	1,589
Net securities (losses) gains	(61)	97	1,084	552
Other	2,324	2,331	5,506	6,042
Total noninterest income	25,537	20,682	50,766	43,738
Noninterest expense				
Salaries and employee benefits	29,160	24,992	56,207	51,717
Occupancy	5,219	4,222	10,196	8,713
Data processing and communications	3,854	3,431	7,309	6,689
Professional fees and outside services	3,237	2,388	6,138	5,113
Equipment	2,910	2,409	5,492	4,789
Office supplies and postage	1,656	1,574	3,246	3,245
FDIC expenses	1,273	942	2,403	1,873
Advertising	1,000	805	1,723	1,607
Amortization of intangible assets	1,351	841	2,202	1,660
Loan collection and other real estate owned	421	799	1,139	1,437
Merger expenses	1,269	826	11,950	1,337
Other	5,100	4,161	9,150	7,684
Total noninterest expense	56,450	47,390	117,155	95,864
Income before income tax expense	24,340	18,940	35,346	38,443
Income tax expense	7,424	5,683	10,781	11,536
Net income	$16,916	$13,257	$24,565	$26,907
Earnings per share				
Basic	$0.39	$0.40	$0.61	$0.81
Diluted	$0.38	$0.40	$0.61	$0.80

See accompanying notes to unaudited interim consolidated financial statements.

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Consolidated Statements of Comprehensive Income (unaudited)	Three months ended June 30, 2013	2012	Six months ended June 30, 2013	2012
(In thousands)				
Net income	$16,916	$13,257	$24,565	$26,907
Other comprehensive income, net of tax				
Unrealized net holding (losses) gains arising during the period (pre-tax amounts of ($24,712), ($309), ($26,464) and $335)	(14,923)	(185)	(15,978)	201
Reclassification adjustment for net losses (gains) related to securities available for sale included in net income (pre-tax amounts of ($61), $97, $1,084 and $552)	37	(58)	(650)	(331)
Pension and other benefits:				
Amortization of prior service cost and actuarial gains (pre-tax amounts of $710, $856, $1,536 and $1,713)	426	511	922	1,027
Total other comprehensive (loss) income	(14,460)	268	(15,706)	897
Comprehensive income	$2,456	$13,525	$8,859	$27,804

See accompanying notes to unaudited interim consolidated financial statements

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NBT Bancorp Inc. and Subsidiaries

Consolidated Statements of Stockholders' Equity (unaudited)

(in thousands, except share and per share data)	Common Stock	Additional Paid-in-Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Common Stock in Treasury	Total
Balance at December 31, 2011	$ 380	$ 317,329	$ 329,981	$ (6,104)	$ (103,476)	$ 538,110
Net income	-	-	26,907	-	-	26,907
Cash dividends - $0.40 per share	-	-	(13,232)	-	-	(13,232)
Purchase of 769,568 treasury shares	-	-	-	-	(15,490)	(15,490)
Net issuance of 1,269,592 shares for acquisition	13	25,811	-	-	-	25,824
Net issuance of 79,052 shares to employee benefit plans and other stock plans, including tax benefit	-	(753)	(196)	-	1,641	692
Stock-based compensation	-	2,797	-	-	-	2,797
Other comprehensive income	-	-	-	897	-	897
Balance at June 30, 2012	$ 393	$ 345,184	$ 343,460	$ (5,207)	$ (117,325)	$ 566,505
Balance at December 31, 2012	$ 393	$ 346,692	$ 357,558	$ (5,880)	$ (116,490)	$ 582,273
Net income	-	-	24,565	-	-	24,565
Cash dividends - $0.40 per share	-	-	(15,568)	-	-	(15,568)
Purchase of 267,425 treasury shares	-	-	-	-	(5,460)	(5,460)
Issuance of 10,346,363 shares, net of 408,957 treasury shares, for Alliance acquisition	104	225,447	-	-	(5,779)	219,772
Net issuance of 89,338 shares to employee benefit plans and other stock plans, including tax benefit	-	(2,506)	-	-	1,479	(1,027)
Stock-based compensation	-	2,726	-	-	-	2,726
Other comprehensive loss	-	-	-	(15,706)	-	(15,706)
Balance at June 30, 2013	$ 497	$ 572,359	$ 366,555	$ (21,586)	$ (126,250)	$ 791,575

See accompanying notes to unaudited interim consolidated financial statements.

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NBT Bancorp Inc. and Subsidiaries Consolidated Statements of Cash Flows (unaudited) (In thousands, except per share data)	Six Months Ended June 30, 2013	2012
Operating activities		
Net income	$24,565	$26,907
Adjustments to reconcile net income to net cash provided by operating activities		
Provision for loan losses	12,060	8,574
Depreciation and amortization of premises and equipment	3,828	3,020
Net accretion on securities	2,811	1,197
Amortization of intangible assets	2,202	1,660
Stock based compensation	2,726	2,797
Bank owned life insurance income	(1,735)	(1,589)
Purchases of trading securities	(949)	(657)
Unrealized (gains) losses in trading securities	(225)	78
Deferred income tax benefit	(519)	(1,794)
Proceeds from sales of loans held for sale	39,060	28,774
Originations and purchases of loans held for sale	(40,233)	(34,182)
Net gains on sales of loans held for sale	(817)	(894)
Net security gains	(1,084)	(552)
Net gain on sales of other real estate owned	(571)	(417)
Net decrease in other assets	9,144	11,099
Net decrease in other liabilities	(8,333)	(10,897)
Net cash provided by operating activities	41,930	33,124
Investing activities		
Net cash provided by acquisitions	80,909	53,121
Securities available for sale:		
Proceeds from maturities, calls, and principal paydowns	234,543	205,390
Proceeds from sales	26,236	1,791
Purchases	(219,000)	(185,112)
Securities held to maturity:		
Proceeds from maturities, calls, and principal paydowns	16,822	16,655
Purchases	(71,988)	(9,858)
Net increase in loans	(119,872)	(142,433)
Net increase in Federal Reserve and FHLB stock	(5,584)	(672)
Purchases of premises and equipment	(2,272)	(2,769)
Proceeds from sales of other real estate owned	2,122	1,661
Net cash used in investing activities	(58,084)	(62,226)
Financing activities		
Net (decrease) increase in deposits	(19,593)	39,653
Net increase in short-term borrowings	201,066	30,611
Repayments of long-term debt	(163,307)	(3,347)
Issuance of shares to employee benefit plans and other stock plans	(965)	690
Purchase of treasury stock	(5,460)	(15,490)
Cash dividends and payment for fractional shares	(15,568)	(13,232)
Net cash (used in) provided by financing activities	(3,827)	38,885
Net (decrease) increase in cash and cash equivalents	(19,981)	9,783
Cash and cash equivalents at beginning of period	163,668	129,381
Cash and cash equivalents at end of period	$143,687	$139,164

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Supplemental disclosure of cash flow information	Six Months Ended June 30,	
Cash paid during the period for:	2013	2012
Interest	$16,853	$18,245
Income taxes paid	4,525	14,122
Noncash investing activities:		
Loans transferred to OREO	$3,031	$889
Acquisitions:		
Fair value of assets acquired	$1,503,810	$258,256
Fair value of liabilities assumed	1,284,038	285,403
Fair value of debt issued in asset purchase	-	150

See accompanying notes to unaudited interim consolidated financial statements.

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NBT BANCORP INC. and Subsidiaries
NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2013

Note 1. Description of Business

NBT Bancorp Inc. (the "Registrant") is a registered financial holding company incorporated in the State of Delaware in 1986, with its principal headquarters located in Norwich, New York. The Registrant is the parent holding company of NBT Bank, N.A. (the "Bank"), NBT Financial Services, Inc. ("NBT Financial"), NBT Holdings, Inc. ("NBT Holdings"), CNBF Capital Trust I, NBT Statutory Trust I, NBT Statutory Trust II, Alliance Financial Capital Trust I and Alliance Financial Capital Trust II (the "Trusts"). Through the Bank, the Company is focused on community banking operations. Through NBT Financial, the Company operates EPIC Advisors, Inc. ("EPIC"), a retirement plan administrator. Through NBT Holdings, the Company operates Mang Insurance Agency, LLC ("Mang"), a full-service insurance agency. The Trusts were organized to raise additional regulatory capital and to provide funding for certain acquisitions. The Registrant's primary business consists of providing commercial banking and financial services to customers in its market area. The principal assets of the Registrant are all of the outstanding shares of common stock of its direct subsidiaries, and its principal sources of revenue are the management fees and dividends it receives from the Bank, NBT Financial, and NBT Holdings.

The Bank is a full service commercial bank formed in 1856, which provides a broad range of financial products to individuals, corporations and municipalities throughout the central and upstate New York, northeastern Pennsylvania, northwestern Vermont, western Massachusetts, and southern New Hampshire market areas.

Note 2. Basis of Presentation

The accompanying unaudited interim consolidated financial statements include the accounts of the Registrant and its wholly owned subsidiaries, the Bank, NBT Financial and NBT Holdings. Collectively, the Registrant and its subsidiaries are referred to herein as "the Company." The interim data includes all adjustments, consisting only of normal recurring adjustments, necessary for a fair statement of the results for the interim periods in accordance with generally accepted accounting principles ("GAAP"). These consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in our 2012 Annual Report on Form 10-K. The results of operations for the interim periods are not necessarily indicative of the results that may be expected for the full year or any other interim period. All intercompany transactions have been eliminated in consolidation. Amounts in the prior period financial statements are reclassified whenever necessary to conform to current period presentation. The Company has evaluated subsequent events for potential recognition and/or disclosure and there were none identified.

Note 3. Acquisitions

Alliance Financial Corporation ("Alliance")
On March 8, 2013, the Company acquired Alliance, the parent company of Alliance Bank, N.A., for total consideration of $226 million. As part of the acquisition, Alliance was merged with and into the Company and Alliance Bank, with 26 branch locations in the central New York counties of Onondaga, Cortland, Madison, Oneida and Oswego, was merged with and into the Bank. The merger with Alliance enabled the Company to expand its footprint into demographically attractive and contiguous markets located in the aforementioned New York counties. Alliance operations were integrated into the Company and were included in the Consolidated Statements of Income from the date of acquisition.

Under the terms of the merger agreement, each outstanding share of Alliance common stock was converted into the right to receive 2.1779 shares of the Company's common stock. As a result, Alliance shareholders received 10.3

million shares of Company common stock valued at $226 million.

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In connection with the merger, the consideration paid and the fair value of the assets acquired and the liabilities assumed on the date of acquisition are as summarized in the following table, in thousands:

Consideration paid:	
NBT Bancorp common stock issued to Alliance common shareholders	$225,551
Cash in lieu of fractional shares paid to Alliance common shareholders	11
Less treasury shares	5,779
Net consideration paid	$219,783
Recognized Amounts of Identifiable Assets Acquired and (Liabilities Assumed) At Fair Value:	
Cash and short term investments	$81,060
Securities	320,618
Loans	904,473
Intangible assets	13,161
Other assets	71,823
Deposits	(1,113,420)
Borrowings	(126,530)
Trust preferred debentures	(25,774)
Other liabilities	(18,466)
Total identifiable net assets	$106,945
Goodwill	$112,838

The above recognized amounts of loans, other assets and other liabilities, at fair value, are preliminary estimates and are subject to adjustment but actual amounts are not expected to differ materially from those shown.

The estimated fair value of loans acquired from Alliance was determined by utilizing a methodology wherein similar loans were aggregated into pools. Cash flows for each pool were determined by estimating future credit losses and the rate of prepayments. Projected monthly cash flows were then discounted to present value based on a current market rate for similar loans. There was no carryover of Alliance’s allowance for credit losses associated with the loans acquired as loans were initially recorded at fair value.

Information about the acquired loan portfolio as of March 8, 2013 is as follows (in thousands):

Contractually required principal and interest at acquisition	$908,614
Contractual cash flows not expected to be collected	(15,466)
Expected cash flows at acquisition	893,148
Interest component of expected cash flows (accretable premium)	11,325
Fair value of acquired loans	$904,473

The following table presents changes in the accretable discount (in thousands):

Balance at January 1, 2013	$-
Alliance acquisition	11,325
Accretion recognized to date	(994)
Balance at June 30, 2013	$10,331

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The core deposit and trust intangible assets recognized as part of the Alliance merger are being amortized over their estimated useful lives of approximately 10 and 15 years, respectively, utilizing an accelerated method. The goodwill, which is not amortized for book purposes, is not deductible for tax purposes.

The fair value of savings and transaction deposit accounts acquired from Alliance was assumed to approximate the carrying value as these accounts have no stated maturity and are payable on demand. Certificates of deposit were valued by projecting the expected cash flows based on the contractual terms of the certificates of deposit. These cash flows were discounted based on a current market rate for a certificate of deposit with a corresponding maturity.

The fair value of borrowings, which was comprised of FHLB advances, was determined by obtaining settlement quotes from the FHLB.

Direct costs related to the Alliance acquisition were expensed as incurred and amounted to $12.0 million for the six months ended June 30, 2013.

The following table presents unaudited pro forma information as if the acquisition had occurred on January 1, 2012 under the “Pro forma” columns. This pro forma information gives effect to certain adjustments, including purchase accounting fair value adjustments, amortization of core deposit and other intangibles and related income tax effects. Merger and acquisition integration costs related to the Alliance acquisition are excluded from the periods in which they were incurred. The pro forma information does not necessarily reflect the results of operations that would have occurred had the Company merged with Alliance at the beginning of 2012. Cost savings are also not reflected in the unaudited pro forma amounts for the six months ended June 30, 2012 and 2013.

	Pro forma Six months ended June 30,	
	2013	2012
Net interest income	$120,593	$119,471
Noninterest income	55,445	52,738
Net income	33,911	32,104

Supplemental financial information regarding the former Alliance operations included in our Consolidated Statement of Income from the date of acquisition through June 30, 2013 has not been provided as it would be impracticable to do so. The operations of Alliance have been integrated into the Bank’s operations and therefore financial information specific to revenues and expense associated with the former Alliance operations is not accessible.

Other Goodwill Adjustments

During the six months ended June 30, 2013, the Company recorded a deferred tax adjustment related to the 2012 acquistion of Hampshire First Bank resulting in a decrease in goodwill of approximately $1.0 million. In addition, the Company recorded a goodwill adjustment of approximately $0.1 million related to the 2012 acquisition of a financial services company.

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Note 4. Commitments and Contingencies

The Company is a party to financial instruments in the normal course of business to meet the financing needs of its customers and to reduce its own exposure to fluctuating interest rates. These financial instruments include commitments to extend credit, unused lines of credit, and standby letters of credit. Exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to make loans and standby letters of credit is represented by the contractual amount of those instruments. The Company uses the same credit origination guidelines, portfolio maintenance and management procedures as other credit and off-balance sheet products. Commitments to extend credit and unused lines of credit totaled $1.1 billion at June 30, 2013 and $841.7 million at December 31, 2012. Since commitments to extend credit and unused lines of credit may expire without being fully drawn upon, this amount does not necessarily represent future cash commitments. Collateral obtained upon exercise of the commitment is determined using management’s credit evaluation of the borrower and may include accounts receivable, inventory, property, land and other items.

The Company guarantees the obligations or performance of customers by issuing standby letters of credit to third parties. These standby letters of credit are frequently issued in support of third party debt, such as corporate debt issuances, industrial revenue bonds and municipal securities. The credit risk involved in issuing standby letters of credit is essentially the same as the credit risk involved in extending loan facilities to customers, and they are subject to the same credit origination guidelines, portfolio maintenance and management procedures as other credit and off-balance sheet products. Typically, these instruments have terms of five years or less and expire unused; therefore, the total amounts do not necessarily represent future cash commitments. Standby letters of credit totaled $41.5 million at June 30, 2013 and $37.5 million at December 31, 2012. As of June 30, 2013, the fair value of standby letters of credit was not significant to the Company’s consolidated financial statements.

The Company has also entered into commercial letter of credit agreements on behalf of its customers. Under these agreements, the Company, on the request of its customer, opens the letter of credit and makes a commitment to honor draws made under the agreement, whereby the beneficiary is normally the provider of goods and/or services and the Company essentially replaces the customer as the payee. The credit risk involved in issuing commercial letters of credit is essentially the same as the credit risk involved in extending loan facilities to customers, and they are subject to the same credit origination guidelines, portfolio maintenance and management procedures as other credit and off-balance sheet products. Typically, these agreements vary in terms and the total amounts do not necessarily represent future cash commitments. Commercial letters of credit totaled $36.9 million at June 30, 2013 and $16.6 million at December 31, 2012. As of June 30, 2013, the fair value of commercial letters of credit was not significant to the Company’s consolidated financial statements.

Note 5. Allowance for Loan Losses and Credit Quality of Loans

Allowance for Loan Losses

The allowance for loan losses is maintained at a level estimated by management to provide adequately for risk of probable losses inherent in the current loan portfolio. The adequacy of the allowance for loan losses is continuously monitored. It is assessed for adequacy using a methodology designed to ensure the level of the allowance reasonably reflects the loan portfolio’s risk profile. It is evaluated to ensure that it is sufficient to absorb all reasonably estimable credit losses inherent in the current loan portfolio.

To develop and document a systematic methodology for determining the allowance for loan losses, the Company has divided the loan portfolio into three segments, each with different risk characteristics and methodologies for assessing risk. Those segments are further segregated between our loans accounted for under the amortized cost method (referred to as “originated” loans) and loans acquired in a business combination (referred to as “acquired” loans). Prior to 2013, separate disclosures for acquired loans were not significant and were included with originated loans in the Company’s asset quality disclosures. Each portfolio segment is broken down into class segments where appropriate.

Class segments contain unique measurement attributes, risk characteristics and methods for monitoring and assessing risk that are necessary to develop the allowance for loan losses. Unique characteristics such as borrower type, loan type, collateral type, and risk characteristics define each class segment. The following table illustrates the portfolio and class segments for the Company’s loan portfolio:

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Portfolio	Class
Commercial Loans	Commercial
	Commercial Real Estate
	Agricultural
	Agricultural Real Estate
	Business Banking
Consumer Loans	Indirect
	Home Equity
	Direct
Residential Real Estate Mortgages	

Commercial Loans

The Company offers a variety of commercial loan products including commercial (non-real estate), commercial real estate, agricultural, agricultural real estate, and business banking loans. The Company's underwriting analysis for commercial loans typically includes credit verification, independent appraisals, a review of the borrower's financial condition, and a detailed analysis of the borrower's underlying cash flows.

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 is generally less liquid than real estate. To reduce the risk, management also attempts to secure real estate as collateral and obtain 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 other 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.

Agricultural – The Company offers a variety of agricultural loans to meet the needs of our agricultural customers including term loans, time notes, and lines of credit. These loans are made to purchase livestock, purchase and modernize equipment, and finance seasonal crop expenses. Generally, a collateral lien is placed on the livestock, equipment, produce inventories, and/or receivables owned by the borrower. These loans may carry a higher risk than commercial and agricultural real estate loans due to the industry price volatility, and in some cases, the perishable nature of the underlying collateral. To reduce these risks, management may attempt to secure these loans with additional real estate collateral, obtain personal guarantees of the borrowers, or obtain government loan guarantees to provide further support.

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Agricultural Real Estate – The Company offers real estate loans to our agricultural customers to finance farm related real estate purchases, refinancings, expansions, and improvements to agricultural properties such as barns, production facilities, and land. The agricultural real estate loans are secured by first liens on the farm real estate. Because they are secured by land and buildings, these loans may be less risky than agricultural loans. These loans are typically originated in amounts of no more than 75% of the appraised value of the property. Government loan guarantees may be obtained to provide further support.

Business Banking - The Company offers a variety of loan options to meet the specific needs of our business banking customers including term loans, business banking mortgages and lines of credit. Such loans are generally less than \$0.5 million and are made available to businesses for working capital such as inventory and receivables, business expansion, equipment purchases, and agricultural needs. Generally, a collateral lien is placed on equipment or other assets owned by the borrower such as inventory and/or receivables. These loans carry a higher risk than commercial loans due to the smaller size of the borrower and lower levels of capital. To reduce the risk, the Company obtains personal guarantees of the owners for a majority of the loans.

Consumer Loans

The Company offers a variety of consumer loan products including indirect, home equity, and direct loans.

Indirect – The Company maintains relationships with many dealers primarily in the communities that we serve. Through these relationships, the company finances the purchases of automobiles and recreational vehicles (such as campers, boats, etc.) indirectly through dealer relationships. Approximately 75% of the indirect relationships represent automobile financing. Most of these loans carry a fixed rate of interest with principal repayment terms typically ranging from three to six years, based upon the nature of the collateral and the size of the loan. The majority of indirect consumer loans are underwritten on a secured basis using the underlying collateral being financed.

Home Equity – 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. Consumers are able to borrow up to 85% of the equity in their homes. 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). These loans carry a higher risk than first mortgage residential loans as they are in a second position with respect to collateral. Risk is 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.

Direct – The Company offers a variety of consumer installment loans to finance vehicle purchases, mobile home purchases and personal expenditures. Most of these loans carry a fixed rate of interest with principal repayment terms typically ranging from one to ten years, based upon the nature of the collateral and the size of the loan. The majority of consumer loans are underwritten on a secured basis using the underlying collateral being financed or a customer's deposit account. In addition to installment loans, the Company also offers personal lines of credit and overdraft protection. A minimal amount of loans are unsecured, which carry a higher risk of loss.

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Residential Real Estate Mortgages

Residential real estate loans consist primarily of loans secured by first or second deeds of trust on primary residences. We originate adjustable-rate and fixed-rate, one-to-four-family residential real estate loans for the construction, purchase or refinancing of a mortgage. These loans are collateralized by owner-occupied properties located in the Company's market area. Loans on one-to-four-family residential real estate are generally originated in amounts of no more than 85% of the purchase price or appraised value (whichever is lower), or have private mortgage insurance. The Company's underwriting analysis for residential mortgage loans typically includes credit verification, independent appraisals, and a review of the borrower's financial condition. Mortgage title insurance and hazard insurance are normally required. Construction loans have a unique risk, because they are secured by an incomplete dwelling. This risk is reduced through periodic site inspections, including one at each loan draw period.

For purposes of evaluating the adequacy of the allowance, the Company considers a number of significant factors that affect the collectability of the portfolio. For individually analyzed loans, these include estimates of loss exposure, which reflect the facts and circumstances that affect the likelihood of repayment of such loans as of the evaluation date. For homogeneous pools of loans, estimates of the Company's exposure to credit loss reflect a current assessment of a number of factors, which could affect collectability. These factors include: past loss experience; size, trend, composition, and nature of loans; changes in lending policies and procedures, including underwriting standards and collection, charge-offs and recoveries; trends experienced in nonperforming and delinquent loans; current economic conditions in the Company's market; portfolio concentrations that may affect loss experienced across one or more components of the portfolio; the effect of external factors such as competition, legal and regulatory requirements; and the experience, ability, and depth of lending management and staff. In addition, various regulatory agencies, as an integral component of their examination process, periodically review the Company's allowance for loan losses. Such agencies may require the Company to make loan grade changes as well as recognize additions to the allowance based on their examinations.

After a thorough consideration of the factors discussed above, any required additions or reductions to the allowance for loan losses are made periodically by charges or credits to the provision for loan losses. These charges or credits are necessary to maintain the allowance at a level which management believes is reasonably reflective of overall inherent risk of probable loss in the portfolio. While management uses available information to recognize losses on loans, additions and reductions of the allowance may fluctuate from one reporting period to another. These fluctuations are reflective of changes in risk associated with portfolio content and/or changes in management's assessment of any or all of the determining factors discussed above.

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The following tables illustrate the changes in the allowance for loan losses by our portfolio segments for the three and six months ended June 30, 2013 and 2012:

Three months ended June 30	Commercial Loans	Consumer Loans	Residential Real Estate Mortgages	Unallocated	Total
Balance as of March 31, 2013	$ 35,358	$ 26,285	$ 6,708	$ 383	$ 68,734
Charge-offs	(1,198)	(3,653)	(302)	-	(5,153)
Recoveries	416	696	89	-	1,201
Provision	3,128	3,128	311	(165)	6,402
Ending Balance as of June 30, 2013	$ 37,704	$ 26,456	$ 6,806	$ 218	$ 71,184
Balance as of March 31, 2012	$ 37,787	$ 26,790	$ 6,520	$ 237	$ 71,334
Charge-offs	(1,653)	(3,735)	(292)	-	(5,680)
Recoveries	303	667	7	-	977
Provision	1,058	3,513	(292)	(176)	4,103
Ending Balance as of June 30, 2012	$ 37,495	$ 27,235	$ 5,943	$ 61	$ 70,734

Six months ended June 30	Commercial Loans	Consumer Loans	Residential Real Estate Mortgages	Unallocated	Total
Balance as of December 31, 2012	$ 35,624	$ 27,162	$ 6,252	$ 296	$ 69,334
Charge-offs	(4,520)	(7,376)	(973)	-	(12,869)
Recoveries	883	1,673	103	-	2,659
Provision	5,717	4,997	1,424	(78)	12,060
Ending Balance as of June 30, 2013	$ 37,704	$ 26,456	$ 6,806	$ 218	$ 71,184
Balance as of December 31, 2011	$ 38,831	$ 26,049	$ 6,249	$ 205	$ 71,334
Charge-offs	(2,783)	(7,787)	(650)	-	(11,220)
Recoveries	688	1,342	16	-	2,046
Provision	759	7,631	328	(144)	8,574
Ending Balance as of June 30, 2012	$ 37,495	$ 27,235	$ 5,943	$ 61	$ 70,734

For acquired loans, to the extent that we experience deterioration in borrower credit quality resulting in a decrease in our expected cash flows subsequent to acquisition of the loans, an allowance for loan losses would be established based on our estimate of future credit losses over the remaining life of the loans. As of June 30, 2013 and 2012, there was no allowance for loan losses for the acquired loan portfolio. Net charge-offs related to acquired loans totaled $0.2 million and $0.4 million during the three and six months ended June 30, 2013, respectively, and are included in the table above.

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The following tables illustrate the allowance for loan losses and the recorded investment by portfolio segments as of June 30, 2013 and December 31, 2012:

Allowance for Loan Losses and Recorded Investment in Loans
(in thousands)

	Commercial Loans	Consumer Loans	Residential Real Estate Mortgages	Unallocated	Total
As of June 30, 2013					
Allowance for loan losses	$37,704	$26,456	$6,806	$ 218	$71,184
Allowance for loans individually evaluated for impairment	$2,032	$-	$-		$2,032
Allowance for loans collectively evaluated for impairment	$35,672	$26,456	$6,806	$ 218	$69,152
Ending balance of loans	$2,368,897	$1,920,171	$1,001,642		$5,290,710
Ending balance of loans individually evaluated for impairment	$12,887	$-	$-		$12,887
Ending balance of acquired loans	$460,995	$269,151	$338,750		$1,068,896
Ending balance of loans collectively evaluated for impairment	$1,895,015	$1,651,020	$662,892		$4,208,927
As of December 31, 2012					
Allowance for loan losses	$35,624	$27,162	$6,252	$296	$69,334
Allowance for loans individually evaluated for impairment	$2,848	$-	$-		$2,848
Allowance for loans collectively evaluated for impairment	$32,776	$27,162	$6,252	$296	$66,486
Ending balance of loans	$2,003,371	$1,623,138	$651,107		$4,277,616
Ending balance of loans individually evaluated for impairment	$11,972	$-	$-		$11,972
Ending balance of loans collectively evaluated for impairment	$1,991,399	$1,623,138	$651,107		$4,265,644

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Credit Quality of Loans

Loans are placed on nonaccrual status when timely collection of principal and interest in accordance with contractual terms is doubtful. Loans are transferred to nonaccrual status generally when principal or interest payments become ninety days delinquent, unless the loan is well secured and in the process of collection, or sooner when management concludes or circumstances indicate that borrowers may be unable to meet contractual principal or interest payments. When a loan is transferred to a nonaccrual status, all interest previously accrued in the current period but not collected is reversed against interest income in that period. Interest accrued in a prior period and not collected is charged-off against the allowance for loan losses. The Company’s nonaccrual policies are the same for all classes of financing receivable.

If ultimate repayment of a nonaccrual loan is expected, any payments received are applied in accordance with contractual terms. If ultimate repayment of principal is not expected, any payment received on a nonaccrual loan is applied to principal until ultimate repayment becomes expected. Nonaccrual loans are returned to accrual status when they become current as to principal and interest and demonstrate a period of performance under the contractual terms and, in the opinion of management, are fully collectible as to principal and interest. When in the opinion of management the collection of principal appears unlikely, the loan balance is charged-off in total or in part. For loans in all portfolios, the principal amount is charged off in full or in part as soon as management determines, based on available facts, that the collection of principal in full is improbable. For commercial loans, management considers specific facts and circumstances relative to individual credits in making such a determination. For consumer and residential loan classes, management uses specific guidance and thresholds from the Federal Financial Institutions Examination Council’s Uniform Retail Credit Classification and Account Management Policy.

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The following table illustrates the Company's nonaccrual loans by loan class:

Loans on Nonaccrual Status as of:

(In thousands)	June 30, 2013	December 31, 2012
ORIGINATED		
Commercial Loans		
Commercial	$ 2,622	$ 4,985
Commercial Real Estate	10,716	7,977
Agricultural	595	699
Agricultural Real Estate	968	1,038
Business Banking	5,658	6,738
	20,559	21,437
Consumer Loans		
Indirect	1,301	1,557
Home Equity	6,583	7,247
Direct	128	266
	8,012	9,070
Residential Real Estate Mortgages	6,414	9,169
	$ 34,985	$ 39,676
ACQUIRED		
Commercial Loans		
Commercial	$ 446	
Commercial Real Estate	-	
Business Banking	1,593	
	2,039	
Consumer Loans		
Indirect	139	
Home Equity	425	
Direct	74	
	638	
Residential Real Estate Mortgages	2,863	
	$ 5,540	
Total nonaccrual loans	$ 40,525	$ 39,676

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The following tables set forth information with regard to past due and nonperforming loans by loan class as of June 30, 2013 and December 31, 2012:

Age Analysis of Past Due Financing Receivables
As of June 30, 2013
(in thousands)

	31-60 Days Past Due Accruing	61-90 Days Past Due Accruing	Greater Than 90 Days Past Due Accruing	Total Past Due Accruing	Non-Accrual	Current	Recorded Total Loans and Leases
ORIGINATED							
Commercial Loans							
Commercial	$ 195	$ 20	$ -	$ 215	$ 2,622	$ 583,101	$ 585,938
Commercial Real Estate	1,692	-	-	1,692	10,716	875,555	887,963
Agricultural	154	20	-	174	595	63,834	64,603
Agricultural Real Estate	349	-	-	349	968	30,894	32,211
Business Banking	2,176	590	-	2,766	5,658	328,763	337,187
	4,566	630	-	5,196	20,559	1,882,147	1,907,902
Consumer Loans							
Indirect	10,749	2,259	832	13,840	1,301	1,033,903	1,049,044
Home Equity	6,475	1,198	704	8,377	6,583	525,429	540,389
Direct	611	210	45	866	128	60,593	61,587
	17,835	3,667	1,581	23,083	8,012	1,619,925	1,651,020
Residential Real Estate							
Mortgages	487	1,085	358	1,930	6,414	654,548	662,892
	$ 22,888	$ 5,382	$ 1,939	$ 30,209	$ 34,985	$ 4,156,620	$ 4,221,814
ACQUIRED							
Commercial Loans							
Commercial	$ 473	$ 5	$ -	$ 478	$ 446	$ 137,215	$ 138,139
Commercial Real Estate	-	-	-	-	-	242,322	242,322
Agricultural	-	-	-	-	-	25	25
Business Banking	74	-	-	74	1,593	78,842	80,509
	547	5	-	552	2,039	458,404	460,995
Consumer Loans							
Indirect	751	162	23	936	139	164,267	165,342
Home Equity	307	754	38	1,099	425	93,370	94,894
Direct	38	30	4	72	74	8,769	8,915
	1,096	946	65	2,107	638	266,406	269,151
Residential Real Estate							
Mortgages	2,292	230	-	2,522	2,863	333,365	338,750
	$ 3,935	$ 1,181	$ 65	$ 5,181	$ 5,540	$ 1,058,175	$ 1,068,896
Total Loans	$ 26,823	$ 6,563	$ 2,004	$ 35,390	$ 40,525	$ 5,214,795	$ 5,290,710

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As of December 31, 2012
(in thousands)

	31-60 Days Past Due Accruing	61-90 Days Past Due Accruing	Greater Than 90 Days Past Due Accruing	Total Past Due Accruing	Non-Accrual	Current	Recorded Total Loans
Commercial Loans							
Commercial	$ -	$ -	$ -	$ -	$ 4,985	$ 556,496	$ 561,481
Commercial Real Estate	126	-	-	126	7,977	966,692	974,795
Agricultural	22	-	-	22	699	63,037	63,758
Agricultural Real Estate	108	-	103	211	1,038	36,128	37,377
Business Banking	3,019	708	45	3,772	6,738	355,450	365,960
	3,275	708	148	4,131	21,437	1,977,803	2,003,371
Consumer Loans							
Indirect	10,956	2,477	1,205	14,638	1,557	964,802	980,997
Home Equity	6,065	1,223	681	7,969	7,247	560,066	575,282
Direct	717	144	84	945	266	65,648	66,859
	17,738	3,844	1,970	23,552	9,070	1,590,516	1,623,138
Residential Real Estate Mortgages	1,839	725	330	2,894	9,169	639,044	651,107
	$ 22,852	$ 5,277	$ 2,448	$ 30,577	$ 39,676	$ 4,207,363	$ 4,277,616

There were no material commitments to extend further credit to borrowers with nonperforming loans.

Impaired Loans

The methodology used to establish the allowance for loan losses on impaired loans incorporates specific allocations on loans analyzed individually. Classified loans with outstanding balances of $0.5 million or more are evaluated for impairment through the Company's quarterly status review process. In determining that we will be unable to collect all principal and interest payments due in accordance with the contractual terms of the loan agreements, we consider factors such as payment history and changes in the financial condition of individual borrowers, local economic conditions, historical loss experience and the conditions of the various markets in which the collateral may be liquidated. For loans that are impaired as defined by accounting standards, impairment is measured by one of three methods: 1) the fair value of collateral less cost to sell, 2) present value of expected future cash flows or 3) the loan's observable market price. All impaired loans are reviewed on a quarterly basis for changes in the measurement of impairment. Any change to the previously recognized impairment loss is recognized as a change to the allowance account and recorded in the consolidated statement of income as a component of the provision for credit losses.

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The following table provides information on impaired loans and specific reserve allocations as of June 30, 2013 and December 31, 2012:

(in thousands)	June 30, 2013 Recorded Investment Balance (Book)	June 30, 2013 Unpaid Principal Balance (Legal)	June 30, 2013 Related Allowance	December 31, 2012 Recorded Investment Balance (Book)	December 31, 2012 Unpaid Principal Balance (Legal)	December 31, 2012 Related Allowance
With no related allowance recorded:						
Commercial Loans						
Commercial	$4,067	$5,337		$1,651	$1,710	
Commercial Real Estate	4,347	5,134		8,709	9,553	
Agricultural	616	917		940	1,286	
Agricultural Real Estate	1,634	1,955		1,713	2,026	
Business Banking	7,534	10,213		7,048	9,579	
Total Commercial Loans	18,198	23,556		20,061	24,154	
Consumer Loans						
Home Equity	2,971	3,156		2,553	2,657	
Residential Real Estate Mortgages	2,018	2,360		2,011	2,308	
	$23,187	$29,072		$24,625	$29,119	
With an allowance recorded:						
Commercial Loans						
Commercial	$-	$-	$ -	$4,335	$4,340	$ 2,241
Commercial Real Estate	7,302	8,924	2,032	4,068	5,689	607
Agricultural	-	-	-	-	-	-
Agricultural Real Estate	-	-	-	-	-	-
	7,302	8,924	2,032	8,403	10,029	2,848
Total:	$30,489	$37,996	$ 2,032	$33,028	$39,148	$ 2,848

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The following tables summarize the average recorded investments on impaired loans and the interest income recognized for the three and six months ended June 30, 2013 and 2012:

	For the three months ended			
	June 30, 2013		June 30, 2012	
(in thousands)	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
Commercial Loans				
Commercial	$2,822	$ 15	$1,128	$ 46
Commercial Real Estate	8,616	11	7,140	-
Agricultural	770	-	2,876	5
Agricultural Real Estate	1,123	12	1,876	53
Business Banking	7,843	16	6,572	8
Consumer Loans				
Home Equity	2,907	6	1,828	2
Residential Real Estate Mortgages	1,990	15	1,055	-
Total:	$26,071	$ 75	$22,475	$ 114

	For the six months ended			
	June 30, 2013		June 30, 2012	
(in thousands)	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
Commercial Loans				
Commercial	$4,430	$ 30	$1,551	$ 69
Commercial Real Estate	10,614	72	6,481	-
Agricultural	887	3	2,997	36
Agricultural Real Estate	1,482	24	1,926	53
Business Banking	8,016	30	7,151	12
Consumer Loans				
Home Equity	2,775	12	1,869	3
Residential Real Estate Mortgages	1,989	27	1,043	-
Total:	$30,193	$ 198	$23,018	$ 173

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Credit Quality Indicators

The Company has developed an internal loan grading system to evaluate and quantify the Bank's loan portfolio with respect to quality and risk. The system focuses on, among other things, financial strength of borrowers, experience and depth of borrower's management, primary and secondary sources of repayment, payment history, nature of the business, and outlook on particular industries. The internal grading system enables the Company to monitor the quality of the entire loan portfolio on a consistent basis and provide management with an early warning system, enabling recognition and response to problem loans and potential problem loans.

Commercial Grading System

For commercial and agricultural loans, the Company uses a grading system that relies on quantifiable and measurable characteristics when available. This would include comparison of financial strength to available industry averages, comparison of transaction factors (loan terms and conditions) to loan policy, and comparison of credit history to stated repayment terms and industry averages. Some grading factors are necessarily more subjective such as economic and industry factors, regulatory environment, and management. Classified commercial loans consist of loans graded substandard and below. The grading system for commercial and agricultural loans is as follows:

· Doubtful

A doubtful loan has a high probability of total or substantial loss, but because of specific pending events that may strengthen the asset, its classification as a loss is deferred. Doubtful borrowers are usually in default, lack adequate liquidity or capital, and lack the resources necessary to remain an operating entity. Pending events can include mergers, acquisitions, liquidations, capital injections, the perfection of liens on additional collateral, the valuation of collateral, and refinancing. Generally, pending events should be resolved within a relatively short period and the ratings will be adjusted based on the new information. Nonaccrual treatment is required for doubtful assets because of the high probability of loss.

· Substandard

Substandard loans have a high probability of payment default, or they have other well-defined weaknesses. They require more intensive supervision by bank management. Substandard loans are generally characterized by current or expected unprofitable operations, inadequate debt service coverage, inadequate liquidity, or marginal capitalization. Repayment may depend on collateral or other credit risk mitigants. For some Substandard loans, the likelihood of full collection of interest and principal may be in doubt and those loans should be placed on nonaccrual. Although Substandard assets in the aggregate will have a distinct potential for loss, an individual asset's loss potential does not have to be distinct for the asset to be rated Substandard.

· Special Mention

Special Mention loans have potential weaknesses that may, if not checked or corrected, weaken the asset or inadequately protect the Company's position at some future date. These loans pose elevated risk, but their weakness does not yet justify a Substandard classification. Borrowers may be experiencing adverse operating trends (declining revenues or margins) or may be struggling with an ill-proportioned balance sheet (e.g., increasing inventory without an increase in sales, high leverage, tight liquidity). Adverse economic or market conditions, such as interest rate increases or the entry of a new competitor, may also support a Special Mention rating. Although a Special Mention loan has a higher probability of default than a pass asset, its default is not imminent.

· Pass

Loans graded as Pass encompass all loans not graded as Doubtful, Substandard, or Special Mention. Pass loans are in compliance with loan covenants, and payments are generally made as agreed. Pass loans range from superior quality to fair quality.

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Business Banking Grading System

Business banking loans are graded as either Classified or Non-classified:

- Classified

Classified loans are inadequately protected by the current worth and paying capacity of the obligor or, if applicable, the collateral pledged. These loans have a well-defined weakness, or weaknesses, that jeopardize the liquidation of the debt, or in some cases make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable. They are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected. Classified loans have a high probability of payment default, or a high probability of total or substantial loss. These loans require more intensive supervision by management and are generally characterized by current or expected unprofitable operations, inadequate debt service coverage, inadequate liquidity, or marginal capitalization. Repayment may depend on collateral or other credit risk mitigants. When the likelihood of full collection of interest and principal may be in doubt; classified loans are considered to have a nonaccrual status. In some cases, Classified loans are considered uncollectible and of such little value that their continuance as assets is not warranted.

- Non-classified

Loans graded as Non-classified encompass all loans not graded as Classified. Non-classified loans are in compliance with loan covenants, and payments are generally made as agreed.

Consumer and Residential Mortgage Grading System

Consumer and Residential Mortgage loans are graded as either Performing or Nonperforming. Nonperforming loans are loans that are 1) over 90 days past due and interest is still accruing, 2) on nonaccrual status or 3) restructured. All loans not meeting any of these three criteria are considered Performing.

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The following tables illustrate the Company's credit quality by loan class as of June 30, 2013 and December 31, 2012:

Credit Quality Indicators
As of June 30, 2013

ORIGINATED

Commercial Credit Exposure By Internally Assigned Grade:	Commercial	Commercial Real Estate	Agricultural	Agricultural Real Estate	Total
Pass	$ 566,686	$ 855,687	$ 59,026	$ 28,722	$ 1,510,121
Special Mention	1,899	11,657	78	3	13,637
Substandard	16,850	19,856	5,476	3,486	45,668
Doubtful	503	763	23	-	1,289
Total	$ 585,938	$ 887,963	$ 64,603	$ 32,211	$ 1,570,715

Business Banking Credit Exposure By Internally Assigned Grade:	Small Business	Total
Non-classified	$ 317,362	$ 317,362
Classified	19,825	19,825
Total	$ 337,187	$ 337,187

Consumer Credit Exposure By Payment Activity:	Indirect	Home Equity	Direct	Total
Performing	$ 1,046,911	$ 533,102	$ 61,414	$ 1,641,427
Nonperforming	2,133	7,287	173	9,593
Total	$ 1,049,044	$ 540,389	$ 61,587	$ 1,651,020

Residential Mortgage Credit Exposure By Payment Activity:	Residential Mortgage	Total
Performing	$ 656,120	$ 656,120
Nonperforming	6,772	6,772
Total	$ 662,892	$ 662,892

Credit Quality Indicators
As of June 30, 2013

ACQUIRED

Commercial Credit Exposure By Internally Assigned Grade:	Commercial	Commercial Real Estate	Agricultural	Total
Pass	$ 121,901	$ 220,131	$ 25	$ 342,057
Special Mention	8,323	8,822	-	17,145
Substandard	7,915	13,369	-	21,284
Doubtful	-	-	-	-
Total	$ 138,139	$ 242,322	$ 25	$ 380,486

Business Banking Credit Exposure By Internally Assigned Grade:	Small Business	Total
Non-classified	$ 75,418	$ 75,418

Classified	5,091			5,091
Total	$ 80,509			$80,509

Consumer Credit Exposure				
By Payment Activity:	Indirect	Home Equity	Direct	Total
Performing	$ 165,180	$ 94,006	$ 8,763	$267,949
Nonperforming	162	888	152	1,202
Total	$ 165,342	$ 94,894	$ 8,915	$269,151

Residential Mortgage Credit Exposure By Payment Activity:	Residential Mortgage	Total
Performing	$ 335,887	$335,887
Nonperforming	2,863	2,863
Total	$ 338,750	$338,750

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Credit Quality Indicators
As of December 31, 2012

Commercial Credit Exposure By Internally Assigned Grade:	Commercial	Commercial Real Estate	Agricultural	Agricultural Real Estate	Total
Pass	$ 522,985	$ 901,928	$ 57,347	$ 33,472	$1,515,732
Special Mention	18,401	32,135	13	3	50,552
Substandard	17,351	40,732	6,362	3,902	68,347
Doubtful	2,744	-	36	-	2,780
Total	$ 561,481	$ 974,795	$ 63,758	$ 37,377	$1,637,411

Business Banking. Credit Exposure By Internally Assigned Grade:	Small Business	Total
Non-classified	$ 342,528	$342,528
Classified	23,432	23,432
Total	$ 365,960	$365,960

Consumer Credit Exposure By Payment Activity:	Indirect	Home Equity	Direct	Total
Performing	$ 978,235	$ 567,354	$ 66,509	$1,612,098
Nonperforming	2,762	7,928	350	11,040
Total	$ 980,997	$ 575,282	$ 66,859	$1,623,138

Residential Mortgage Credit Exposure By Payment Activity:	Residential Mortgage	Total
Performing	$ 641,608	$641,608
Nonperforming	9,499	9,499
Total	$ 651,107	$651,107

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Troubled Debt Restructured Loans

The Company's loan portfolio includes certain loans that have been modified where economic concessions have been granted to borrowers who have experienced or are expected to experience financial difficulties. These concessions typically result from the Company's loss mitigation activities and could include reductions in the interest rate, payment extensions, forgiveness of principal, forbearance or other actions. Certain troubled debt restructured loans ("TDRs") are classified as nonperforming at the time of restructure and may only be returned to performing status after considering the borrower's sustained repayment performance for a reasonable period, generally six months.

When the Company modifies a loan, management evaluates any possible impairment based on the present value of the expected future cash flows, discounted at the contractual interest rate of the original loan agreement, except when the sole (remaining) source of repayment for the loan is the operation or liquidation of the collateral. In these cases, management uses the current fair value of the collateral, less selling costs, instead of discounted cash flows. If management determines that the value of the modified loan is less than the recorded investment in the loan (net of previous charge-offs, deferred loan fees or costs and unamortized premium or discount), impairment is recognized by segment or class of loan as applicable, through an allowance estimate or a charge-off to the allowance. Segment and class status is determined by the loan's classification at origination.

TDRs that occurred during the three month period ending June 30, 2013 consisted of 10 home equity loans, one residential real estate mortgage, and one commercial real estate loan totaling $0.5 million, $0.1 million, and $0.9 million, respectively. For all such modifications, the pre and post outstanding recorded investment amount remained unchanged. During the three month period ending June 30, 2013 there were three defaults on home equity loans totaling $0.2 million.

TDRs that occurred during the three month period ending June 30, 2012 consisted of 1 commercial loan totaling $1.0 million. The pre and post outstanding recorded investment amount remained unchanged. During the three month period ending June 30, 2012 there was one default on a home equity loan and three defaults on residential real estate mortgages totaling $25,000 and $0.4 million, respectively, on previously modified loans.

TDRs that occurred during the six month period ending June 30, 2013 consisted of 14 home equity loans, one residential real estate mortgage, and one commercial real estate loan totaling $0.6 million, $0.1 million, and $0.9 million, respectively. For all such modifications, the pre and post outstanding recorded investment amount remained unchanged. During the six month period ending June 30, 2013 there were three defaults on home equity loans totaling $0.2 million.

TDRs that occurred during the six month period ending June 30, 2012 consisted of 1 commercial loan totaling $1.0 million and one residential real estate mortgage totaling $0.2 million. The pre and post outstanding recorded investment amount remained unchanged. During the six month period ending June 30, 2012 there was one default on a home equity loan totaling $25,000 that was previously modified.

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Note 6. Earnings Per Share

Basic earnings per share excludes dilution and is computed by dividing income available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted earnings per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the entity (such as the Company’s dilutive stock options and restricted stock units).

The following is a reconciliation of basic and diluted earnings per share for the periods presented in the consolidated statements of income.

Three months ended June 30,	2013	2012
(in thousands, except per share data)		
Basic EPS:		
Weighted average common shares outstanding	43,923	33,191
Net income available to common shareholders	16,916	13,257
Basic EPS	$0.39	$0.40
Diluted EPS:		
Weighted average common shares outstanding	43,923	33,191
Dilutive effect of common stock options and restricted stock	393	301
Weighted average common shares and common share equivalents	44,316	33,492
Net income available to common shareholders	16,916	13,257
Diluted EPS	$0.38	$0.40

Six months ended June 30,	2013	2012
(in thousands, except per share data)		
Basic EPS:		
Weighted average common shares outstanding	40,187	33,128
Net income available to common shareholders	24,565	26,907
Basic EPS	$0.61	$0.81
Diluted EPS:		
Weighted average common shares outstanding	40,187	33,128
Dilutive effect of common stock options and restricted stock	388	325
Weighted average common shares and common share equivalents	40,575	33,453
Net income available to common shareholders	24,565	26,907
Diluted EPS	$0.61	$0.80

There were 1,231,395 stock options for the quarter ended June 30, 2013 and 1,271,116 stock options for the quarter ended June 30, 2012 that were not considered in the calculation of diluted earnings per share since the stock options’ exercise price was greater than the average market price during these periods.

There were 1,203,046 stock options for the six months ended June 30, 2013 and 1,209,201 stock options for the six months ended June 30, 2012 that were not considered in the calculation of diluted earnings per share since the stock options’ exercise price was greater than the average market price during these periods.

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Note 7. Defined Benefit Postretirement Plans

The Company has a qualified, noncontributory, defined benefit pension plan covering substantially all of its employees at June 30, 2013, including eligible Alliance employees as of March 8, 2013. Benefits paid from the plan are based on age, years of service, compensation and social security benefits, and are determined in accordance with defined formulas. The Company's policy is to fund the pension plan in accordance with Employee Retirement Income Security Act of 1974 ("ERISA") standards. Assets of the plan are invested in publicly traded stocks and bonds.

The Company assumed a noncontributory, defined benefit pension plan in the Alliance acquisition. The plan covers certain Alliance full-time employees who met eligibility requirements on October 6, 2006, at which time all benefits were frozen. Under the plan, retirement benefits are primarily a function of both the years of service and the level of compensation. The Company is not required to make contributions to the plans in 2013, and did not do so during the six months ended June 30, 2013. Effective May 1, 2013, this plan was merged into the NBT Bancorp Inc. Defined Benefit Pension Plan. The merging of the plans did not have a significant impact on the Company's financial statements and related footnotes.

In addition to the pension plans, the Company also provides supplemental employee retirement plans to certain current and former executives. These supplemental employee retirement plans and the defined benefit pension plans are collectively referred to herein as "Pension Benefits."

Also, the Company provides certain health care benefits for retired employees. Benefits are accrued over the employees' active service period. Only employees that were employed by the Company on or before January 1, 2000 are eligible to receive postretirement health care benefits. The plan is contributory for participating retirees, requiring participants to absorb certain deductibles and coinsurance amounts with contributions adjusted annually to reflect cost sharing provisions and benefit limitations called for in the plan. Eligibility is contingent upon the direct transition from active employment status to retirement without any break in employment from the Company. Employees also must be participants in the Company's medical plan prior to their retirement. The Company funds the cost of postretirement health care as benefits are paid. The Company elected to recognize the transition obligation on a delayed basis over twenty years. In addition, the Company assumed post-retirement medical life insurance benefits for certain Alliance employees, retirees and their spouses, if applicable, in the Alliance acquisition. These postretirement benefits are referred to herein as "Other Benefits." The components of expense for Pension Benefits and Other Benefits are set forth below (in thousands):

	Pension Benefits		Other Benefits	
	Three months ended June 30,		Three months ended June 30,	
Components of net periodic benefit cost:	2013	2012	2013	2012
Service cost	$604	$757	$6	$5
Interest cost	830	774	75	40
Expected return on plan assets	(1,929)	(1,675)	-	-
Net amortization	711	859	(1)	(3)
Total cost (benefit)	$216	$715	$80	$42

	Pension Benefits	Other Benefits
	Six months ended June 30,	Six months ended June

			30,	
Components of net periodic benefit cost:	2013	2012	2013	2012
Service cost	$1,209	$1,513	$12	$ 10
Interest cost	1,659	1,548	150	79
Expected return on plan assets	(3,858)	(3,350)	-	-
Net amortization	1,314	1,718	222	(5)
Total cost (benefit)	$324	$1,429	$384	$ 84

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The Company is not required to make contributions to the plans in 2013, and did not do so during the six months ended June 30, 2013.

Market conditions can result in an unusually high degree of volatility and increase the risks and short term liquidity associated with certain investments held by the Company's defined benefit pension plan ("the Plan") which could impact the value of these investments.

Note 8. Trust Preferred Debentures

The Company sponsors five business trusts, CNBF Capital Trust I, NBT Statutory Trust I, NBT Statutory Trust II, Alliance Financial Capital Trust I and Alliance Financial Capital Trust II. The trusts were formed for the purpose of issuing company-obligated mandatorily redeemable preferred securities to third-party investors and investing in the proceeds from the sale of such preferred securities solely in junior subordinated debt securities of the Company. The debentures held by each trust are the sole assets of that trust. These five statutory business trusts are collectively referred herein to as "the Trusts." The Company guarantees, on a limited basis, payments of distributions on the trust preferred securities and payments on redemption of the trust preferred securities. The Trusts are variable interest entities ("VIEs") for which the Company is not the primary beneficiary, as defined by U.S. GAAP. In accordance with U.S. GAAP, the accounts of the Trusts are not included in the Company's consolidated financial statements.

As of June 30, 2013, the Trusts had the following issues of trust preferred debentures, all held by the Trusts, outstanding (dollars in thousands):

Description	Issuance Date	Trust Preferred Securities Outstanding	Interest Rate	Trust Preferred Debt Owed To Trust	Final Maturity Date
CNBF Capital Trust I	August-99	$ 18,000	3-month LIBOR plus 2.75%	$ 18,720	August-29
NBT Statutory Trust I	November-05	5,000	3-month LIBOR plus 1.40%	5,155	December-35
NBT Statutory Trust II	February-06	50,000	3-month LIBOR plus 1.40%	51,547	March-36
Alliance Financial Capital Trust I	December-03	10,000	3-month LIBOR plus 2.85%	10,310	January-34
Alliance Financial Capital Trust II	September-06	15,000	3-month LIBOR plus 1.65%	15,464	September-36

The Company owns all of the common stock of the Trusts, which have issued trust preferred securities in conjunction with the Company issuing trust preferred debentures to the Trusts. The terms of the trust preferred debentures are substantially the same as the terms of the trust preferred securities.

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Note 9. Fair Value Measurements and Fair Value of Financial Instruments

U.S. GAAP states that fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. Fair value measurements are not adjusted for transaction costs. A fair value hierarchy exists within U.S. GAAP that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements). The three levels of the fair value hierarchy are described below:

Level 1 - Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;

Level 2 - Quoted prices for similar assets or liabilities in active markets, quoted prices in markets that are not active, or inputs that are observable, either directly or indirectly, for substantially the full term of the asset or liability;

Level 3 - Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (i.e., supported by little or no market activity).

A financial instrument's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement.

The types of instruments valued based on quoted market prices in active markets include most U.S. government and agency securities, many other sovereign government obligations, liquid mortgage products, active listed equities and most money market securities. Such instruments are generally classified within level 1 or level 2 of the fair value hierarchy. The Company does not adjust the quoted price for such instruments.

The types of instruments valued based on quoted prices in markets that are not active, broker or dealer quotations, or alternative pricing sources with reasonable levels of price transparency include most investment-grade and high-yield corporate bonds, less liquid mortgage products, less liquid agency securities, less liquid listed equities, state, municipal and provincial obligations, and certain physical commodities. Such instruments are generally classified within level 2 of the fair value hierarchy.

Level 3 is for positions that are not traded in active markets or are subject to transfer restrictions, valuations are adjusted to reflect illiquidity and/or non-transferability, and such adjustments are generally based on available market evidence. In the absence of such evidence, management's best estimate will be used. Management's best estimate consists of both internal and external support on certain Level 3 investments. Subsequent to inception, management only changes level 3 inputs and assumptions when corroborated by evidence such as transactions in similar instruments, completed or pending third-party transactions in the underlying investment or comparable entities, subsequent rounds of financing, recapitalizations and other transactions across the capital structure, offerings in the equity or debt markets, and changes in financial ratios or cash flows.

For the six month period ending June 30, 2013, the Company has made no transfers of assets between Level 1 and Level 2, and has had no Level 3 activity.

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The following tables set forth the Company’s financial assets and liabilities measured on a recurring basis that were accounted for at fair value. Assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement (in thousands):

June 30, 2013:

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance as of June 30, 2013
Assets:				
Securities Available for Sale:				
U.S. Treasury	$53,949	$-	$ -	$53,949
Federal Agency	-	279,458	-	279,458
State & municipal	-	126,674	-	126,674
Mortgage-backed	-	291,594	-	291,594
Collateralized mortgage obligations	-	622,768	-	622,768
Other securities	10,909	5,051	-	15,960
Total Securities Available for Sale	$64,858	$1,325,545	$ -	$1,390,403
Trading Securities	5,092	-	-	5,092
Interest Rate Swaps	-	68	-	68
Total	$69,950	$1,325,613	$ -	$1,395,563
Liabilities:				
Interest Rate Swaps	$-	$68	$ -	$68
Total	$-	$68	$ -	$68

December 31, 2012:

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance as of December 31, 2012
Assets:				
Securities Available for Sale:				
U.S. Treasury	$64,425	$-	$ -	$64,425
Federal Agency	-	282,814	-	282,814
State & municipal	-	86,802	-	86,802
Mortgage-backed	-	250,281	-	250,281
Collateralized mortgage obligations	-	449,723	-	449,723

Other securities	11,866	2,088	-	13,954
Total Securities Available for Sale	$76,291	$1,071,708	$ -	$1,147,999
Trading Securities	3,918	-	-	3,918
Interest Rate Swaps	-	1,490	-	1,490
Total	$80,209	$1,073,198	$ -	$1,153,407
Liabilities:				
Interest Rate Swaps	$-	$1,490	$ -	$1,490
Total	$-	$1,490	$ -	$1,490

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Certain common equity securities are reported at fair value utilizing Level 1 inputs (exchange quoted prices). The majority of the other investment securities are reported at fair value utilizing Level 2 inputs. The prices for these instruments are obtained through an independent pricing service or dealer market participants with whom the Company has historically transacted both purchases and sales of investment securities. Prices obtained from these sources include prices derived from market quotations and matrix pricing. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond's terms and conditions, among other things. Management reviews the methodologies used in pricing the securities by its third party providers.

U.S. GAAP requires disclosure of assets and liabilities measured and recorded at fair value on a nonrecurring basis such as goodwill, loans held for sale, other real estate owned, collateral-dependent impaired loans, mortgage servicing rights, and held-to-maturity securities. The only nonrecurring fair value measurement recorded during the six month period ended June 30, 2013 and December 31, 2012 was related to impaired loans. The Company had collateral dependent impaired loans with a carrying value of approximately $7.3 million which had specific reserves included in the allowance for loan losses of $2.0 million at June 30, 2013. The Company had collateral dependent impaired loans with a carrying value of approximately $8.4 million which had specific reserves included in the allowance for loan losses of $2.8 million at December 31, 2012. The Company uses the fair value of underlying collateral, less costs to sell, to estimate the specific reserves for collateral dependent impaired loans. The appraisals may be adjusted by management for qualitative factors such as economic conditions and estimated liquidation expenses ranging from 10% to 35%. Based on the valuation techniques used, the fair value measurements for collateral dependent impaired loans are classified as Level 3.

The following table sets forth information with regard to estimated fair values of financial instruments at June 30, 2013 and December 31, 2012. This table excludes financial instruments for which the carrying amount approximates fair value. Financial instruments for which the fair value approximates carrying value include cash and cash equivalents, securities available for sale, trading securities, accrued interest receivable, non-maturity deposits, short-term borrowings, accrued interest payable, and interest rate swaps.

		June 30, 2013		December 31, 2012	
(In thousands)	Fair Value Hierarchy	Carrying amount	Estimated fair value	Carrying amount	Estimated fair value
Financial assets					
Securities held to maturity	2	$122,302	$121,069	$60,563	$61,535
Net loans	3	5,219,526	5,287,651	4,208,282	4,313,244
Financial liabilities					
Time deposits	2	$1,105,038	$1,112,212	$983,261	$994,376
Long-term debt	2	309,111	336,980	367,492	407,404
Trust preferred debentures	2	101,196	100,460	75,422	74,147

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular financial instrument. Because no market exists for a significant portion of the Company's financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

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Fair value estimates are based on existing on and off balance sheet financial instruments without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. For example, the Company has a substantial trust and investment management operation that contributes net fee income annually. The trust and investment management operation is not considered a financial instrument, and its value has not been incorporated into the fair value estimates. Other significant assets and liabilities include the benefits resulting from the low-cost funding of deposit liabilities as compared to the cost of borrowing funds in the market, and premises and equipment. In addition, the tax ramifications related to the realization of the unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in the estimate of fair value.

Securities Held to Maturity

The fair value of the Company's investment securities held to maturity is primarily measured using information from a third party pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond's terms and conditions, among other things.

Net Loans

The fair value of the Company's loans was estimated by discounting the expected future cash flows using the current interest rates at which similar loans would be made for the same remaining maturities. Loans were first segregated by type, and then further segmented into fixed and variable rate and loan quality categories. Expected future cash flows were projected based on contractual cash flows, adjusted for estimated prepayments.

Time Deposits

The fair value of time deposits was estimated using a discounted cash flow approach that applies prevailing market interest rates for similar maturity instruments. The fair values of the Company's time deposit liabilities do not take into consideration the value of the Company's long-term relationships with depositors, which may have significant value.

Long-Term Debt

The fair value of long-term debt was estimated using a discounted cash flow approach that applies prevailing market interest rates for similar maturity instruments.

Trust Preferred Debentures

The fair value of trust preferred debentures has been estimated using a discounted cash flow analysis.

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Note 10. Securities

The amortized cost, estimated fair value, and unrealized gains and losses of securities available for sale are as follows:

(In thousands)	Amortized cost	Unrealized gains	Unrealized losses	Estimated fair value
June 30, 2013				
U.S. Treasury	$53,440	$ 509	$ -	$53,949
Federal Agency	286,049	192	6,783	279,458
State & municipal	125,792	2,375	1,493	126,674
Mortgage-backed:				
Government-sponsored enterprises	260,130	6,149	1,487	264,792
U.S. government securities	25,608	1,269	75	26,802
Collateralized mortgage obligations:				
Government-sponsored enterprises	573,487	2,677	6,747	569,417
U.S. government securities	52,421	970	40	53,351
Other securities	13,409	2,720	169	15,960
Total securities available for sale	$1,390,336	$ 16,861	$ 16,794	$1,390,403
December 31, 2012				
U.S. Treasury	$63,668	$ 757	$ -	$64,425
Federal Agency	281,398	1,507	91	282,814
State & municipal	82,675	4,127	-	86,802
Mortgage-backed:				
Government-sponsored enterprises	221,110	11,175	-	232,285
U.S. government securities	16,351	1,645	-	17,996
Collateralized mortgage obligations:				
Government-sponsored enterprises	399,147	4,418	-	403,565
U.S. government securities	44,825	1,333	-	46,158
Other securities	11,210	2,832	88	13,954
Total securities available for sale	$1,120,384	$ 27,794	$ 179	$1,147,999

Other securities primarily represent marketable equity securities.

Proceeds from the sales of securities available for sale were $26.2 million during the six months ended June 30, 2013, and gains on the sales were $1.1 million. Proceeds from the sales of securities available for sale were $1.8 million during the six months ended June 30, 2012, and gains on the sales were $0.6 million.

Securities with amortized costs totaling $1.5 billion at June 30, 2013 and $1.2 billion at December 31, 2012, were pledged to secure public deposits and for other purposes required or permitted by law. Additionally, at June 30, 2013 and December 31, 2012, securities available for sale with an amortized cost of $224.6 million and $209.0 million, respectively, were pledged as collateral for securities sold under repurchase agreements.

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The amortized cost, estimated fair value, and unrealized gains and losses of securities held to maturity are as follows:

(In thousands)	Amortized cost	Unrealized gains	Unrealized losses	Estimated fair value
June 30, 2013				
Mortgage-backed	$ 1,070	$ 151	$ -	$ 1,221
Collateralized mortgage oblications	64,022	-	1,964	62,058
State & municipal	57,210	580	-	57,790
Total securities held to maturity	$ 122,302	$ 731	$ 1,964	$ 121,069
December 31, 2012				
Mortgage-backed	$ 1,168	$ 184	$ -	$ 1,352
Collateralized mortgage oblications	-	-	-	0
State & municipal	59,395	788	-	60,183
Total securities held to maturity	$ 60,563	$ 972	$ -	$ 61,535

The following table sets forth information with regard to investment securities with unrealized losses at June 30, 2013 and December 31, 2012:

	Less than 12 months			12 months or longer			Total		
Security Type:	Fair Value	Unrealized losses	Number of Positions	Fair Value	Unrealized losses	Number of Positions	Fair Value	Unrealized losses	Number of Positions
June 30, 2013									
Investment securities available for sale:									
U.S. Treasury	$ -	$ -	-	$ -	$ -	-	$ -	$ -	-
Federal agency	286,049	(6,783)	20	-	-	-	286,049	(6,783)	20
State & municipal	125,792	(1,493)	193	-	-	-	125,792	(1,493)	193
Mortgage-backed	285,687	(1,562)	94	-	-	-	285,687	(1,562)	94
Collateralized mortgage obligations	625,908	(6,787)	28	-	-	-	625,908	(6,787)	28
Other securities	5,560	(132)	2	211	(37)	1	5,771	(169)	3
Total securities with unrealized losses	$ 1,328,996	$ (16,757)	337	$ 211	$ (37)	1	$ 1,329,207	$ (16,794)	338
June 30, 2013									
Investment securities held to maturity:									
Collateralized mortgage obligations	64,022	(1,964)	5	-	-	-	64,022	(1,964)	5
Total securities with unrealized losses	$ 64,022	$ (1,964)	5	$ -	$ -	-	$ 64,022	$ (1,964)	5

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	Less than 12 months			12 months or longer			Total		
	Fair Value	Unrealized losses	Number of Positions	Fair Value	Unrealized losses	Number of Positions	Fair Value	Unrealized losses	Number of Positions
December 31, 2012									
Investment securities available for sale:									
U.S. Treasury	$-	$ -	-	$-	$ -	-	$-	$ -	-
Federal agency	39,906	(91)	4	-	-	-	39,906	(91)	4
State & municipal	-	-	-	-	-	-	-	-	-
Mortgage-backed	-	-	-	-	-	-	-	-	-
Collateralized mortgage obligations	23	-	2	-	-	-	23	-	2
Other securities	468	(6)	1	167	(82)	1	635	(88)	2
Total securities with unrealized losses	$40,397	$ (97)	7	$167	$ (82)	1	$40,564	$ (179)	8

Declines in the fair value of held-to-maturity and available-for-sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses or in other comprehensive income, depending on whether the Company intends to sell the security or more likely than not will be required to sell the security before recovery of its amortized cost basis less any current-period credit loss. If the Company intends to sell the security or more likely than not will be required to sell the security before recovery of its amortized cost basis less any current-period credit loss, the other-than-temporary impairment shall be recognized in earnings equal to the entire difference between the investment's amortized cost basis and its fair value at the balance sheet date. If the Company does not intend to sell the security and it is not more likely than not that the entity will be required to sell the security before recovery of its amortized cost basis less any current-period credit loss, the other-than-temporary impairment shall be separated into (a) the amount representing the credit loss and (b) the amount related to all other factors. The amount of the total other-than-temporary impairment related to the credit loss shall be recognized in earnings. The amount of the total other-than-temporary impairment related to other factors shall be recognized in other comprehensive income, net of applicable taxes.

In estimating other-than-temporary impairment losses, management considers, among other things, (i) the length of time and the extent to which the fair value has been less than cost, (ii) the financial condition and near-term prospects of the issuer, and (iii) the historical and implied volatility of the fair value of the security.

Management has the intent to hold the securities classified as held to maturity until they mature, at which time it is believed the Company will receive full value for the securities. Furthermore, as of June 30, 2013, management also had the intent to hold, and will not be required to sell, the securities classified as available for sale for a period of time sufficient for a recovery of cost, which may be until maturity. The unrealized losses are due to increases in market interest rates over the yields available at the time the underlying securities were purchased. When necessary, the Company has performed a discounted cash flow analysis to determine whether or not it will receive the contractual principal and interest on certain securities. The fair value is expected to recover as the bonds approach their maturity date or repricing date or if market yields for such investments decline. As of June 30, 2013, management believes the impairments detailed in the table above are temporary and no other-than-temporary impairment losses have been realized in the Company's consolidated statements of income.

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The following tables set forth information with regard to contractual maturities of debt securities at June 30, 2013:

(In thousands)	Amortized cost	Estimated fair value
Debt securities classified as available for sale		
Within one year	$26,789	$26,915
From one to five years	194,833	195,558
From five to ten years	348,099	345,525
After ten years	807,206	806,445
	$1,376,927	$1,374,443
Debt securities classified as held to maturity		
Within one year	$25,315	$25,415
From one to five years	24,620	25,095
From five to ten years	5,651	5,656
After ten years	66,716	64,903
	$122,302	$121,069

Maturities of mortgage-backed, collateralized mortgage obligations and asset-backed securities are stated based on their estimated average lives. Actual maturities may differ from estimated average lives or contractual maturities because, in certain cases, borrowers have the right to call or prepay obligations with or without call or prepayment penalties.

Except for U.S. Government securities, there were no holdings, when taken in the aggregate, of any single issuer that exceeded 10% of consolidated stockholders' equity at June 30, 2013.

Note 11. Reclassification Adjustments Out of Other Comprehensive (Loss) Income

The following table summarizes the reclassification adjustments out of accumulated other comprehensive loss (in thousands):

Detail About Accumulated Other Comprehensive (Loss) Income Components	Amount reclassified from accumulated other comprehensive income (loss) Three months ended June 30, 2013	June 30, 2012	Affected line item in the consolidated statement of comprehensive income
Available for sale securities:			
Unrealized losses (gains) on available for sale securities	$ 61	$ (97)	Net securities gains
Tax (benefit) expense	(24)	39	Income tax expense
Net of tax	$ 37	$ (58)	
Pension and other benefits:			
Amortization of net gains	$ 765	$ 911	Salaries and employee benefits

Amortization of prior service costs	(55)	(55)	Salaries and employee benefits
Tax benefit	284	345	Income tax expense
Net of tax	$ 426	$ 511	
Total reclassifications during the period, net of tax	$ 463	$ 453	

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Detail About Accumulated Other Comprehensive (Loss) Income Components	Amount reclassified from accumulated other comprehensive income (loss) Six months ended June 30, 2013	June 30, 2012	Affected line item in the consolidated statement of comprehensive income
Available for sale securities:			
Unrealized gains on available for sale securities	$(1,084)	$(552)	Net securities gains
Tax expense	434	221	Income tax expense
Net of tax	$(650)	$(331)	
Pension and other benefits:			
Amortization of net gains	$1,647	$1,824	Salaries and employee benefits
Amortization of prior service costs	(111)	(111)	Salaries and employee benefits
Tax benefit	614	686	Income tax expense
Net of tax	$922	$1,027	
Total reclassifications during the period, net of tax	$272	$696	

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NBT BANCORP INC. AND SUBSIDIARIES

Item 2 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The purpose of this discussion and analysis is to provide a concise description of the financial condition and results of operations of NBT Bancorp Inc. and its wholly owned consolidated subsidiaries, NBT Bank, N.A. (the “Bank”), NBT Financial Services, Inc. (“NBT Financial”), and NBT Holdings, Inc. (“NBT Holdings”) (collectively referred to herein as the “Company”). This discussion will focus on results of operations, financial condition, capital resources and asset/liability management. Reference should be made to the Company's consolidated financial statements and footnotes thereto included in this Form 10 Q as well as to the Company's Annual Report on Form 10 K for the year ended December 31, 2012 for an understanding of the following discussion and analysis. Operating results for the three and six month periods ending June 30, 2013 are not necessarily indicative of the results of the full year ending December 31, 2013 or any future period.

Forward-looking Statements

Certain statements in this filing and future filings by the Company with the Securities and Exchange Commission, in the Company’s press releases or other public or shareholder communications, contain forward-looking statements, as defined in the Private Securities Litigation Reform Act. These statements may be identified by the use of phrases such as “anticipate,” “believe,” “expect,” “forecasts,” “projects,” “could,” or other similar terms. There are a number of factors, ma of which are beyond the Company’s control, that could cause actual results to differ materially from those contemplated by the forward-looking statements. Factors that may cause actual results to differ materially from those contemplated by such forward-looking statements include, among others, the following: (1) competitive pressures among depository and other financial institutions may increase significantly; (2) revenues may be lower than expected; (3) changes in the interest rate environment may affect interest margins; (4) general economic conditions, either nationally or regionally, may be less favorable than expected, resulting in, among other things, a deterioration in credit quality and/or a reduced demand for credit; (5) legislative or regulatory changes, including changes in accounting standards or tax laws, may adversely affect the businesses in which the Company is engaged; (6) competitors may have greater financial resources and develop products that enable such competitors to compete more successfully than the Company; (7) adverse changes may occur in the securities markets or with respect to inflation; (8) acts of war or terrorism; (9) the costs and effects of litigation and of unexpected or adverse outcomes in such litigation; (10) internal control failures; (11) the successful completion and integration of acquisitions; and (12) the Company’s success in managing the risks involved in the foregoing.

The Company cautions readers not to place undue reliance on any forward-looking statements, which speak only as of the date made, and advises readers that various factors, including those described above and other factors discussed in the Company’s annual and quarterly reports previously filed with the Securities and Exchange Commission, could affect the Company’s financial performance and could cause the Company’s actual results or circumstances for future periods to differ materially from those anticipated or projected.

Unless required by law, the Company does not undertake, and specifically disclaims any obligations to publicly release any revisions to any forward-looking statements to reflect the occurrence of anticipated or unanticipated events or circumstances after the date of such statements.

Non-GAAP Measures

This Quarterly Report on Form 10-Q contains financial information determined by methods other than in accordance with accounting principles generally accepted in the United States of America (GAAP). These measures adjust GAAP measures to exclude the effects of sales of securities and certain non-recurring and merger-related expenses. Where non-GAAP disclosures are used in this Quarterly Report on Form 10-Q, the comparable GAAP measure, as well as a reconciliation to the comparable GAAP measure, is provided in the accompanying tables. Management believes that these non-GAAP measures provide useful information that is important to an understanding of the operating results of the Company’s core business due to the non-recurring nature of the excluded items. Non-GAAP measures should not be considered substitutes for financial measures determined in accordance with GAAP and investors should consider the Company’s performance and financial condition as reported under GAAP and all other relevant information when assessing the performance or financial condition of the Company.

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Recent Legislation

The following section should be read in conjunction with the Supervision and Regulation section of NBT's 2012 Form 10-K.

On July 2, 2013, the Federal Reserve Board issued final rules, and on July 9, 2013, the Office of the Comptroller of the Currency issued interim final rules that revise the existing regulatory capital requirements to incorporate certain revisions to the Basel capital framework, including Basel III, and to implement certain provisions of the Dodd Frank Wall Street Reform and Consumer Protection Act ("Dodd Frank Act") . The final and interim final rules seek to strengthen the components of regulatory capital, increase risk-based capital requirements, and make selected changes to the calculation of risk-weighted assets. The final and interim final rules, among other things:

- revise minimum capital requirements and adjust prompt corrective action thresholds;
- revise the components of regulatory capital, add a new minimum common equity Tier 1 capital ratio of 4.5% of risk-weighted assets, increase the minimum Tier 1 capital ratio requirement from 4% to 6%;
- retain the existing risk-based capital treatment for 1-4 family residential mortgage exposures;
- permit most banking organizations, including the Company, to retain, through a one-time permanent election, the existing capital treatment for accumulated other comprehensive income;
- implement a new capital conservation buffer of common equity Tier 1 capital equal to 2.5% of risk-weighted assets, which will be in addition to the 4.5% common equity Tier 1 capital ratio and be phased in over a three year period beginning January 1, 2016 which buffer is generally required to make capital distributions and pay executive bonuses;
- increase capital requirements for past-due loans, high volatility commercial real estate exposures, and certain short-term loan commitments;
- require the deduction of mortgage servicing assets and deferred tax assets that exceed 10% of common equity Tier 1 capital in each category and 15% of common equity Tier 1 capital in the aggregate; and
- remove references to credit ratings consistent with the Dodd-Frank Act and establish due diligence requirements for securitization exposures.

Under the final and interim rules, compliance is required beginning January 1, 2015, for most banking organizations including the Company, subject to a transition period for several aspects of the rule, including the new minimum capital ratio requirements, the capital conservation buffer, and the regulatory capital adjustments and deductions. We are still in the process of assessing the impacts of these complex final and interim final rules, however, we believe we will continue to exceed all estimated well-capitalized regulatory requirements on a fully phased-in basis.

In May 2013, the Securities and Exchange Commission and the Commodity Futures Trading Commission (together, the "Commissions") jointly issued final rules and guidelines to require certain regulated entities to establish programs to address risks of identity theft. The rules and guidelines implement provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act. These provisions amend Section 615(e) of the Fair Credit Reporting Act and directed the Commissions to adopt rules requiring entities that are subject to the Commissions' jurisdiction to address identity theft in two ways. First, the rules require financial institutions and creditors to develop and implement a written identity theft prevention program that is designed to detect, prevent, and mitigate identity theft in connection with certain existing accounts or the opening of new accounts. The rules include guidelines to assist entities in the formulation and maintenance of programs that would satisfy the requirements of the rules. Second, the rules establish special requirements for any credit and debit card issuers that are subject to the Commissions' jurisdiction, to assess the validity of notifications of changes of address under certain circumstances.

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Critical Accounting Policies

The Company has identified policies as being critical because they require management to make particularly difficult, subjective and/or complex judgments about matters that are inherently uncertain and because of the likelihood that materially different amounts would be reported under different conditions or using different assumptions. These policies relate to the allowance for loan losses, pension accounting, other-than-temporary impairment, provision for income taxes and intangible assets.

Management of the Company considers the accounting policy relating to the allowance for loan losses to be a critical accounting policy given the uncertainty in evaluating the level of the allowance required to cover credit losses inherent in the loan portfolio and the material effect that such judgments can have on the results of operations. While management's current evaluation of the allowance for loan losses indicates that the allowance is adequate, under adversely different conditions or assumptions, the allowance may need to be increased. For example, if historical loan loss experience significantly worsened or if current economic conditions significantly deteriorated, additional provision for loan losses would be required to increase the allowance. In addition, the assumptions and estimates used in the internal reviews of the Company's nonperforming loans and potential problem loans have a significant impact on the overall analysis of the adequacy of the allowance for loan losses. While management has concluded that the current evaluation of collateral values is reasonable under the circumstances, if collateral values were significantly lower, the Company's allowance for loan loss policy would also require additional provision for loan losses.

Management is required to make various assumptions in valuing the Company's pension assets and liabilities. These assumptions include the expected rate of return on plan assets, the discount rate, and the rate of increase in future compensation levels. Changes to these assumptions could impact earnings in future periods. The Company takes into account the plan asset mix, funding obligations, and expert opinions in determining the various rates used to estimate pension expense. The Company also considers the Citigroup Pension Liability Index, market interest rates and discounted cash flows in setting the appropriate discount rate. In addition, the Company reviews expected inflationary and merit increases to compensation in determining the rate of increase in future compensation levels.

Management of the Company considers the accounting policy relating to other-than-temporary impairment to be a critical accounting policy. Management systematically evaluates certain assets for other-than-temporary declines in fair value, primarily investment securities. Management considers historical values and current market conditions as a part of the assessment. The amount of the total other-than-temporary impairment related to the credit loss is recognized in earnings and the amount of the total other-than-temporary impairment related to other factors is generally recognized in other comprehensive income, net of applicable taxes.

The Company is subject to examinations from various taxing authorities. Such examinations may result in challenges to the tax return treatment applied by the Company to specific transactions. Management believes that the assumptions and judgments used to record tax-related assets or liabilities have been appropriate. Should tax laws change or the taxing authorities determine that management's assumptions were inappropriate, an adjustment may be required which could have a material effect on the Company's results of operations.

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Another critical accounting policy is the policy for acquired loans. Acquired loans are initially recorded at their acquisition date fair values. The carryover of allowance for loan losses is prohibited as any credit losses in the loans are included in the determination of the fair value of the loans at the acquisition date. Fair values for acquired loans are based on a discounted cash flow methodology that involves assumptions and judgments as to credit risk, prepayment risk, liquidity risk, default rates, loss severity, payment speeds, collateral values and discount rate. Subsequent to the acquisition of acquired impaired loans, applicable accounting guidance requires the continued estimation of expected cash flows to be received. This estimation involves the use of key assumptions and estimates, similar to those used in the initial estimate of fair value. Changes in expected cash flows could result in the recognition of impairment through provision for credit losses. Subsequent to the purchase date, the methods utilized to estimate the required allowance for loan losses for the non-impaired acquired loans is similar to originated loans.

As a result of acquisitions, the Company has acquired goodwill and identifiable intangible assets. Goodwill represents the cost of acquired companies in excess of the fair value of net assets at the acquisition date. Goodwill is evaluated at least annually or when business conditions suggest that an impairment may have occurred. Goodwill will be reduced to its carrying value through a charge to earnings if impairment exists. Core deposits and other identifiable intangible assets are amortized to expense over their estimated useful lives. The determination of whether or not impairment exists is based upon discounted cash flow modeling techniques that require management to make estimates regarding the amount and timing of expected future cash flows. It also requires them to select a discount rate that reflects the current return requirements of the market in relation to present risk-free interest rates, required equity market premiums and Company-specific risk indicators, all of which are susceptible to change based on changes in economic conditions and other factors. Future events or changes in the estimates used to determine the carrying value of goodwill and identifiable intangible assets could have a material impact on the Company's results of operations.

The Company's policies on the allowance for loan losses, pension accounting, acquired loans, provision for income taxes and intangible assets are disclosed in Note 1 to the consolidated financial statements presented in our 2012 Annual Report on Form 10-K. All accounting policies are important, and as such, the Company encourages the reader to review each of the policies included in Note 1 to obtain a better understanding of how the Company's financial performance is reported.

Overview

Significant factors management reviews to evaluate the Company's operating results and financial condition include, but are not limited to: net income and earnings per share, return on assets and equity, tangible common equity, net interest margin, noninterest income, operating expenses, asset quality indicators, loan and deposit growth, capital management, liquidity and interest rate sensitivity, enhancements to customer products and services, technology advancements, market share and peer comparisons. The following information should be considered in connection with the Company's results for the first six months of 2013:

- Core net income was $32.1 million for the six months ended June 30, 2013, up 19.6% from $26.9 million for the same period in 2012. Core diluted earnings per share for the six months ended June 30, 2013 were $0.79, down 1.3% from $0.80 in the same period in 2012. Core annualized return on average assets and return on average equity were 0.93% and 8.93%, respectively, for the six months ended June 30, 2013, compared with 0.94% and 9.86%, respectively, for the six months ended June 30, 2012.

- Reported results for the six months ending June 30, 2013 include the impact of the acquisition of Alliance Financial Corporation ("Alliance") since March 8, 2013, including $12.0 million in merger related expenses for the six months ended June 30, 2013.

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- Net interest margin (on a fully taxable equivalent basis (“FTE”)) was 3.68% for the six months ended June 30, 2013 as compared to 3.86% for the same period in 2012.

- Past due loans as a percentage of total loans were 0.71% at June 30, 2013 and December 31, 2012.

- Net charge-offs, annualized, were 0.42% of average loans for the first six months of 2013, compared to 0.55% for the year ended December 31, 2012.

The following table depicts several annualized measurements of performance using core and U.S. GAAP net income that management reviews in analyzing the Company’s performance. Returns on average assets and average equity measure how effectively an entity utilizes its total resources and capital, respectively.

(Dollars in thousands)	For the three months ended June 30,		For the six months ended June 30,	
	2013	2012	2013	2012
Reconciliation of Non-GAAP Financial Measures:				
Reported net income (GAAP)	$16,916	$13,257	$24,565	$26,907
Adj: Loss / (Gain) on sale of securities, net	61	(97)	(1,084)	(552)
Adj: Other adjustments (1)	-	(115)	-	(865)
Plus: Merger related expenses	1,269	826	11,950	1,337
Total Adjustments	1,330	614	10,866	(80)
Income tax effect on adjustments	(406)	(187)	(3,314)	24
Core net income	$17,840	$13,684	$32,117	$26,851
Weighted Average Diluted Shares	44,316,531	33,492,659	40,574,934	33,452,970
Core Diluted Earnings Per Share	$0.40	$0.41	$0.79	$0.80
Performance measures:				
Core Return on Average Assets (2)	0.95%	0.95%	0.93%	0.94%
Core Return on Average Equity (2)	8.88%	9.97%	8.93%	9.86%
Core Return on Average Tangible Common Equity (2)(3)	14.57%	14.35%	14.11%	14.18%

(1) Other adjustments were primarily a flood insurance recovery for the 2012 quarter, and for the first half of 2012 a prepayment penalty fee and a flood insurance recovery
(2) Annualized
(3) Excludes amortization of intangible assets (net of tax) from net income and average tangible common equity is calculated as follows:

	For the three months ended June 30,		For the six months ended June 30,	
	2013	2012	2013	2012
Average stockholders equity	$806,200	$551,865	$724,898	$547,246
Less: average goodwill and other intangibles	292,775	154,058	247,031	152,268
Average tangible common equity	$513,425	$397,807	$477,867	$394,978

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Net Interest Income

Net interest income is the difference between interest income on earning assets, primarily loans and securities, and interest expense on interest bearing liabilities, primarily deposits and borrowings. Net interest income is affected by the interest rate spread, the difference between the yield on earning assets and cost of interest bearing liabilities, as well as the volumes of such assets and liabilities. Net interest income is one of the key determining factors in a financial institution's performance as it is the principal source of earnings.

Fully Taxable Equivalent ("FTE") net interest income increased $11.9 million during the three months ended June 30, 2013, compared to the same period of 2012. The Company's FTE net interest margin was 3.69% for the three months ended June 30, 2013, down from 3.82% for the three months ended June 30, 2012. Average interest earning assets were $6.8 billion for the second quarter of 2013, an increase of 27.4% compared to the same period in 2012. The growth in earning assets was due to the acquisition of Alliance in March 2013 combined with organic loan growth. The increase in average earning assets for the three months ended June 30, 2013 as compared to the same period of 2012 offset the decline in the yield on earning assets, resulting in the increase in net interest income over the same period last year.

For the three months ended June 30, 2013, total FTE interest income increased $10.9 million, or 18.3%, from the same period in 2012 as a result of the increase in average earning assets, attributed to aforementioned acquisition activity and organic loan growth in the previous year and current quarter. The average balance of loans for the three months ended June 30, 2013 was $5.2 billion, up approximately $1.3 billion, or 33.1%, from the three months ended June 30, 2012. The average balance of securities available for sale for the three months ended June 30, 2013 was $1.4 billion, down 18% from the three months ended June 30, 2012. The growth in average earning assets from the second quarter of 2012 was partially offset by a 33 basis point decrease in the yield earned on earning assets. The yield on securities available for sale decreased 56 basis points to 1.97% for the second quarter of 2013 from 2.53% for same period in 2012. In addition, the yield on loans decreased 42 basis points to 4.76% for the three months ended June 30, 2013 from 5.18% for the three months ended June 30, 2012. The decreases in the yield on securities and loans were due primarily to the reinvestment of cash flows from loan principal payments and maturing of securities in the current low interest rate environment. At the end of the second quarter, long-term rates increased providing more favorable yields on the reinvestment of cash flows.

The reduction in yields on earning assets was partially offset by a reduction in rates paid on interest bearing liabilities. The cost of interest bearing liabilities for the three months ended June 30, 2013 was down 26 bps to 0.62%. Rates paid on interest bearing deposits and borrowings decreased by 17 and 49 basis points, respectively, from the same period in 2012. The decrease in interest paid on interest bearing deposits primarily resulted from the 42 basis point decrease in the cost of time deposits. The cost of long term debt also decreased as maturing higher cost borrowings were replaced with lower rate short term borrowings during the period. In future periods, additional rate reductions on deposits could be more difficult as deposit rates are at or near their floors.

Average interest bearing liabilities increased approximately $1.1 billion, or 25.7%, for the three months ended June 30, 2013 as compared to the same period in 2012, which partially offset the decrease in total interest expense attributed to the decrease in the rates on interest bearing liabilities. The increase in average interest bearing liabilities is primarily due to the Alliance acquisition, partly offset by the pay down of long term borrowings in the first six months of 2013.

FTE net interest income was $115.7 million for the six months ended June 30, 2013, up 14.3% from the same period in 2012. This increase from the previous year was due primarily to the 20.1% increase in average earning assets for the six months ended June 30, 2013 over the prior year, partly offset by an 18 basis point decrease in the net interest margin for the same period. The acquisition of Hampshire First Bank in June 2012, the acquisition of Alliance in March 2013, and organic loan growth during the period contributed to the growth in average earning assets.

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The Company's FTE net interest margin was 3.68% for the six months ended June 30, 2013, down from 3.86% for the same period last year. Rate compression on earning assets continued to negatively impact net interest margin for the first six months of 2013 as evidenced by decreasing loan yields from 5.25% for the first six months of 2012 to 4.81% for the first six months of 2013. In addition, yields on available for sale securities declined 54 basis points in the first six months of 2013 as compared to the same period in 2012.

The reduction in yields on earning assets was partially offset by a reduction in rates paid on interest bearing liabilities in the first six months of 2013 as compared to the same period in 2012. The cost of interest bearing liabilities for the six months ended June 30, 2013 was down 22 bps to 0.68%. The reduction in the cost of interest bearing liabilities was primarily attributable to the decrease in the cost of deposits and long term borrowings.

Average interest bearing liabilities increased approximately $736.3 million, or 18.2%, for the six months ended June 30, 2013 as compared to the same period in 2012, which partially offset the decrease in total interest expense attributed to the decrease in the rates on interest bearing liabilities. The increase in average interest bearing liabilities is primarily due to the acquisition of Hampshire First Bank in June 2012, the Alliance acquisition in March 2013, partly offset by the pay down of long term debt.

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Average Balances and Net Interest Income

The following tables include the condensed consolidated average balance sheet, an analysis of interest income/expense and average yield/rate for each major category of earning assets and interest bearing liabilities on a taxable equivalent basis. Interest income for tax-exempt securities and loans has been adjusted to a taxable-equivalent basis using the statutory Federal income tax rate of 35%.

Three Months ended June 30,	2013			2012		
(dollars in thousands)	Average Balance	Interest	Yield/ Rates	Average Balance	Interest	Yield/ Rates
ASSETS						
Short-term interest bearing accounts	$41,313	$59	0.57 %	$102,192	$84	0.33 %
Securities available for sale (1)(2)	1,428,864	7,033	1.97 %	1,208,384	7,605	2.53 %
Securities held to maturity (1)	62,463	815	5.23 %	68,472	931	5.47 %
Investment in FRB and FHLB Banks	35,497	430	4.85 %	27,886	328	4.73 %
Loans (3)	5,243,534	62,268	4.76 %	3,938,592	50,741	5.18 %
Total interest earning assets	$6,811,671	$70,605	4.16 %	$5,345,526	$59,689	4.49 %
Other assets	705,869			465,058		
Total assets	$7,517,540			$5,810,584		
LIABILITIES AND STOCKHOLDERS' EQUITY						
Money market deposit accounts	$1,402,429	524	0.15 %	$1,115,812	$539	0.19 %
NOW deposit accounts	927,037	443	0.19 %	704,896	480	0.27 %
Savings deposits	983,413	209	0.09 %	676,794	127	0.08 %
Time deposits	1,136,511	3,120	1.10 %	973,051	3,688	1.52 %
Total interest bearing deposits	$4,449,390	$4,296	0.39 %	$3,470,553	$4,834	0.56 %
Short-term borrowings	229,906	67	0.12 %	171,545	48	0.11 %
Trust preferred debentures	101,196	560	2.22 %	75,422	434	2.31 %
Long-term debt	355,702	3,026	3.41 %	368,251	3,580	3.91 %
Total interest bearing liabilities	$5,136,194	$7,949	0.62 %	$4,085,771	$8,896	0.88 %
Demand deposits	1,496,486			1,111,804		
Other liabilities	78,660			61,144		
Stockholders' equity	806,200			551,865		
Total liabilities and stockholders' equity	$7,517,540			$5,810,584		
Net interest income (FTE)		62,656			50,793	
Interest rate spread			3.54 %			3.61 %
Net interest margin			3.69 %			3.82 %
Taxable equivalent adjustment		1,001			1,042	
Net interest income		$61,655			$49,751	

(1) Securities are shown at average amortized cost
(2) Excluding unrealized gains or losses
(3) For purposes of these computations, nonaccrual loans are included in the average loan balances outstanding

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Six Months ended June 30,

(dollars in thousands)	2013 Average Balance	2013 Interest	2013 Yield/ Rates	2012 Average Balance	2012 Interest	2012 Yield/ Rates
ASSETS						
Short-term interest bearing accounts	$58,118	$98	0.34 %	$91,159	$120	0.26 %
Securities available for sale (1)(2)	1,313,691	13,212	2.03 %	1,210,575	15,460	2.57 %
Securities held to maturity (1)	57,710	1,605	5.61 %	69,507	1,896	5.48 %
Investment in FRB and FHLB Banks	33,416	796	4.80 %	27,453	685	5.02 %
Loans (3)	4,869,896	116,171	4.81 %	3,874,027	101,184	5.25 %
Total interest earning assets	$6,332,831	$131,882	4.20 %	$5,272,721	$119,345	4.55 %
Other assets	630,532			462,300		
Total assets	$6,963,363			$5,735,021		
LIABILITIES AND STOCKHOLDERS' EQUITY						
Money market deposit accounts	$1,297,077	934	0.15 %	$1,102,579	$1,151	0.21 %
NOW deposit accounts	863,481	889	0.21 %	699,917	1,010	0.29 %
Savings deposits	877,574	354	0.08 %	659,381	242	0.07 %
Time deposits	1,076,445	6,269	1.17 %	964,701	7,574	1.58 %
Total interest bearing deposits	$4,114,577	$8,446	0.41 %	$3,426,578	$9,977	0.59 %
Short-term borrowings	199,513	109	0.11 %	167,176	89	0.11 %
Trust preferred debentures	91,798	988	2.17 %	75,422	883	2.35 %
Long-term debt	368,867	6,635	3.63 %	369,323	7,161	3.90 %
Total interest bearing liabilities	$4,774,755	$16,178	0.68 %	$4,038,499	$18,110	0.90 %
Demand deposits	1,390,700			1,087,180		
Other liabilities	73,010			62,096		
Stockholders' equity	724,898			547,246		
Total liabilities and stockholders' equity	$6,963,363			$5,735,021		
Net interest income (FTE)		115,704			101,235	
Interest rate spread			3.52 %			3.65 %
Net interest margin			3.68 %			3.86 %
Taxable equivalent adjustment		1,909			2,092	
Net interest income		$113,795			$99,143	

(1) Securities are shown at average amortized cost

(2) Excluding unrealized gains or losses

(3) For purposes of these computations, nonaccrual loans are included in the average loan balances outstanding

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The following table presents changes in interest income and interest expense attributable to changes in volume (change in average balance multiplied by prior year rate), changes in rate (change in rate multiplied by prior year volume), and the net change in net interest income. The net change attributable to the combined impact of volume and rate has been allocated to each in proportion to the absolute dollar amounts of change.

Three months ended June 30,

	Increase (Decrease) 2013 over 2012		
(in thousands)	Volume	Rate	Total
Short-term interest bearing accounts	$(233)	$208	$(25)
Securities available for sale	5,843	(6,415)	(572)
Securities held to maturity	(78)	(38)	(116)
Investment in FRB and FHLB Banks	93	9	102
Loans	35,768	(24,241)	11,527
Total interest income	41,393	(30,477)	10,916
Money market deposit accounts	517	(532)	(15)
NOW deposit accounts	575	(612)	(37)
Savings deposits	64	18	82
Time deposits	2,891	(3,459)	(568)
Short-term borrowings	17	2	19
Trust preferred debentures	240	(114)	126
Long-term debt	(117)	(437)	(554)
Total interest expense	4,187	(5,134)	(947)
Change in FTE net interest income	$37,206	$(25,343)	$11,863

Six months ended June 30,

	Increase (Decrease) 2013 over 2012		
(in thousands)	Volume	Rate	Total
Short-term interest bearing accounts	$(89)	$67	$(22)
Securities available for sale	3,122	(5,370)	(2,248)
Securities held to maturity	(408)	117	(291)
Investment in FRB and FHLB Banks	191	(80)	111
Loans	37,089	(22,102)	14,987
Total interest income	39,905	(27,368)	12,537
Money market deposit accounts	440	(657)	(217)
NOW deposit accounts	467	(588)	(121)
Savings deposits	86	26	112
Time deposits	2,023	(3,328)	(1,305)
Short-term borrowings	17	3	20
Trust preferred debentures	281	(176)	105
Long-term debt	(9)	(517)	(526)
Total interest expense	3,305	(5,237)	(1,932)
Change in FTE net interest income	$36,600	$(22,131)	$14,469

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Noninterest Income

Noninterest income is a significant source of revenue for the Company and an important factor in the Company's results of operations. The following table sets forth information by category of noninterest income for the periods indicated:

	Three months ended June 30,		Six months ended June 30,	
	2013	2012	2013	2012
(in thousands)				
Insurance and other financial services revenue	$5,755	$5,279	$12,648	$11,433
Service charges on deposit accounts	4,933	4,571	9,256	8,912
ATM and debit card fees	4,044	3,063	7,286	6,025
Retirement plan administration fees	2,957	2,411	5,639	4,744
Trust	4,699	2,312	7,612	4,441
Bank owned life insurance	886	618	1,735	1,589
Net securities (losses) gains	(61)	97	1,084	552
Other	2,324	2,331	5,506	6,042
Total noninterest income	$25,537	$20,682	$50,766	$43,738

Noninterest income for the three months ended June 30, 2013 was $25.5 million, up 23.5% compared with $20.7 million for the same period in 2012. Increases in other financial services revenue, service charges on deposit accounts, ATM and debit card fees, trust revenue and bank owned life insurance were primarily the result of the acquisition of Alliance. Retirement plan administration fees increased approximately $0.5 million for the three months ended June 30, 2013, compared to the three months ended June 30, 2012, due primarily to the addition of two large clients during the third quarter of 2012.

Noninterest income for the six months ended June 30, 2013 was $50.8 million, up 16.1% from the same period in 2012, with the primary drivers being the aforementioned increases in trust revenue and ATM and debit card fees. In addition, insurance and financial services revenue increased 10.6% for the six months ended June 30, 2013 as compared to the same period in 2012, due primarily to an increase in financial services revenue from the Alliance acquisition as well as an increase in insurance contingent revenue in 2013. Retirement plan administration fees were also up 18.9% for the six months ended June 30, 2013 as compared to the same period in 2012 due to growth in new business in 2012.

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Noninterest Expense

Noninterest expenses are also an important factor in the Company's results of operations. The following table sets forth the major components of noninterest expense for the periods indicated:

	Three months ended June 30,		Six months ended June 30,	
	2013	2012	2013	2012
(in thousands)				
Salaries and employee benefits	$29,160	$24,992	$56,207	$51,717
Occupancy	5,219	4,222	10,196	8,713
Data processing and communications	3,854	3,431	7,309	6,689
Professional fees and outside services	3,237	2,388	6,138	5,113
Equipment	2,910	2,409	5,492	4,789
Office supplies and postage	1,656	1,574	3,246	3,245
FDIC expenses	1,273	942	2,403	1,873
Advertising	1,000	805	1,723	1,607
Amortization of intangible assets	1,351	841	2,202	1,660
Loan collection and other real estate owned	421	799	1,139	1,437
Merger	1,269	826	11,950	1,337
Other	5,100	4,161	9,150	7,684
Total noninterest expense	$56,450	$47,390	$117,155	$95,864

Noninterest expense for the three months ended June 30, 2013 was $56.5 million, up $9.1 million or 19.1%, for the same period in 2012. Excluding merger expenses totaling $1.3 million during the second quarter of 2013 and $0.8 million during the second quarter of 2012, noninterest expense was up $8.6 million, or 18.5%, for the second quarter of 2013 as compared to the second quarter of 2012. Increases in noninterest expenses were primarily due to the Alliance and Hampshire First Bank acquisitions. The Company experienced a decrease in loan collection and other real estate owned expense by 47% compared to the prior year quarter and 21% from the prior year to date period.

Noninterest expense for the six months ended June 30, 2013 was $117.2 million, up $21.3 million or 22.2%, from the same period in 2012. Excluding merger expenses totaling $12.0 million and $1.3 million for the six months ended June 30, 2013 and 2012, respectively, noninterest expense was up $10.7 million, or 11.3%, for the first six months of 2013 as compared to the same period in 2012. Several noninterest expense categories were affected by the acquisition of Alliance and Hampshire First Bank with salaries and employee benefits and occupancy expenses being the primary drivers of the increase over last year.

Income Taxes

Income tax expense for the three month period ended June 30, 2013 was $7.4 million, up from $5.7 million for the same period in 2012. The effective tax rate was 30.5% for the three months ended June 30, 2013, compared to 30.0% for the same period in 2012.

Income tax expense for the six months ended June 30, 2013 was $10.8 million, down from $11.5 million from the same period in 2012 due to the decrease in pre-tax income for the first six months of 2013, offset slightly by the increase in the effective tax rate to 30.5% for the six months ended June 30, 2013 as compared with 30.0% for the same period last year.

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ANALYSIS OF FINANCIAL CONDITION

Securities

Average total earning securities increased $214.5 million, or 16.8%, for the three months ended June 30, 2013 when compared to the same period in 2012. This increase resulted primarily from the Alliance acquisition. The average total securities portfolio represents 21.9% of total average earning assets for the three months ended June 30, 2013, down from 23.9% for the same period in 2012.

Average total earning securities increased $91.3 million, or 7.1%, for the six months ended June 30, 2013 when compared to the same period in 2012. This increase resulted primarily from the acquisition of Alliance, partly offset by the scheduled run-off of municipal securities in the held to maturity portfolio. The average total securities portfolio represents 21.7% of total average earning assets for the six months ended June 30, 2013, down from 24.3% for the same period in 2012.

The following table details the composition of securities available for sale, securities held to maturity and regulatory investments for the periods indicated:

	June 30, 2013	December 31, 2012
Mortgage-backed securities:		
With maturities 15 years or less	21 %	18 %
With maturities greater than 15 years	1 %	2 %
Collateral mortgage obligations	38 %	36 %
Municipal securities	13 %	12 %
US agency notes	24 %	28 %
Other	3 %	4 %
Total	100 %	100 %

The Company's mortgage backed securities, U.S. agency notes, and collateralized mortgage obligations are all "prime/conforming" and are guaranteed by Fannie Mae, Freddie Mac, Federal Home Loan Bank, Federal Farm Credit Banks, or Ginnie Mae ("GNMA"). GNMA securities are considered equivalent to U.S. Treasury securities, as they are backed by the full faith and credit of the U.S. government. Currently, there are no subprime mortgages in our investment portfolio.

Loans

A summary of loans, net of deferred fees and origination costs, by category for the periods indicated follows:

(In thousands)	June 30, 2013	December 31, 2012
Residential real estate mortgages	$1,001,642	$651,107
Commercial	867,513	694,799
Commercial real estate mortgages	1,241,271	1,072,807
Real estate construction and development	152,548	123,078
Agricultural and agricultural real estate mortgages	107,565	112,687
Consumer	1,284,888	1,047,856
Home equity	635,283	575,282
Total loans	$5,290,710	$4,277,616

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Total loans increased by $1.0 billion, or 23.7%, at June 30, 2013 from December 31, 2012, and represent approximately 70.2% of assets, as compared to 70.8% of total assets at December 31, 2012. The increase in loan is primarily due to the loans acquired in the Alliance acquisition combined with organic growth during the second quarter of 2013. The following table summarizes the Alliance acquired loan balances at fair value of as of March 8, 2013 (in thousands):

	Acquired Balances
Residential real estate mortgages	$333,105
Commercial	179,672
Commercial real estate mortgages	117,752
Consumer	200,470
Home equity	73,474
Total loans	$904,473

Allowance for Loan Losses, Provision for Loan Losses, and Nonperforming Assets

The allowance for loan losses is maintained at a level estimated by management to provide adequately for risk of probable losses inherent in the current loan portfolio. The adequacy of the allowance for loan losses is continuously monitored using a methodology designed to ensure that the level of the allowance reasonably reflects the loan portfolio's risk profile. It is evaluated to ensure that it is sufficient to absorb all reasonably estimable credit losses inherent in the current loan portfolio.

Management considers the accounting policy relating to the allowance for loan losses to be a critical accounting policy given the degree of judgment exercised in evaluating the level of the allowance required to cover credit losses in the portfolio and the material effect that such judgments can have on the consolidated results of operations.

For purposes of evaluating the adequacy of the allowance, the Company considers a number of significant factors that affect the collectability of the portfolio. For individually analyzed loans, these factors include estimates of loss exposure, which reflect the facts and circumstances that affect the likelihood of repayment of such loans as of the evaluation date. For homogeneous pools of loans, estimates of the Company's exposure to credit loss reflect a thorough current assessment of a number of factors, which could affect collectability. These factors include: past loss experience; the size, trend, composition, and nature of the loans; changes in lending policies and procedures, including underwriting standards and collection, charge-off and recovery practices; trends experienced in nonperforming and delinquent loans; current economic conditions in the Company's market; portfolio concentrations that may affect loss experienced across one or more components of the portfolio; the effect of external factors such as competition, legal and regulatory requirements; and the experience, ability, and depth of lending management and staff. In addition, various regulatory agencies, as an integral component of their examination process, periodically review the Company's allowance for loan losses. Such agencies may require the Company to recognize additions to the allowance based on their judgment about information available to them at the time of their examination, which may not be currently available to management.

After a thorough consideration and validation of the factors discussed above, required additions or reductions to the allowance for loan losses are made periodically by charges or credits to the provision for loan losses. These charges are necessary to maintain the allowance at a level which management believes is reasonably reflective of the overall inherent risk of probable loss in the portfolio. While management uses available information to recognize losses on loans, additions or reductions to the allowance may fluctuate from one reporting period to another. These fluctuations are reflective of changes in risk associated with portfolio content and/or changes in management's assessment of any or all of the determining factors discussed above. Management considers the allowance for loan losses to be adequate based on evaluation and analysis of the loan portfolio.

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The following table reflects changes to the allowance for loan losses for the periods presented. The allowance is increased by provisions for losses charged to operations and is reduced by net charge-offs. Charge-offs are made when the ability to collect loan principal within a reasonable time becomes unlikely. Any recoveries of previously charged-off loans are credited directly to the allowance for loan losses.

Allowance For Loan Losses

	Three months ended			
(dollars in thousands)	June 30, 2013		June 30, 2012	
Balance, beginning of period	$ 68,734		$ 71,334	
Recoveries	1,201		977	
Chargeoffs	(5,153)		(5,680)	
Net chargeoffs	(3,952)		(4,703)	
Provision for loan losses	6,402		4,103	
Balance, end of period	$ 71,184		$ 70,734	
Composition of Net Chargeoffs				
Commercial and agricultural	$ (782)	20 %	$ (1,350)	29 %
Real estate mortgage	(213)	5 %	(285)	6 %
Consumer	(2,957)	75 %	(3,068)	65 %
Net chargeoffs	$ (3,952)	100 %	$ (4,703)	100 %
Annualized net chargeoffs to average loans	0.30 %		0.48 %	

Allowance For Loan Losses

	Six months ended			
(dollars in thousands)	June 30, 2013		June 30, 2012	
Balance, beginning of period	$ 69,334		$ 71,334	
Recoveries	2,659		2,046	
Chargeoffs	(12,869)		(11,220)	
Net chargeoffs	(10,210)		(9,174)	
Provision for loan losses	12,060		8,574	
Balance, end of period	$ 71,184		$ 70,734	
Composition of Net Chargeoffs				
Commercial and agricultural	$ (3,637)	36 %	$ (2,095)	23 %
Real estate mortgage	(870)	9 %	(634)	7 %
Consumer	(5,703)	55 %	(6,445)	70 %
Net chargeoffs	$ (10,210)	100 %	$ (9,174)	100 %
Annualized net chargeoffs to average loans	0.42 %		0.48 %	

Nonperforming assets consist of nonaccrual loans, loans 90 days or more past due and still accruing, restructured loans, OREO, and nonperforming securities. Loans are generally placed on nonaccrual when principal or interest payments become ninety days past due, unless the loan is well secured and in the process of collection. Loans may also be placed on nonaccrual when circumstances indicate that the borrower may be unable to meet the contractual principal or interest payments. OREO represents property acquired through foreclosure and is valued at the lower of the carrying amount or fair value, less any estimated disposal costs. Nonperforming securities include securities which management believes are other-than-temporarily impaired, are carried at their estimated fair value and are not accruing interest.

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Nonperforming Assets

(Dollars in thousands)	June 30, 2013		December 31, 2012	
Nonaccrual loans	Amount	%	Amount	%
Commercial and agricultural loans and real estate	$18,974	46 %	$20,923	53 %
Real estate mortgages	8,341	21 %	8,083	20 %
Consumer	7,534	19 %	8,440	21 %
Troubled debt restructured loans	5,676	14 %	2,230	6 %
Total nonaccrual loans	40,525	100%	39,676	100%
Loans 90 days or more past due and still accruing				
Commercial and agricultural loans and real estate	-	0 %	148	6 %
Real estate mortgages	358	18 %	330	13 %
Consumer	1,646	82 %	1,970	81 %
Total loans 90 days or more past due and still accruing	2,004	100%	2,448	100%
Total nonperforming loans	42,529		42,124	
Other real estate owned (OREO)	3,757		2,276	
Total nonperforming assets	46,286		44,400	
Total nonperforming loans to total loans	0.80 %		0.98 %	
Total nonperforming assets to total assets	0.61 %		0.73 %	
Allowance for loan losses to total nonperforming loans	167.38%		164.60%	

Past due loans as a percentage of total loans was 0.71% at June 30, 2013, equal to December 31, 2012. In addition to nonperforming loans, the Company has also identified approximately $91.0 million in potential problem loans at June 30, 2013 as compared to $79.6 million at December 31, 2012. The increase is primarily due to the acquired loans of Alliance. At June 30, 2013, potential problem loans primarily consisted of commercial real estate and commercial and agricultural loans. Potential problem loans are loans that are currently performing, but known information about possible credit problems of the borrowers causes management to have serious doubts as to the ability of such borrowers to comply with the present loan repayment terms and which may result in classification of such loans as nonperforming at some time in the future. Potential problem loans are typically defined as loans that are performing but are classified by the Company's loan rating system as "substandard." Management cannot predict the extent to which economic conditions may worsen or other factors which may impact borrowers and the potential problem loans. Accordingly, there can be no assurance that other loans will not become 90 days or more past due, be placed on nonaccrual, become restructured, or require increased allowance coverage and provision for loan losses.

The Company recorded a provision for loan losses of $6.4 million for the three months ended June 30, 2013, compared with $4.1 million for the three months ended June 30, 2012. This increase was due primarily to a $1.4 million specific reserve established on a commercial real estate loan during the second quarter and loan growth during the period, partially offset by a general improvement in asset quality indicators. Net charge-offs were $4.0 million for the three months ended June 30, 2013, down from $4.7 million for the same period in 2012. Net charge-offs (annualized) to average loans for the three months ended June 30, 2013 was 0.30%, compared to 0.48% for the three months ended June 30, 2012.

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The Company recorded a provision for loan losses of $12.1 million for the six months ended June 30, 2013, compared with $8.6 million for the three months ended June 30, 2012. This increase was due primarily to the aforementioned specific reserve in the second quarter of 2013 and organic loan growth during the period, partially offset by a general improvement in asset quality indicators. Net charge-offs were $10.2 million for the six months ended June 30, 2013, up from $9.2 million for the same period in 2012, due primarily to the charge-off of one large commercial loan that was previously reserved for. Net charge-offs to average loans for the six months ended June 30, 2013 was 0.42%, compared to 0.48% for the six months ended June 30, 2012.

The allowance for loan losses totaled $71.2 million at June 30, 2013, compared to $69.3 million at December 31, 2012. The allowance for loan losses as a percentage of loans was 1.35% (1.68% excluding acquired loans with no related allowance recorded) at June 30, 2013, compared to 1.62% (1.72% excluding acquired loans with no related allowance recorded) at December 31, 2012.

Subprime mortgage lending, which has been the riskiest sector of the residential housing market, is not a market that the Company has ever actively pursued. The market does not apply a uniform definition of what constitutes "subprime" lending. Our reference to subprime lending relies upon the "Statement on Subprime Mortgage Lending" issued by the Office of Thrift Supervision and the other federal bank regulatory agencies, or the Agencies, on September 29, 2007, which further referenced the "Expanded Guidance for Subprime Lending Programs," or the Expanded Guidance, issued by the Agencies by press release dated January 31, 2001. In the Expanded Guidance, the Agencies indicated that subprime lending does not refer to individual subprime loans originated and managed, in the ordinary course of business, as exceptions to prime risk selection standards. The Agencies recognize that many prime loan portfolios will contain such accounts. The Agencies also excluded prime loans that develop credit problems after acquisition and community development loans from the subprime arena. According to the Expanded Guidance, subprime loans are other loans to borrowers which display one or more characteristics of reduced payment capacity. Five specific criteria, which are not intended to be exhaustive and are not meant to define specific parameters for all subprime borrowers and may not match all markets or institutions' specific subprime definitions, are set forth, including having a FICO score of 660 or below. Based upon the definition and exclusions described above, management believes that the Company is a prime lender. Within the loan portfolio, there are loans that, at the time of origination, had FICO scores of 660 or below. However, since the Company is a portfolio lender, it reviews all data contained in borrower credit reports and does not base underwriting decisions solely on FICO scores. We believe the aforementioned loans, when made, were amply collateralized and otherwise conformed to our prime lending standards. The Company has not originated Alt A loans or no interest loans.

Deposits

Total deposits were $5.9 billion at June 30, 2013, up $1.1 billion, or 22.9%, from December 31, 2012, due primarily to the acquisition of Alliance on March 8, 2013. Savings, NOW and money market accounts increased to $3.3 billion as of June 30, 2013 as compared with $2.6 billion at December 31, 2012. Time deposits increased $121.8 million, or 12.4%, from December 31, 2012 to June 30, 2013. Demand deposits increased by $273.7 million, or 22.0%, from December 31, 2012 to June 30, 2013.

The following table summarizes the Alliance acquired deposit balances at fair value of as of March 8, 2013 (in thousands):

	Acquired Balances
Noninterest bearing demand	$222,843
Savings, NOW and money market	660,412
Time	230,165
Total	$1,113,420

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Total average deposits for the three months ended June 30, 2013 increased $1.4 billion, or 29.6%, from the same period in 2012, due primarily to the acquisitions of Hampshire First Bank and Alliance. Average savings accounts increased to $983.4 million for the second quarter of 2013 from $676.8 million for the same period in 2012. Average time deposits increased $163.5 million, or 16.8%, for the three months ended June 30, 2013 from the same period in 2012. Average demand deposit (interest and noninterest bearing) accounts increased $606.8 million, or 33.4%, for the three months ended June 30, 2013 as compared to the same period in 2012.

Total average deposits for the six months ended June 30, 2013 increased $991.5 million, or 22.0%, from the same period in 2012, due primarily to the acquisitions of Hampshire First Bank and Alliance. Average savings accounts increased to $877.6 million for the first six months of 2013 from $659.4 million for the same period in 2012. Average time deposits increased $111.7 million, or 11.6%, for the six months ended June 30, 2013 from the same period in 2012. Average demand deposit (interest and noninterest bearing) accounts increased $467.1 million, or 26.1%, for the six months ended June 30, 2013 as compared to the same period in 2012.

Borrowed Funds

The Company's borrowed funds consist of short-term borrowings and long-term debt. Short-term borrowings totaled $385.6 million at June 30, 2013 compared to $162.9 million at December 31, 2012. Long-term debt was $309.1 million at June 30, 2013, as compared to $367.5 million at December 31, 2012. The Company assumed $21.6 million in short-term customer sweep accounts and $100.0 million in long-term FHLB advances from Alliance on March 8, 2013. The Company paid down $40.0 million of the long-term FHLB advances assumed from Alliance prior to the end of the first quarter and $119 million of long-term borrowings matured in the second quarter of 2013, resulting in the net decrease in long-term borrowed funds compared to year-end. Long term borrowings were replaced with short-term borrowings in the second quarter, resulting in the net increase in short-term borrowed funds compared to year-end. For more information about the Company’s borrowing capacity and liquidity position, see “Liquidity Risk” below.

Capital Resources

Stockholders' equity of $791.6 million represented 10.51% of total assets at June 30, 2013, compared with $582.3 million, or 9.64% as of December 31, 2012. The Company issued 10.3 million shares at a value of $226 million for the acquisition of Alliance on March 8, 2013. The Company held a 0.8% equity interest in Alliance prior to acquisition with an acquisition date fair value of $1.9 million. The Company realized a $1.0 million gain as a result of measuring the equity interest to fair value in accordance with step acquisition accounting.

Under a previously disclosed stock repurchase plan, the Company purchased 267,425 shares of its common stock during the six month period ended June 30, 2013, for a total of $5.5 million at an average price of $20.42 per share. At June 30, 2013, there were 480,588 shares available for repurchase under this repurchase plan, which expires on December 31, 2013.

On July 22, 2013, the Bank’s board of directors authorized a new repurchase program for the Company to repurchase up to an additional 1,000,000 shares (approximately 2%) of its outstanding common stock, effective July 24, 2013, as market conditions warrant in open market and privately negotiated transactions. This plan expires on December 31, 2014.

The Board of Directors considers the Company's earnings position and earnings potential when making dividend decisions. The Company does not have a target dividend pay-out ratio.

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As the capital ratios in the following table indicate, the Company remained “well capitalized” at June 30, 2013 under applicable bank regulatory requirements. Capital measurements are well in excess of regulatory minimum guidelines and meet the requirements to be considered well capitalized for all periods presented. Tier 1 leverage, Tier 1 capital and Total risk-based capital ratios have regulatory minimum guidelines of 3%, 4% and 8% respectively, with requirements to be considered well capitalized of 5%, 6% and 10%, respectively. The Tier 1 leverage ratio was 8.72% at June 30, 2013 compared to 8.54% at December 31, 2012.

Capital Measurements	June 30, 2013	December 31, 2012
Tier 1 leverage ratio	8.72 %	8.54 %
Tier 1 capital ratio	11.20%	11.00 %
Total risk-based capital ratio	12.45%	12.25 %
Cash dividends as a percentage of net income	63.37%	48.96 %
Per common share:		
Book value	$18.18	$ 17.24
Tangible book value (1)	$11.46	$ 12.23

(1) Stockholders' equity less goodwill and intangible assets divided by common shares outstanding

On July 2, 2013, the Federal Reserve Board issued final rules and on July 9, 2013, the Office of the Comptroller of the Currency issued interim final rules implementing the Basel III capital standards. The final rules change how banks and their holding companies calculate their regulatory capital requirements by increasing the minimum levels of required capital, narrowing the definition of capital and placing greater emphasis on common equity. The Company is still in the process of assessing the impacts of these rules, however, we believe we will continue to exceed all estimated well capitalized regulatory requirements on a fully phased-in basis.

Liquidity and Interest Rate Sensitivity Management

Market Risk

Interest rate risk is the primary market risk affecting the Company. Other types of market risk, such as foreign currency exchange rate risk and commodity price risk, do not arise in the normal course of the Company’s business activities. Interest rate risk is defined as an exposure to a movement in interest rates that could have an adverse effect on the Company’s net interest income. Net interest income is susceptible to interest rate risk to the degree that interest bearing liabilities mature or reprice on a different basis than earning assets. When interest bearing liabilities mature or reprice more quickly than earning assets in a given period, a significant increase in market rates of interest could adversely affect net interest income. Similarly, when earning assets mature or reprice more quickly than interest bearing liabilities, falling interest rates could result in a decrease in net interest income.

In an attempt to manage the Company's exposure to changes in interest rates, management monitors the Company’s interest rate risk. Management’s Asset Liability Committee (“ALCO”) meets monthly to review the Company’s interest rate risk position and profitability, and to recommend strategies for consideration by the Board of Directors. Management also reviews loan and deposit pricing and the Company’s securities portfolio, formulates investment and funding strategies, and oversees the timing and implementation of transactions to assure attainment of the Board’s objectives in the most effective manner. Notwithstanding the Company’s interest rate risk management activities, the potential effect of changing interest rates is an uncertainty that can have an adverse effect on net income.

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In adjusting the Company's asset/liability position, the Board and management attempt to manage the Company's interest rate risk while minimizing net interest margin compression. At times, depending on the level of general interest rates, the relationship between long- and short-term interest rates, market conditions and competitive factors, the Board and management may determine to increase the Company's interest rate risk position somewhat in order to increase its net interest margin. The Company's results of operations and net portfolio values remain vulnerable to changes in interest rates and fluctuations in the difference between long- and short-term interest rates. Assuming interest rates remain at or near current historical lows, net interest margin will continue to experience compression. Additional rate reductions on deposits are becoming more difficult as deposit rates are at or near their floors, and with asset yields continuing to reprice at lower rates, this could result in additional margin pressure as well as a decrease in net interest income.

The primary tool utilized by ALCO to manage interest rate risk is a balance sheet/income statement simulation model (interest rate sensitivity analysis). Information such as principal balance, interest rate, maturity date, cash flows, next repricing date (if needed), and current rates is uploaded into the model to create an ending balance sheet. In addition, ALCO makes certain assumptions regarding prepayment speeds for loans and mortgage related investment securities along with any optionality within the deposits and borrowings.

The model is first run under an assumption of a flat rate scenario (i.e. no change in current interest rates) with a static balance sheet over a 12-month period. Two additional models are run with static balance sheets: (1) a gradual increase of 200 bp, and (2) a gradual decrease of 100 bp taking place over a 12-month period. Under these scenarios, assets subject to prepayments are adjusted to account for faster or slower prepayment assumptions. Any investment securities or borrowings that have callable options embedded into them are handled accordingly based on the interest rate scenario. The resulting changes in net interest income are then measured against the flat rate scenario.

In the declining rate scenario, net interest income is projected to decrease when compared to the forecasted net interest income in the flat rate scenario through the simulation period. The decrease in net interest income is a result of earning assets repricing downward at a faster rate than interest bearing liabilities. The inability to effectively lower deposit rates will likely reduce or eliminate the benefit of lower interest rates. In the rising rate scenarios, net interest income is projected to experience a decline from the flat rate scenario. Net interest income is projected to remain at lower levels than in a flat rate scenario through the simulation period primarily due to a lag in assets repricing while funding costs increase. The potential impact on earnings is dependent on the ability to lag deposit repricing. If short-term rates continue to increase, the Company expects competitive pressures will likely lead to core deposit pricing increases, which will likely continue compression of the net interest margin.

Net interest income for the next 12 months in the + 200/- 100 bp scenarios, as described above, is within the internal policy risk limits of not more than a 7.5% change in net interest income. The following table summarizes the percentage change in net interest income in the rising and declining rate scenarios over a 12-month period from the forecasted net interest income in the flat rate scenario using the June 30, 2013 balance sheet position:

Interest Rate Sensitivity Analysis

Change in interest rates (in bp points)	Percent change in net interest income
+200	(3.16%)
-100	(1.45%)

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Liquidity Risk

Liquidity involves the ability to meet the cash flow requirements of customers who may be depositors wanting to withdraw funds or borrowers needing assurance that sufficient funds will be available to meet their credit needs. The ALCO is responsible for liquidity management and has developed guidelines which cover all assets and liabilities, as well as off balance sheet items that are potential sources or uses of liquidity. Liquidity policies must also provide the flexibility to implement appropriate strategies and tactical actions. Requirements change as loans grow, deposits and securities mature, and payments on borrowings are made. Liquidity management includes a focus on interest rate sensitivity management with a goal of avoiding widely fluctuating net interest margins through periods of changing economic conditions.

The primary liquidity measurement the Company utilizes is called the Basic Surplus, which captures the adequacy of its access to reliable sources of cash relative to the stability of its funding mix of average liabilities. Basic Surplus is calculated by subtracting short-term liabilities from liquid assets. This approach recognizes the importance of balancing levels of cash flow liquidity from short- and long-term securities with the availability of dependable borrowing sources which can be accessed when necessary. At June 30, 2013, the Company's Basic Surplus measurement was 8.3% of total assets or approximately $625 million as compared to the December 31, 2012 Basic Surplus of 9.0% or $540 million, and was above the Company's minimum of 5% or $375 million set forth in its liquidity policies.

This Basic Surplus approach enables the Company to adequately manage liquidity from both operational and contingency perspectives. By tempering the need for cash flow liquidity with reliable borrowing facilities, the Company is able to operate with a more fully invested and, therefore, higher interest income generating securities portfolio. The makeup and term structure of the securities portfolio is, in part, impacted by the overall interest rate sensitivity of the balance sheet. Investment decisions and deposit pricing strategies are impacted by the liquidity position.

The Company's primary source of funds is the Bank. Certain restrictions exist regarding the ability of the Bank to transfer funds to the Company in the form of cash dividends. The approval of the Office of Comptroller of the Currency (OCC) is required to pay dividends when a bank fails to meet certain minimum regulatory capital standards or when such dividends are in excess of a subsidiary bank's earnings retained in the current year plus retained net profits for the preceding two years (as defined in the regulations). At June 30, 2013, approximately $26.3 million of the total stockholders' equity of the Bank was available for payment of dividends to the Company without approval by the OCC. The Bank's ability to pay dividends is also subject to the Bank being in compliance with regulatory capital requirements. The Bank is currently in compliance with these requirements. Under the General Corporation Law of the State of Delaware, the Company may declare and pay dividends either out of its surplus or, in case there is no surplus, out of its net profits for the fiscal year in which the dividend is declared and/or the preceding fiscal year.

At June 30, 2013 and December 31, 2012, FHLB advances outstanding totaled approximately $529 million and $339 million, respectively. The Bank is a member of the FHLB system and had additional borrowing capacity from the FHLB of approximately $557 million at June 30, 2013 and $418 million at December 31, 2012. In addition, unpledged securities could have been used to increase borrowing capacity at the FHLB by an additional $332 million at June 30, 2013, or used to collateralize other borrowings, such as repurchase agreements. At June 30, 2013 the Bank also had additional borrowing capacity from unused collateral at the Federal Reserve of $697 million.

Recent Accounting Pronouncements

Accounting Standards Update ("ASU") 2011-11, "Balance Sheet" (Topic 210) - Disclosures about Offsetting Assets and Liabilities" amends Topic 210, "Balance Sheet," to require an entity to disclose both gross and net information about financial instruments, such as sales and repurchase agreements and reverse sale and repurchase agreements and securities borrowing/lending arrangements, and derivative instruments that are eligible for offset in the statement of financial position and/or subject to a master netting arrangement or similar agreement. In October 2012, the FASB limited the scope to derivatives, repurchase and reverse purchase agreements, and securities borrowing and lending agreements subject to master netting arrangements or similar agreements. ASU 2011-11 was effective for annual and interim periods beginning on January 1, 2013, and did not have a significant impact on the Company’s financial statements.

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ASU 2012-02 “Intangibles – Goodwill and Other (Topic 350) – Testing Indefinite-Lived Intangible Assets for Impairment” gives entities the option to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that an indefinite-lived intangible asset is impaired. If, after assessing the totality of events or circumstances, an entity determines it is more likely than not that an indefinite-lived intangible asset is impaired, then the entity must perform the quantitative impairment test. If, under the quantitative impairment test, the carrying amount of the intangible asset exceeds its fair value, an entity should recognize an impairment loss in the amount of that excess. Permitting an entity to assess qualitative factors when testing indefinite-lived intangible assets for impairment results in guidance that is similar to the goodwill impairment testing guidance in ASU 2011-08. ASU 2012-02 was effective for the Company beginning January 1, 2013 (early adoption permitted) and did not have an impact on the Company’s financial statements.

ASU 2013-01 “Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities” was issued in January 2013 and clarifies that the scope of ASU 2011-11 would apply to derivatives including bifurcated embedded derivatives, repurchase agreements and reverse repurchase agreements, and securities borrowing and securities lending transactions that are either offset in accordance with Section 210-20-45 or Section 815-10-45 or are subject to a master netting arrangement or similar agreement. ASU 2013-01 was effective for annual and interim periods beginning on January 1, 2013, and did not have a significant impact on the Company’s financial statements.

ASU 2013-02 “Reporting of Amounts Reclassified Out of Other Comprehensive Income” was issued in February 2013 and amends, supersedes and replaces the presentation requirements for reclassifications out of accumulated other comprehensive income in ASUs 2011-05 (issued in June 2011) and 2011-12 (issued in December 2011) for all public and private organizations. The amendments would require an entity to provide additional information about reclassifications out of accumulated other comprehensive income. ASU 2013-02 was effective for the Company beginning January 1, 2013 and did not have a significant impact on the Company’s financial statements.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Information called for by Item 3 is contained in the Liquidity and Interest Rate Sensitivity Management section of the Management’s Discussion and Analysis of Financial Condition and Results of Operations.

Item 4. CONTROLS AND PROCEDURES

The Company's management, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended). Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that, as of June 30, 2013, the Company's disclosure controls and procedures were effective.

There were no changes made in the Company's internal control over financial reporting that occurred during the Company's most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

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PART II. OTHER INFORMATION

Item 1 – LEGAL PROCEEDINGS

There are no material legal proceedings, other than ordinary routine litigation incidental to the business, to which the Company or any of its subsidiaries is a party or of which any of their property is subject, except as described in the Company's 2012 Annual Report on Form 10-K.

Item 1A – RISK FACTORS

There are no material changes to the risk factors as previously discussed in Item 1A, to Part 1 of our 2012 Annual Report on Form 10-K.

Item 2 – UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

(a) Not applicable

(b) Not applicable

(c) The table below sets forth the information with respect to purchases made by the Company (as defined in Rule 10b-18(a)(3) under the Securities Exchange Act of 1934), of our common stock during the quarter ended June 30, 2013:

Period	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans	Maximum Number of Shares That May Yet be Purchased Under The Plans (1)
4/1/13 - 4/30/13	-	-	-	748,013
5/1/13 - 5/31/13	-	-	-	748,013
6/1/13 - 6/30/13	267,425	$ 20.42	267,425	480,588
Total	267,425	$ 20.42	267,425	480,588

(1) Under a previously disclosed stock repurchase plan announced on October 24, 2011, the Company purchased 267,425 shares of its common stock during the three month period ended June 30, 2013, for a total of $5.5 million at an average price of $20.42 per share. At June 30, 2013, there were 480,588 shares available for repurchase under the previously disclosed repurchase plan, which expires on December 31, 2013. On July 22, 2013, the Company's board of directors authorized a new repurchase program to repurchase up to an additional 1,000,000 shares of its outstanding common stock. This plan expires on December 31, 2014.

Item 3 – DEFAULTS UPON SENIOR SECURITIES

None

Item 4 – MINE SAFETY DISCLOSURES

None

Item 5 – OTHER INFORMATION

None

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Item 6 – EXHIBITS

3.1	Certificate of Incorporation of NBT Bancorp Inc. as amended through May 2, 2012 (filed as Exhibit 3.1 to the Registrant's Form 10-Q for the quarter ended September 30, 2012, filed on November 9, 2012 and incorporated herein by reference).
3.2	Amended and Restated By-laws of NBT Bancorp Inc., effective May 7, 2013 (filed as Exhibit 3.1 to the Registrant's Form 8-K, filed on May 7, 2013 and incorporated herein by reference).
3.3	Certificate of Designation of the Series A Junior Participating Preferred Stock (filed as Exhibit A to Exhibit 4.1 of the Registrant's Form 8-K, filed on November 18, 2004, and incorporated herein by reference).
4.1	Specimen common stock certificate for NBT's common stock (filed as exhibit 4.3 to the Registrant's Amendment No. 1 to Registration Statement on Form S-4 filed on December 27, 2005 and incorporated herein by reference).
4.2	Rights Agreement, dated as of November 15, 2004, between NBT Bancorp Inc. and Registrar and Transfer Company, as Rights Agent (filed as Exhibit 4.1 to the Registrant's Form 8-K, file number 0-14703, filed on November 18, 2004, and incorporated by reference herein).
31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Written Statement of the Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Written Statement of the Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document.
101.SCH	XBRL Taxonomy Extension Schema Document.
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.

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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, this 8th day of August 2013.

NBT BANCORP INC.

By: /s/ Michael J. Chewens
Michael J. Chewens, CPA
Senior Executive Vice President
Chief Financial Officer

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