CHEMUNG FINANCIAL CORP
Form 10-K
March 14, 2014

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

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

For the fiscal year ended December 31, 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 0-13888

CHEMUNG FINANCIAL CORPORATION
(Exact name of registrant as specified in its charter)

NEW YORK	16-123703-8
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
One Chemung Canal Plaza, P.O. Box 1522, Elmira, New York	14902
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (607) 737-3711

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, Par Value $0.01 Per Share	NASDAQ Stock Market, LLC

Securities registered pursuant to Section 12(g) of the Act:
(Title of Class)
None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
YES o NO x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.
YES o NO x

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 (§ 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

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

Large accelerated filer	o	Accelerated filer	x	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

Based upon the closing price of the registrant's Common Stock as of June 30, 2013, the aggregate market value of the voting stock held by non-affiliates of the registrant was $117,114,195.

As of March 14, 2014, there were 4,614,382 shares of Common Stock, $0.01 par value, outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the Annual Meeting of Shareholders to be held on May 8, 2014 are incorporated by reference into Part III, Items 10, 11, 12, 13, and 14 of this Form 10-K.

CHEMUNG FINANCIAL CORPORATION

ANNUAL REPORT ON FORM 10-K FOR THE FISCAL YEAR ENDED DECEMBER 31, 2013

Form 10-K Item Number:	Page No.
PART I	1
Item 1. Business	1
Item 1A. Risk Factors	16
Item 1B. Unresolved Staff Comments	22
Item 2. Properties	23
Item 3. Legal Proceedings	23
Item 4. Mine Safety Disclosures	23
PART II	24
Item 5. Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	24
Item 6. Selected Financial Data	26
Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations	28
Item 7A. Quantitative and Qualitative Disclosures about Market Risk	50
Item 8. Financial Statements and Supplementary Data	51
Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	51
Item 9A. Controls and Procedures	51
Item 9B. Other Information	52
PART III	53
Item 10. Directors, Executive Officers and Corporate Governance	53
Item 11. Executive Compensation	53
Item 12. Security Ownership of Certain Beneficial Owners and Management, and Related Stockholder Matters	53
Item 13. Certain Relationships and Related Transactions, and Director Independence	53
Item 14. Principal Accountant Fees and Services	53
PART IV	54
Item 15. Exhibits and Financial Statement Schedules	54
Index to Consolidated Financial Statements	56
Report of Independent Registered Public Accounting Firm-Crowe Horwath LLP	F-1

SIGNATURES	F-56

Some of the information contained in this report concerning the markets and industry in which we operate is derived from publicly available information and from industry sources. Although we believe that this publicly available information and information provided by these industry sources are reliable, we have not independently verified the accuracy of any of this information.

To assist the reader, the Corporation has provided the following list of commonly used acronyms and abbreviations included in Part I.

FASB: Financial Accounting Standards Board	OTTI: Other-than-temporary impairment
FDIC: Federal Deposit Insurance Corporation	PCI: Purchased credit impaired
FHLBNY: Federal Home Loan Bank of New York	SEC: Securities and Exchange Commission
GAAP: U.S. generally accepted accounting principles	CDO: Collateralized Debt Obligation

PART I
ITEM 1. BUSINESS

General

Chemung Financial Corporation (the "Corporation") was incorporated on January 2, 1985 under the laws of the State of New York and is headquartered in Elmira, NY. The Corporation was organized for the purpose of acquiring Chemung Canal Trust Company (the "Bank"). The Bank was established in 1833 under the name Chemung Canal Bank, and was subsequently granted a New York State bank charter in 1895. In 1902, the Bank was reorganized as a New York State trust company under the name Elmira Trust Company, and its name was changed to Chemung Canal Trust Company in 1903.

The Corporation became a financial holding company in June, 2000. Financial holding company status provided the Corporation with the flexibility to offer an array of financial services, such as insurance products, mutual funds, and brokerage services, which provide additional sources of fee based income and allow the Corporation to better serve its customers. The Corporation established a financial services subsidiary, CFS Group, Inc., in September 2001 which offers non-banking financial services such as mutual funds, annuities, brokerage services, insurance and tax preparation services.

The Corporation's Board of Directors has concluded that the expansion of the franchise's geographic footprint, an increase in the Bank's earning assets and the generation of new sources of non-interest income are important components of its strategic plan. Towards that end, in recent years it has completed the following transactions:

- On May 3, 2007, the Bank acquired the trust business of Partners Trust Bank, Utica, New York. At the time of the acquisition, the Bank acquired $351.0 million in trust assets.

- On March 14, 2008, the Bank acquired three branches from Manufacturers and Traders Trust Company in the New York counties of Broome and Tioga. At the time of the acquisition, the Bank assumed $64.4 million in deposits and acquired $12.6 million in loans.

- On May 29, 2009, the Corporation acquired Canton Bancorp, Inc., the holding company of Bank of Canton based in Canton, Pennsylvania. At the time of the merger, Canton Bancorp, Inc. had $81.1 million in assets, $58.8 million in loans and $72.9 million in deposits.

- On April 8, 2011, the Corporation acquired Fort Orange Financial Corp. ("FOFC"), the holding company of Capital Bank & Trust Company ("Capital Bank") based in Albany, New York. At the time of the merger, Capital Bank had $254.4 million in assets, $170.7 million in loans and $199.2 million in deposits.

- On November 23, 2013, the Bank completed the acquisition of six branch offices from Bank of America located in Cayuga, Cortland, Seneca and Tompkins counties in New York. As part of the transaction, the Corporation acquired $177.7 million in deposits and $1.2 million in loans.

As a result of these transactions and organic growth, the Corporation had $1.476 billion in assets, $995.9 million in loans, $1.263 billion in deposits and $138.6 million in shareholders' equity at December 31, 2013.

Growth Strategy

The Corporation's growth strategy is to leverage its expanding branch network in current or new markets to build client relationships and grow loans and deposits. Consistent with the Corporation's community banking model, emphasis is placed on acquiring stable, low-cost deposits, primarily checking account deposits and other low interest-bearing deposits to fund high-quality loans. Expanding the branch network involves branch purchases or opening de novo branches in contiguous markets and acquiring other financial institutions in the Northeast. The Corporation evaluates acquisition targets based on the economic viability of the markets they are in, the degree to which they can be effectively integrated into the Corporation's current operations and the degree to which they are accretive to capital and earnings.

Description of Business

The Corporation, through the Bank and CFS Group, Inc., provides a wide range of financial services, including demand, savings and time deposits, commercial, residential and consumer loans, letters of credit, wealth management services, employee benefit plans, securities and insurance brokerage services. The Bank derives its income primarily from interest and fees on loans, interest on investment securities, Wealth Management Group fee income and fees received in connection with deposit and other services. The Bank's operating expenses are interest expense paid on deposits and borrowings, salaries and employee benefit plans and general operating expenses.

In order to compete with other financial services companies, the Corporation relies upon personal relationships established by its officers, employees and directors with our clients. The Corporation has maintained a strong community orientation by supporting the active participation of officers and employees in local charitable, civic, school, religious and community development activities. The Corporation believes that its emphasis on local relationship banking together with a prudent approach to lending, are important factors in its success and growth.

Lending Activities

Lending Strategy

The Corporation's objective is to channel deposits gathered locally into high-quality, market-yielding loans without taking unacceptable credit and/or interest rate risk. The Corporation seeks to have a diversified loan portfolio consisting of commercial and agricultural loans, commercial mortgages, residential mortgages, home equity lines of credit and home equity term loans, consumer and indirect auto loans. The Bank operates with a traditional community bank model where the relationship manager possesses credit skills and has significant influence over credit decisions. This creates value since clients and prospects know they are dealing with a decision maker.

Lending Authority

The Board of Directors establishes the lending policies, underwriting standards and loan approval limits of the Bank. In accordance with those policies, the Board of Directors has designated certain officers to consider and approve loans within their designated authority. These officers exercise substantial authority over credit and pricing decisions, subject to loan committee approval for larger credits. The Bank recognizes that exceptions to the lending policies may occasionally occur and has established procedures for approving exceptions to these policies.

2

In underwriting loans, primary emphasis is placed on the borrower's financial condition, including ability to generate cash flow to support the debt and other cash expenses. In addition, substantial consideration is given to collateral value and marketability as well as the borrower's character, reputation and other relevant factors. Interest rates charged by the Bank vary with degree of risk, type, size, complexity, repricing frequency and other relevant factors associated with the loans. Competition from other financial services companies also impacts interest rates charged on loans.

The Corporation has also implemented reporting systems to monitor loan originations, loan quality, concentrations of credit, loan delinquencies, non-performing loans and potential problem loans.

Lending Segments

The Corporation segments its loan portfolio into the following major lending categories: (i) commercial and agricultural, (ii) commercial mortgages, (iii) residential mortgages and (iv) consumer loans.

Commercial and agricultural loans primarily consist of loans to small to mid-sized businesses in our market area in a diverse range of industries. These loans are of higher risk and typically are made on the basis of the borrower's ability to make repayment from the cash flow of the borrower's business. Further, the collateral securing the loans may depreciate over time, may be difficult to appraise and may fluctuate in value. The credit risk related to commercial loans is largely influenced by general economic conditions and the resulting impact on a borrower's operations or on the value of underlying collateral, if any.

Commercial mortgage loans generally have larger balances and involve a greater degree of risk than residential mortgage loans, and they therefore pose higher potential losses on an individual customer basis. Loan repayment is often dependent on the successful operation and management of the properties and/or the businesses occupying the properties, as well as on the collateral securing the loan. Economic events or conditions in the real estate market could have an adverse impact on the cash flows generated by properties securing the Company's commercial real estate loans and on the value of such properties.

Residential mortgage loans are generally made on the basis of the borrower's ability to make repayment from his or her employment and other income, but are secured by real property whose value tends to be more easily ascertainable. Credit risk for these types of loans is generally influenced by general economic conditions, the characteristics of individual borrowers and the nature of the loan collateral.

The consumer loan segment includes home equity lines of credit and home equity loans, which exhibit many of the same risk characteristics as residential mortgages. Indirect and other consumer loans may entail greater credit risk than residential mortgage and home equity loans, particularly in the case of other consumer loans which are unsecured or, in the case of indirect consumer loans, secured by depreciable assets, such as automobiles or boats. In such cases, any repossessed collateral for a defaulted consumer loan may not provide an adequate source of repayment of the outstanding loan balance. In addition, consumer loan collections are dependent on the borrower's continuing financial stability, thus are more likely to be affected by adverse personal circumstances such as job loss, illness or personal bankruptcy. Furthermore, the application of various federal and state laws, including bankruptcy and insolvency laws, may limit the amount which can be recovered on such loans.

Funding Activities

Funding Strategy

The Corporation's deposit strategy is to fund the Bank with stable, low-cost deposits, primarily checking account deposits and other low interest-bearing deposit accounts. A checking account is the driver of a banking relationship and consumers consider the bank where they have their checking account as their primary bank. These customers will typically turn to their primary bank first when in need of other financial services. The Corporation also considers brokered deposits to be an element of its deposit strategy and anticipates that it will continue using brokered deposits as a secondary source of funding to support growth. Borrowings may be used on a short-term basis for liquidity purposes or on a long-term basis to fund asset growth.

Funding Sources

The Corporation's primary sources of funds are deposits, principal and interest payments on loans and securities, borrowings and funds generated from operations of the Bank. The Bank also has access to advances from the FHLBNY, other financial institutions and the FRBNY. Contractual loan payments are a relatively stable source of funds, while deposit inflows and outflows and loan prepayments are significantly influenced by general market interest rates and economic conditions.

The Corporation considers core deposits, consisting of non-interest-bearing and interest-bearing checking accounts, savings accounts, and insured money market accounts, to be a significant component of our deposits. The Corporation monitors the activity on these core deposits and, based on historical experience and pricing strategy, believes it will continue to retain a large portion of such accounts. The Bank is currently not limited with respect to the rates that it may offer on deposit products. The Bank believes it is competitive in the types of accounts and interest rates it has offered on its deposit products. The Bank regularly evaluates the internal cost of funds, surveys rates offered by competitors, reviews cash flow requirements for lending and liquidity, and executes rate changes when necessary as part of its asset/liability management, profitability and growth strategies.

The flow of deposits is influenced significantly by general economic conditions, changes in prevailing interest rates and competition. The Bank's deposits are obtained predominantly from the areas in which its retail offices are located. The Bank relies primarily on customer service, long-standing relationships and other banking services, including loans and wealth management services, to attract and retain these deposits. However, market interest rates and rates offered by competing financial institutions affect the Bank's ability to attract and retain deposits. The Bank uses traditional means of advertising its deposit products, including radio and print media.

Wealth Management Strategy

With $1.888 billion of assets under management or administration at year-end 2013, the Wealth Management Group is responsible for the largest component of non-interest income. Wealth management services provided by the Bank include services as executor and trustee under wills and agreements, and guardian, custodian, trustee and agent for pension, profit-sharing and other employee benefit trusts, as well as various investment, pension, estate planning and employee benefit administrative services. The Corporation's growth strategy also includes the acquisition of trust businesses to generate new sources of fee income.

The Corporation offers an array of financial services including mutual funds, securities and insurance brokerage, tax preparation and other services through CFS Group Inc., its wholly owned subsidiary

For additional information, including information concerning the results of operations of the Corporation and its subsidiaries, see Management's Discussion and Analysis of Financial Condition and Results of Operations in Part II, Item 7.

There were no material changes in the manner of doing business by the Corporation or its subsidiaries during the fiscal year ended December 31, 2013.

Market Area and Competition

The Bank operates 34 branch offices located in 11 counties in New York and Bradford County in Pennsylvania. Bank branch offices are located in the following New York counties: Chemung, where the Bank is headquartered, Broome, Cayuga, Cortland, Schuyler, Seneca, Steuben, Tioga and Tompkins. The Bank also operates under the name "Capital Bank, a division of Chemung Canal Trust Company", with branch offices located in Albany and Saratoga counties in New York.

Albany and Saratoga counties rely heavily on business related to New York State government activities, the nanotechnology industry and colleges located within these counties. Tompkins County is dominated by the presence of Cornell University and Ithaca College. The world headquarters of Corning Incorporated, the region's largest employer, is located in Steuben County. The remaining New York counties have a combination of service, small manufacturing and tourism related businesses, with colleges located in Broome, Chemung and Cortland counties.

Within all these market areas, the Bank encounters intense competition in the lending and deposit gathering aspects of its business from local, regional and national commercial banks and thrift institutions, credit unions and other providers of financial services, such as brokerage firms, investment companies, insurance companies and internet banking institutions. The Bank also competes with non-financial institutions, including retail stores and certain utilities that maintain their own credit programs, as well as governmental agencies that make loans to certain borrowers. Many of these competitors are not subject to regulation as extensive as that affecting the Bank and, as a result, may have a competitive advantage over the Bank in certain respects. This is particularly true of credit unions because their pricing structure is not encumbered by the payment of income taxes.

Similarly, the competition for the Bank's wealth management services is primarily from local offices of national brokerage firms, independent investment advisors, national and regional banks as well as internet based brokerage/advisory firms. The Bank operates full-service wealth management centers in Chemung and Broome counties in New York.

Employees

As of December 31, 2013, the Corporation and its subsidiaries employed 390 persons on a full-time equivalent basis. None of the Corporation's employees are covered by collective bargaining agreements, and the Corporation believes that its relationship with its employees is good.

Available Information

The SEC maintains a web site at www.sec.gov that contains reports, proxy and information statements, and other information regarding the Corporation. You may also read and copy materials we file with the SEC at the SEC's Public Reference Room at 100 F St., NE, Washington, D.C. 20549. You may obtain information concerning the operation of the Public Reference Room by calling 1-800-SEC-0330. In addition, we maintain a corporate web site at www.chemungcanal.com. We make available free of charge through our web site our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and any amendments to those reports filed with the SEC pursuant to Section 13(a) or 15(d) of the Exchange Act. These items are available as soon as reasonably practicable after we electronically file or furnish such material with the SEC. These items are also available on our web site as Interactive Data Files as required pursuant to Rule 405 of Regulation S-T (§232.405). The contents of our web site are not a part of this report. These materials are also available free of charge by written request to: Kathleen S. McKillip, Corporate Secretary, Chemung Canal Trust Company, One Chemung Canal Plaza, Elmira, NY 14901.

Supervision and Regulation

The Corporation and the Bank are subject to comprehensive regulation, supervision and examination by regulatory authorities. Numerous statutes and regulations apply to the Corporation's and, to a greater extent, the Bank's, operations, including required reserves, investments, loans, deposits, issuances of securities, payments of dividends and establishment of branches. Set forth below is a brief description of some of these laws and regulations. The description does not purport to be complete, and is qualified in its entirety by reference to the text of the applicable laws and regulations.

The Corporation

Bank Holding Company Act

The Corporation is a bank holding company registered with, and subject to regulation and examination by, the Board of Governors of the Federal Reserve System ("Federal Reserve") pursuant to the Bank Holding Company Act of 1956, as amended (the "BHCA"). The Federal Reserve regulates and requires the filing of reports describing the activities of bank holding companies, and conducts periodic examinations to test compliance with applicable regulatory requirements. The Federal Reserve has enforcement authority over bank holding companies, including, among other things, the ability to assess civil money penalties, to issue cease and desist or removal orders, and to require a bank holding company to divest subsidiaries.

The Corporation generally may engage in the activities permissible for a bank holding company, which includes banking, managing or controlling banks, performing certain servicing activities for subsidiaries, and engaging in other activities that the Federal Reserve has determined to be so closely related to banking as to be a proper incident thereto. Because the Corporation also has elected financial holding company status, it may also engage in a broader range of activities that are determined by the Federal Reserve and the Secretary of the Treasury to be financial in nature or incidental to financial activities or activities that are determined by the Federal Reserve to be complementary to a financial activity and that do not pose a substantial risk to the safety and soundness of depository institutions or the financial system generally.

The BHCA prohibits a bank holding company from acquiring direct or indirect ownership or control of more than 5% of the voting shares of any bank, or increasing such ownership or control of any bank, without the prior approval of the Federal Reserve.

New York Law

The Corporation is organized under New York law and is subject to the New York Business Corporation Law, which governs the rights and obligations of directors and shareholders and other corporate matters.

The Corporation is also a bank holding company as defined in the New York Banking Law by virtue of its ownership and control of the Bank. Generally, this means that the New York State Department of Financial Services ("NYSDFS") must approve the Corporation's acquisition of control of other banking institutions and similar transactions.

Federal Securities Law

The Corporation is subject to the information, reporting, proxy solicitation, insider trading, and other rules contained in the Securities Exchange Act of 1934 (the "Exchange Act"), the disclosure requirements of the Securities Act of 1933 (the "Securities Act") and the regulations of the SEC thereunder. In addition, the Corporation must comply with the corporate governance and listing standards of the NASDAQ Stock Market to maintain the listing of its common stock on the exchange. These standards include rules relating to a listed company's board of directors, audit committees and independent director oversight of executive compensation, the director nomination process, a code of conduct and shareholder meetings.

The SEC has adopted certain proxy disclosure rules regarding executive compensation and corporate governance, with which the Corporation must comply. They include: (i) increased disclosure as it relates to stock and option award compensation; (ii) disclosure regarding any potential conflict of interest of any compensation consultants of the Corporation; (iii) enhanced disclosure regarding compensation committee independence and experience, qualifications, skills and diversity of its directors and any director nominees; (iv) "say-on-pay" disclosure; and (v) information relating to the leadership structure of the Corporation's board of directors and the board's role in the risk management process. Additionally, these rules require the Corporation to report the voting results of annual meetings in a much more timely manner on Form 8-K, rather than on a quarterly or annual report.

Sarbanes-Oxley Act of 2002

The Corporation is also subject to the Sarbanes-Oxley Act of 2002 (the "Sarbanes-Oxley Act"). The Sarbanes-Oxley Act revised the laws affecting public companies' corporate governance, accounting obligations, and corporate reporting by: (i) creating a new federal accounting oversight body; (ii) revamping auditor independence rules; (iii) enacting new corporate responsibility and governance measures; (iv) enhancing disclosures by public companies, their directors, and their executive officers; (v) strengthening the powers and resources of the SEC; and (vi) imposing new criminal and civil penalties for securities fraud and related wrongful conduct.

The SEC has adopted regulations under the Sarbanes-Oxley Act, including: (i) executive compensation disclosure rules; (ii) standards of independence for directors who serve on the Corporation's audit committee; (iii) disclosure requirements as to whether at least one member of the Corporation's audit committee qualifies as a "financial expert" as defined in the SEC regulations; (iv) whether the Corporation has adopted a code of ethics applicable to its chief executive officer, chief financial officer, or those persons performing similar functions; (v) and disclosure requirements regarding the operations of board nominating committees and the means, if any, by which security holders may communicate with directors.

Support of Subsidiary Banks

The Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"), discussed in the section of this document entitled "Additional Important Legislation and Regulation", codifies the Federal Reserve's long-standing policy of requiring bank holding companies to act as a source of financial and managerial strength to their subsidiary banks, as a statutory requirement. Under this requirement, the Corporation is expected to commit resources to support its banking subsidiaries, including at times when it may not be advantageous for the Corporation to do so.

The Bank

General

The Bank is a commercial bank chartered under the laws of New York State and is supervised by the NYSDFS. The Bank also is a member bank of the Federal Reserve System and, therefore, the Federal Reserve serves as its primary federal regulator. The FDIC insures the Bank's deposit accounts up to applicable limits. The Bank must file reports with the Federal Financial Institution Examination Council ("FFIEC"), the Federal Reserve and the FDIC concerning its activities and financial condition and must obtain regulatory approval before commencing certain activities or engaging in transactions such as mergers and other business combinations or the establishment, closing, purchase or sale of branch offices. This regulatory structure gives the regulatory authorities extensive discretion in the enforcement of laws and regulations and the supervision of the Bank.

Loans to One Borrower

The Bank generally may not make a loan or extend credit to a single or related group of borrowers in excess of 15% of its unimpaired capital and surplus. Up to an additional 10% of unimpaired capital and surplus can be lent if the additional amount is fully secured by readily marketable collateral. At December 31, 2013, the Bank’s legal lending limit on loans to one borrower was $20.0 million for loans not fully secured by readily marketable collateral and $22.0 million for loans secured by readily marketable collateral. The Bank’s internal limit on loans is set at $15.0 million. At that date, the Bank did not have any loans or agreements to extend credit to a single or related group of borrowers in excess of its legal lending limit.

Branching

Subject to the approval of the NYSDFS, New York chartered commercial banks may establish branch offices anywhere within New York State, except in communities having populations of less than 50,000 inhabitants in which another New York chartered commercial bank or a national bank has its principal office. Additionally, under the Dodd-Frank Act, state chartered banks may generally branch into other states to the same extent as commercial banks chartered under the laws of that state may branch.

Payment of Dividends

The Bank is subject to substantial regulatory restrictions relating to its ability to pay dividends to the Corporation. Under Federal Reserve and NYSDFS regulations, the Bank may not pay a dividend without prior approval of the Federal Reserve and the NYSDFS if the total amount of all dividends declared during such calendar year, including the proposed dividend, exceeds the sum of its retained net income to date during the calendar year and its retained net income over the preceding two calendar years. As of December 31, 2013, approximately $8.5 million was available for the payment of dividends by the Bank to the Corporation without prior approval. The Bank's ability to pay dividends also is subject to the Bank being in compliance with regulatory capital requirements. The Bank is currently in compliance with these requirements.

Federal Reserve System

All depository institutions must maintain with a Federal Reserve Bank reserves against their transaction accounts (primarily checking, NOW, and Super NOW accounts) and nonpersonal time accounts. As of December 31, 2013, the Bank was in compliance with applicable reserve requirements. In all years preceding 2008, these reserves were maintained as vault cash or noninterest-bearing accounts, thereby reducing the Bank’s earnings potential. In the fourth quarter of 2008, the Federal Reserve Banks announced that they would begin to pay interest on member banks’ required reserve balances, as well as excess reserve balances.

Standards for Safety and Soundness

The Federal Reserve has adopted guidelines prescribing safety and soundness standards. These guidelines establish general standards relating to capital adequacy, asset quality, management, earnings performance, liquidity and sensitivity to market risk. In evaluating these safety and soundness standards, the Federal Reserve also evaluates internal controls and information systems, internal audit systems, loan documentation, credit underwriting, exposure to changes in interest rates, asset growth, compensation, fees, and benefits. In general, the guidelines require appropriate systems and practices to identify and manage the risks and exposures specified in the guidelines. The Federal Reserve may order an institution that has been given notice that it is not satisfying these safety and soundness standards to submit a compliance plan, and if an institution fails to do so, the Federal Reserve must issue an order directing action to correct the deficiency and may issue an order directing other action. If an institution fails to comply with such an order, the Federal Reserve may seek to enforce such order in judicial proceedings and to impose civil money penalties.

Real Estate Lending Standards

The Federal Reserve has adopted guidelines that generally require each Federal Reserve state member bank to establish and maintain written internal real estate lending standards that are consistent with safe and sound banking practices and appropriate to the size of the bank and the nature and scope of its real estate lending activities. The standards also must be consistent with accompanying Federal Reserve guidelines, which include loan-to-value ratios for the different types of real estate loans.

Transactions with Related Parties

The Federal Reserve Act governs transactions between the Bank and its affiliates, including the Corporation and CFS Group, Inc. In general, an affiliate of the Bank is any company that controls, is controlled by, or is under common control with the Bank. Generally, the Federal Reserve Act limits the extent to which the Bank or its subsidiaries may engage in “covered transactions” with any one affiliate to 10% of the Bank’s capital stock and surplus, and contains an aggregate limit of 20% of capital stock and surplus for covered transactions with all affiliates. Covered transactions include loans, asset purchases, the issuance of guarantees, and similar transactions. The Bank's loans to insiders must be made on terms that are substantially the same as, and follow credit underwriting procedures that are not less stringent than, those prevailing for comparable transactions with unaffiliated persons and that do not involve more than the normal risk of repayment or present other unfavorable features. The loans are also subject to maximum dollar limits and must generally be approved by the Board.

Deposit Insurance

The FDIC insures the deposits of the Bank up to regulatory limits and the deposits are subject to the deposit insurance premium assessments of the Deposit Insurance Fund ("DIF"). The FDIC currently maintains a risk-based assessment system under which assessment rates vary based on the level of risk posed by the institution to the DIF. The assessment rate may, therefore, change after any of these measurements change.

The FDIC has adopted a final rule making certain changes to the deposit insurance assessment system. Among other things, the rule revised the assessment rate schedule effective April 1, 2011, and adopted additional rate schedules that will go into effect when the DIF reserve ratio reaches various milestones. The rule changed the deposit insurance assessment system from one that was based on domestic deposits to one that is based on average consolidated total assets minus average tangible equity. In addition, the rule provides that FDIC dividend payments will be suspended if the DIF reserve ratio exceeds 1.5 percent but that assessment rates will decrease when the DIF reserve ratio reaches certain thresholds.

All institutions with deposits insured by the FDIC are required to pay assessments to fund interest payments on bonds issued by the Financing Corporation ("FICO"), an agency of the federal government established to recapitalize the predecessor to the Savings Association Insurance Fund. These assessments will continue until the FICO bonds mature in 2017. The FDIC's FICO assessment authority is separate from its authority to assess risk-based premiums for deposit insurance. The FICO assessment rate is adjusted quarterly to reflect changes in the assessment bases of the fund and is not risk-based by institution. The FICO assessment rate for the first quarter of 2014, due December 31, 2013, was .003875% of insured deposits.

Regulatory Capital Requirements

Current Federal Reserve regulations require state member banks to meet three minimum capital standards, which are:

- a minimum tangible capital ratio requirement of 1.5% of tangible capital to adjusted total assets;
- a general minimum leverage ratio requirement of 4.0% of core capital to adjusted total assets (minimum of 3.% for certain banks that have been assigned the highest composite rating under the Uniform Financial Institutions Ratings System); and
- a minimum risk-based capital ratio requirement of 8.0% of core and supplementary capital to total risk-weighted assets, provided that the amount of supplementary capital used to satisfy this requirement may not exceed 100% of core capital.

On October 11, 2013, the Federal Reserve approved a final rule that amends the regulatory capital rules for state member banks effective January 1, 2015. The Federal Reserve approved the new capital rules in coordination with substantially identical final rules approved by the FDIC and the Office of the Comptroller of the Currency for other types of banking organizations. The revisions make the capital rules consistent with agreements that were reached by the Basel Committee on Banking Supervision ("Basel III") and certain provisions of the Dodd-Frank Act. In general, the new capital rules revise regulatory capital definitions and minimum ratios; redefine Tier 1 Capital as two components (common equity tier 1 capital and additional tier 1 capital); create a new "common equity tier 1 risk-based capital ratio"; implement a capital conservation buffer; revise prompt corrective action thresholds; and change risk weights for certain assets and off-balance sheet exposures.

The new capital rules implement a revised definition of regulatory capital, a new common equity Tier 1 minimum capital requirement of 4.5%, and a higher minimum Tier 1 capital requirement of 6.0% (which is an increase from 4.0%). Under the new rules, the total capital ratio remains at 8.0%, and the minimum leverage ratio (Tier 1 capital to total assets) for all banking organizations, regardless of supervisory rating, is 4.0%. Additionally, under the new capital rules, in order to avoid limitations on capital distributions, including dividend payments and certain discretionary bonus payments to executive officers, a banking organization must hold a capital conservation buffer composed of common equity Tier 1 capital above its minimum risk-based capital requirements. The buffer is measured relative to risk-weighted assets. The final rules also enhance risk sensitivity and address weaknesses identified by the regulators over recent years with the measure of risk-weighted assets, including through new measures of creditworthiness to replace references to credit ratings, consistent with the requirements of the Dodd-Frank Act.

The new capital requirements also include changes in the risk-weights of assets to better reflect credit risk and other risk exposures. These include a 150% risk weight (up from 100%) for certain high volatility commercial real estate acquisition, development and construction loans and the unsecured portion of non-residential mortgage loans that are 90 days past due or otherwise on nonaccrual status; a 20% (up from 0%) credit conversion factor for the unused portion of a commitment with an original maturity of one year or less that is not unconditionally cancellable; a 250% risk weight (up from 100%) for mortgage servicing rights and deferred tax assets that are not deducted from capital; and increased risk weights (from 0% to up to 600%) for equity exposures.

The new minimum capital requirements generally become effective for all banking organizations (except for the largest internationally active banking organizations) on January 1, 2015, whereas the capital conservation buffer and the deductions from common equity Tier 1 capital phase in over time, beginning on January 1, 2016.

The Corporation is subject to Federal Reserve capital requirements applicable to bank holding companies, which are similar to those applicable to the Bank.

In assessing a state member bank's capital adequacy, the Federal Reserve takes into consideration not only these numeric factors but also qualitative factors, and has the authority to establish higher capital requirements for individual banks where necessary. The Bank, in accordance with its internal prudential standards, targets as its goal the maintenance of capital ratios which exceed these minimum requirements and that are consistent with its risk profile.

Prompt Corrective Action

The Federal Deposit Insurance Act (the "FDIA") requires the federal banking agencies to resolve the problems of insured banks at the least possible loss to the DIF. The Federal Reserve has adopted prompt corrective action regulations to carry out this statutory mandate. The Federal Reserve's regulations authorize, and in some situations, require, the Federal Reserve to take certain supervisory actions against undercapitalized state member banks, including the imposition of restrictions on asset growth and other forms of expansion. The prompt corrective action regulations place state member banks in one of the following five categories based, on the bank's capital:

- well capitalized
- adequately capitalized
- undercapitalized
- significantly undercapitalized
- critically undercapitalized

The new capital rules described above under "Regulatory Capital Requirements" maintain the general structure of the current prompt corrective action framework while increasing some of the thresholds for the prompt corrective action capital categories. For example, an adequately capitalized bank is required to maintain a tier 1 risk-based capital ratio of 6.0% (increased from the current level of 4.0%). The rule also introduces the common equity tier 1 capital ratio as a new prompt corrective action capital category threshold.

As an institution's capital decreases within the three undercapitalized categories listed above, the severity of the action that is authorized or required to be taken by the Federal Reserve for state member banks under the prompt corrective action regulations increases. All banks are prohibited from paying dividends or other capital distributions or paying management fees to any controlling person if, following such distribution, the bank would be undercapitalized. The Federal Reserve is required to monitor closely the condition of an undercapitalized institution and to restrict the growth of its assets.

An undercapitalized state member bank is required to file a capital restoration plan with the Federal Reserve within 45 days (or other timeframe prescribed by the Federal Reserve) of the date the bank receives notice that it is within any of the three undercapitalized categories, and the plan must be guaranteed by its parent holding company, subject to a cap on the guarantee that is the lesser of: (i) an amount equal to 5.0% of the bank's total assets at the time it was notified that it became undercapitalized; and (ii) the amount that is necessary to restore the bank's capital ratios to the levels required to be classified as "adequately classified," as those ratios and levels are defined as of the time the bank failed to comply with the plan. If the bank fails to submit an acceptable plan, it is treated as if it were "significantly undercapitalized." Banks that are significantly or critically undercapitalized are subject to a wider range of regulatory requirements and restrictions.

Federal Home Loan Bank

The Bank is also a member of the FHLBNY, which provides a central credit facility primarily for member institutions for home mortgage and neighborhood lending. The Bank is subject to the rules and requirements of the FHLBNY, including the requirement to acquire and hold shares of capital stock in the FHLBNY. The Bank was in compliance with the rules and requirements of the FHLBNY at December 31, 2013.

Community Reinvestment Act

Under the federal Community Reinvestment Act (the "CRA"), the Bank, consistent with its safe and sound operation, must help meet the credit needs of its entire community, including low and moderate income neighborhoods. The Federal Reserve periodically assesses the Bank's compliance with CRA requirements. The Bank received an "outstanding" rating for CRA on its last performance evaluation conducted by the Federal Reserve as of May 29, 2012.

Fair Lending and Consumer Protection Laws

The Bank must also comply with the federal Equal Credit Opportunity Act and the New York Executive Law, which prohibit creditors from discrimination in their lending practices on bases specified in these statutes. In addition, the Bank is subject to a number of federal statutes and regulations implementing them, which are designed to protect the general public, borrowers, depositors, and other customers of depository institutions. These include the Bank Secrecy Act, the Truth in Lending Act, the Home Ownership and Equity Protection Act, the Truth in Savings Act, the Home Mortgage Disclosure Act, the Fair Housing Act, the Real Estate Settlement Procedures Act, the Electronic Funds Transfers Act, the Fair Credit Reporting Act, the Right to Financial Privacy Act, the Expedited Funds Availability Act, the Flood Disaster Protection Act, the Fair Debt Collection Practices Act, Helping Families Save Their Homes Act, and the Consumer Protection for Depository Institutions Sales of Insurance regulation. The Federal Reserve and, in some instances, other regulators, including the U.S. Department of Justice, the Federal Trade Commission ("FTC"), the Consumer Financial Protection Bureau ("CFPB") and state Attorneys General, may take enforcement action against institutions that fail to comply with these laws.

Prohibitions Against Tying Arrangements

Subject to some exceptions, the BHCA and Federal Reserve regulations prohibit banks from extending credit to or offering any other service, or fixing or varying the consideration for such extension of credit or service, on the condition that the customer obtain some additional service from the bank or its affiliates or not obtain services of a competitor of the bank.

Privacy Regulations

Federal Reserve regulations generally require the Bank to disclose its privacy policy. The policy must identify with whom the Bank shares its customers' "nonpublic personal information," at the time of establishing the customer relationship and annually thereafter. In addition, the Bank must provide its customers with the ability to "opt out" of having their personal information shared with unaffiliated third parties and not to disclose account numbers or access codes to non-affiliated third parties for marketing purposes. The Bank's privacy policy complies with Federal Reserve regulations.

The USA PATRIOT Act

The Bank is subject to the USA PATRIOT Act, which gives the federal government powers to address terrorist threats through enhanced domestic security measures, expanded surveillance powers, increased information sharing, and broadened anti-money laundering requirements. The USA PATRIOT Act imposes affirmative obligations on financial institutions, including the Bank, to establish anti-money laundering programs which require: (i) the establishment of internal policies, procedures, and controls; (ii) the designation of an anti-money laundering compliance officer; (iii) ongoing employee training programs; and (iv) an independent audit function to test the anti-money laundering program. The Federal Reserve must consider the Bank's effectiveness in combating money laundering when ruling on merger and other applications.

CFS Group, Inc.

CFS Group, Inc. is subject to supervision by other regulatory authorities as determined by the activities in which it is engaged. Insurance activities are supervised by the NYSDFS, and brokerage activities are subject to supervision by the SEC and the Financial Industry Regulatory Authority ("FINRA").

Additional Important Legislation and Regulation

The Dodd-Frank Act

The Dodd-Frank Act, enacted on July 21, 2010, significantly changed the bank regulatory landscape and has impacted and will continue to impact the lending, deposit, investment, trading and operating activities of financial institutions and their holding companies. The Dodd-Frank Act requires various federal agencies to adopt a broad range of new rules and regulations, and to prepare various studies and reports for Congress. We have summarized below significant rules adopted by the federal agencies pursuant to the Dodd-Frank Act.

The Dodd-Frank Act created the Consumer Financial Protection Bureau (“CFPB”), with wide-ranging powers to supervise and enforce consumer protection laws. The CFPB has broad rule-making authority for a wide range of consumer protection laws that apply to all banks and savings institutions, including the authority to prohibit "unfair, deceptive or abusive" acts and practices. The CFPB has examination and enforcement authority over all banks and savings institutions with more than $10 billion in assets. The Dodd-Frank Act also weakened the federal preemption rules that have been applicable to national banks and federal savings associations, and gives state attorneys general certain powers to enforce federal consumer protection regulations.

Consumer Financial Protection Bureau Rules

In 2013, the CFPB issued several new rules pursuant to the Dodd-Frank Act concerning the regulation of mortgage markets in the U.S. The rules amend several existing regulations, including Regulation Z, which implements the Truth in Lending Act, Regulation X, which implements the Real Estate Settlement Procedures Act and Regulation B, which implements the Equal Credit Opportunity Act.

The amendments to Regulation Z:

- Lengthen the time for which a mandatory escrow account established for a higher-priced mortgage loan must be maintained. This rule, which is subject to a number of transactional exceptions, such as mortgage transactions extended by creditors that operate predominantly in rural or underserved areas, became effective on June 1, 2013.

- Require creditors to make a reasonable, good faith determination of a consumer’s ability to repay any consumer credit transaction secured by a dwelling (excluding an open-end credit plan, timeshare plan, reverse mortgage, or temporary loan) and establish certain protections from liability under this requirement for “qualified mortgages.” The amendments also limit prepayment penalties. This rule became effective on January 10, 2014.

- Expand the types of mortgage loans that are subject to the protections of the Home Ownership and Equity Protections Act of 1994 (“HOEPA”), revise and expand the tests for coverage under HOEPA, and impose additional restrictions on mortgages that are covered by HOEPA, including a pre-loan counseling requirement. The final rule also amends Regulation Z and Regulation X by imposing certain other requirements related to homeownership counseling, including a requirement that consumers receive information about homeownership counseling providers. This rule became effective on January 10, 2014.

- Require creditors to obtain a full interior appraisal by a certified or licensed appraiser for non-exempt "higher-risk mortgage loans", which are mortgages with an annual percentage rates that exceeds the average prime offer rate by a specified percentage. The rule also requires a second such appraisal at the creditor's expense for certain properties held for less than 180 days. Exemptions include qualified mortgages, reverse mortgages, bridge loans, construction loans and certain manufactured homes. In addition, the rule requires creditors to provide the consumer a copy of all written appraisals performed in connection with the mortgage at least 3 days prior to closing. This rule became effective on January18, 2014.

- Regulate mortgage broker and other loan originator compensation by: i) prohibiting dual compensation (payment by both the lender and the borrower) and compensation arrangements that incentivize the originator to steer the borrower to more expensive loan products (by basing the compensation on the interest rate or other term of a transaction); ii) establishing tests for when loan originators can be compensated through certain profits-based compensation arrangements; and iii) prohibiting mandatory arbitration clauses in disputes concerning residential mortgage loans and home equity lines of credit. This rule became effective on January 10, 2014, except for the mandatory arbitration prohibition, which went into effect on June 1, 2013.

- Address initial rate adjustment notices for adjustable-rate mortgages, periodic statements for residential mortgage loans, prompt crediting of mortgage payments, and responses to requests for payoff amounts and the scope, timing, content, and format of disclosures to consumers regarding the interest rate adjustments of their variable-rate transactions. This rule became effective on January 10, 2014.

The Regulation X amendments address loan servicers' obligations to: i) correct errors asserted by mortgage loan borrowers; ii) provide certain information requested by borrowers; iii) provide protections to borrowers in connection with force-placed insurance iv) establish reasonable policies and procedures to achieve certain delineated objectives; v) provide information about mortgage loss mitigation options to delinquent borrowers; vi) establish policies and procedures for providing delinquent borrowers with continuity of contact with servicer personnel; and vii) evaluate borrowers' applications for available loss mitigation options. This rule became effective on January 10, 2014.

The amendments to Regulation B require creditors to provide to applicants free copies of all appraisals and other written valuations developed in connection with an application for a loan to be secured by a first lien on a dwelling, and require creditors to notify applicants in writing that copies of appraisals will be provided to them promptly. This rule became effective on January 18, 2014.

In December 2013, the Federal Reserve and the SEC released final rules to implement the provisions of the Dodd-Frank Act, commonly known as the "Volcker Rule." The Volcker Rule, among other things, prohibits banking entities from engaging in proprietary trading and from sponsoring, having an ownership interest in or having certain relationships with a hedge fund or private equity fund, subject to certain exemptions. At December 31, 2013, we were not engaged in any activities and we did not have any ownership interests in any funds that are not permitted under the Volcker Rule.

Securities and Exchange Commission Rules

As discussed above under “Federal Securities Law”, pursuant to the Dodd-Frank Act, the SEC has issued regulations that provide the shareholders of public companies with an advisory vote on: i) executive compensation ("say-on-pay" votes); ii) the desired frequency of say-on-pay votes; and iii) compensation arrangements and understandings in connection with merger transactions, known as "golden parachute" arrangements. The SEC has also adopted corporate governance regulations that provide to shareholders of companies subject to the SEC’s proxy rules: i) the opportunity to nominate directors at a shareholder meeting and to have their nominees included in the company proxy materials sent to all shareholders; and ii) the ability to use the shareholder proposal process to establish procedures for the inclusion of shareholder director nominations in company proxy materials.

Banking Agency Rules

As discussed above under “Regulatory Capital Requirements”, pursuant to the Dodd-Frank Act, the Federal Reserve and the other federal banking agencies have established minimum leverage and risk-based capital requirements for insured depository institutions and bank holding companies.

The Dodd-Frank Act also broadened the base for FDIC insurance assessments. Assessments are now based on the average consolidated total assets less tangible equity capital of a financial institution. The Dodd-Frank Act also permanently increases the maximum amount of deposit insurance for banks, savings institutions and credit unions to $250,000 per depositor per insured institution, retroactive to January 1, 2008.

The Dodd-Frank Act directs the federal banking regulators to promulgate rules requiring the reporting of incentive-based compensation and prohibiting excessive incentive-based compensation paid to executives of depository institutions and their holding companies with assets in excess of $1.0 billion. In April 2011, the Federal Reserve, along with other federal banking supervisors, issued a joint notice of proposed rulemaking implementing those requirements.

Many other provisions of the Dodd-Frank Act still require extensive rulemaking, guidance and interpretation by regulatory agencies. Accordingly, in many respects, the ultimate impact of the legislation and its effects on the Corporation and the Bank remain uncertain. We are continuing to closely monitor and evaluate regulatory developments. Such developments could adversely affect our financial condition and results of operations through significant increases in our regulatory compliance costs.

Gramm-Leach-Bliley Act

Under the privacy and data security provisions of the Financial Modernization Act of 1999, also known as the Gramm-Leach-Bliley Act ("GLB Act"), and rules promulgated thereunder, all financial institutions, including the Corporation, the Bank and CFS Group, Inc., are required to establish policies and procedures to restrict the sharing of nonpublic customer data with nonaffiliated parties at the customer's request and to protect customer data from unauthorized access. In addition, the Fair Credit Reporting Act ("FCRA"), as amended by the Fair and Accurate Credit Transactions Act of 2003 ("FACT Act"), includes many provisions affecting the Corporation, Bank, and/or CFS Group, Inc., including provisions concerning obtaining consumer reports, furnishing information to consumer reporting agencies, maintaining a program to prevent identity theft, sharing of certain information among affiliated companies, and other provisions. For instance, FCRA requires persons subject to FCRA to notify their customers if they report negative information about them to a credit bureau or if they are granted credit on terms less favorable than those generally available. The Federal Reserve and the FTC have extensive rulemaking authority under the FACT Act, and the Corporation and the Bank are subject to the rules that have been promulgated by the Federal Reserve and

FTC thereunder, including recent rules regarding limitations on affiliate marketing and implementation of programs to identify, detect and mitigate the risk of identity theft through red flags. The Corporation has developed policies and procedures for itself and its subsidiaries to maintain compliance and believes it is in compliance with all privacy, information sharing and notification provisions of the GLB Act and FCRA.

The GLB Act and FCRA also impose requirements regarding data security and the safeguarding of customer information. The Bank is subject to the Interagency Guidelines Establishing Information Security Standards ("Security Guidelines"), which implement section 501(b) of the GLB Act and section 216 of the FACT Act. The Security Guidelines establish standards relating to administrative, technical, and physical safeguards to ensure the security, confidentiality, integrity and the proper disposal of customer information. The Bank believes it is in compliance with all such standards.

ITEM 1A. RISK FACTORS

The Corporation's business is subject to many risks and uncertainties. Although the Corporation seeks ways to manage these risks and develop programs to control those that management can, the Corporation ultimately cannot predict the extent to which these risks and uncertainties could affect our results. Actual results may differ materially from management's expectations. The material risks and uncertainties that management believes affect the Corporation are discussed below. You should consider all of the following risks together with all of the other information in this Annual Report on Form 10-K.

Economic conditions may adversely affect the Corporation's financial performance.

As a consequence of the economic slowdown that the United States experienced, business activity across a wide range of industries continues to face serious difficulties due to reduced consumer spending, the weakened financial condition of some borrowers and employment levels. A continued weakness or further weakening in business and economic conditions generally or specifically in the principal markets in which the Corporation does business could have one or more of the following adverse effects on the Corporation's business: (i) a decrease in the demand for loans and other products and services; (ii) a decrease in the value of the Corporation's loans or other assets secured by consumer or commercial real estate; (iii) an impairment of certain of the Corporation's intangible assets, such as goodwill; and (iv) an increase in the number of borrowers and counterparties who become delinquent, file for protection under bankruptcy laws or default on their loans or other obligations to the Corporation. Additionally, in light of economic conditions, the Corporation's ability to assess the creditworthiness of its customers may be impaired if the models and approaches that it uses to select, manage and underwrite loans become less predictive of future behaviors. Further, competition in the Corporation's industry may intensify as a result of consolidation of financial services companies in response to current market conditions and the Corporation may face increased regulatory scrutiny, which may increase its costs and limit its ability to pursue business opportunities.

Commercial real estate and business loans increase the Corporation's exposure to credit risks.

At December 31, 2013, the Corporation's portfolio of commercial real estate and business loans totaled $519 million or 52.1% of total loans. The Corporation's plans are to continue to emphasize the origination of these types of loans, which generally expose the Corporation to a greater risk of nonpayment and loss than residential real estate or consumer loans because repayment of commercial real estate and business loans often depends on the successful operations and income stream of the borrower's business. Additionally, such loans typically involve larger loan balances to single borrowers or groups of related borrowers compared to residential real estate and consumer loans. Also, some of the Corporation's borrowers have more than one commercial loan outstanding. Consequently, an adverse development with respect to one loan or one credit relationship can expose the Corporation to a significantly greater risk of loss compared to an adverse development with respect to residential real estate and consumer loans. The Corporation targets its business lending and marketing strategy towards small to medium-sized businesses. These small to medium-sized businesses generally have fewer financial resources in terms of capital or borrowing capacity than larger entities. If general economic conditions negatively impact these businesses, the Corporation's results of operations and financial condition may be adversely affected.

Increases to the allowance for loan losses may cause the Corporation's earnings to decrease.

The Corporation's customers may not repay their loans according to the original terms, and the collateral securing the payment of those loans may be insufficient to pay any remaining loan balance. Hence, we may experience significant loan losses, which could have a material adverse effect on our operating results. Management makes various assumptions and judgments about the collectability of its loan portfolio, including the creditworthiness of its borrowers and the value of the real estate and other assets serving as collateral for the repayment of loans. In determining the amount of the allowance for loan losses, management relies on loan quality reviews, past loss experience, and an evaluation of economic conditions, among other factors. If these assumptions prove to be incorrect, the allowance for loan losses may not be sufficient to cover losses inherent in the Corporation's loan portfolio, resulting in additions to the allowance. Material additions to the allowance would materially decrease net income.

The Corporation's emphasis on the origination of commercial loans is one of the more significant factors in evaluating its allowance for loan losses. As the Corporation continues to increase the amount of these loans, additional or increased provisions for loan losses may be necessary, which could result in a decrease in earnings.

Bank regulators periodically review the Corporation's allowance for loan losses and may require the Corporation to increase its provision for loan losses or loan charge-offs. Any increase in the allowance for loan losses or loan charge-offs as required by these regulatory authorities could have a material adverse effect on our results of operations and/or financial condition.

Changes in interest rates could adversely affect the Corporation's results of operations and financial condition.

The Corporation's results of operations and financial condition are significantly affected by changes in interest rates. Our financial results depend substantially on net interest income, which is the difference between the interest income that we earn on interest-earning assets and the interest expense paid on interest-bearing liabilities. If the Corporation's interest-earning assets mature or reprice more quickly than its interest-bearing liabilities in a given period as a result of decreasing interest rates, net interest income may decrease. Likewise, net interest income may decrease if interest-bearing liabilities mature or reprice more quickly than interest-earning assets in a given period as a result of increasing interest rates. The Corporation has taken steps to mitigate this risk, such as holding fewer longer-term residential mortgages, as well as investing excess funds in shorter-term investments.

Changes in interest rates also affect the fair value of the Corporation's interest-earning assets and, in particular, its investment securities available for sale. Generally, the fair value of investment securities fluctuates inversely with changes in interest rates. Decreases in the fair value of investment securities available for sale, therefore, could have an adverse effect on our shareholders' equity or earnings if the decrease in fair value is deemed to be other than temporary.

Changes in interest rates may also affect the average life of loans and mortgage-related securities. Decreases in interest rates can result in increased prepayments of loans and mortgage-related securities, as borrowers refinance to reduce borrowing costs. Under these circumstances, the Corporation is subject to reinvestment risk to the extent that it is unable to reinvest the cash received from such prepayments at rates that are comparable to the rates on its existing loans and securities. Additionally, increases in interest rates may decrease loan demand and make it more difficult for borrowers to repay adjustable rate loans.

Strong competition within our industry and market area could limit the Corporation’s growth and profitability.

The Corporation faces substantial competition in all phases of its operations from a variety of different competitors. Future growth and success will depend on the ability to compete effectively in this highly competitive environment. The Corporation competes for deposits, loans and other financial services with a variety of banks, thrifts, credit unions and other financial institutions as well as other entities, which provide financial services. Some of the financial institutions and financial services organizations with which we compete are not subject to the same degree of regulation as the Corporation. Many competitors have been in business for many years, have established customer bases, are larger, and have substantially higher lending limits. The financial services industry is also likely to become more competitive as further technological advances enable more companies to provide financial services. These technological advances may diminish the importance of depository institutions and other financial intermediaries in the transfer of funds between parties.

The Corporation’s growth strategy may not prove to be successful and our market value and profitability may suffer.

As part of the Corporation's strategy for continued growth, we may open additional branches. New branches do not initially contribute to operating profits due to the impact of overhead expenses and the start-up phase of generating loans and deposits. To the extent that additional branches are opened, the Corporation may experience the effects of higher operating expenses relative to operating income from the new operations, which may have an adverse effect on the Corporation's levels of net income, return on average equity and return on average assets.

In addition, the Corporation may acquire banks and related businesses that it believes provide a strategic fit with its business, such as the 2011 acquisition of Fort Orange Financial Corp (“FOFC”) and the 2013 acquisition of six branches of Bank of America. To the extent that the Corporation grows through acquisitions, it cannot provide assurance that such strategic decisions will be accretive to earnings.

Compliance with the Dodd-Frank Act may increase the Corporation’s costs of operations and adversely affect the Corporation’s earnings and financial condition.

The Dodd-Frank Act represents a significant overhaul of the CFPB as many aspects of the regulation of the financial-services industry. Among other things, the Dodd-Frank Act creates a new federal financial consumer protection agency, tightens capital standards, imposes clearing and margining requirements on many derivatives activities, and generally increases oversight and regulation of financial institutions and financial activities.

In addition to the self-implementing provisions of the statute, the Dodd-Frank Act calls for many administrative rulemakings by various federal agencies to implement various parts of the legislation. While regulators have adopted a number of new rules required by the Dodd-Frank Act, others have not been proposed or if proposed, not been adopted in final form. The Corporation cannot be certain when final rules affecting it will be issued through such rulemakings, and what the specific content of such rules will be. The financial reform legislation and any implementing rules that are ultimately issued could have adverse implications on the financial industry, the competitive environment, and the Corporation’s ability to conduct business. The Corporation will have to apply resources to ensure that it is in compliance with all applicable provisions of the Dodd-Frank Act and any implementing rules, which may increase the Corporation’s costs of operations and adversely impact its earnings.

The Corporation operates in a highly regulated environment and may be adversely affected by changes in laws and regulations.

Currently, the Corporation and its subsidiaries are subject to extensive regulation, supervision, and examination by regulatory authorities. For example, the Federal Reserve regulates the Corporation and the Federal Reserve, the FDIC and the NYSDFS regulate the Bank. Such regulators govern the activities in which the Corporation and its subsidiaries may engage. These regulatory authorities have extensive discretion in connection with their supervisory and enforcement activities, including the imposition of restrictions on the operation of a bank, the classification of assets by a bank, and the adequacy of a bank's allowance for loan losses. Any change in such regulation and oversight, whether in the form of regulatory policy, regulations, or legislation, could have a material impact on the Corporation and its operations. The Corporation believes that it is in substantial compliance with applicable federal, state and local laws, rules and regulations. Because our business is highly regulated, the laws, rules and applicable regulations are subject to regular modification and change. There can be no assurance that proposed laws, rules and regulations, or any other law, rule or regulation, will not be adopted in the future, which could make compliance more difficult or expensive or otherwise adversely affect our business, financial condition or prospects.

The impending capital requirement changes from Basel III discussed in Item 1-"Business-Supervision and Regulation", could have a material adverse impact on the Corporation. Even though the Bank exceeds current and proposed minimum regulatory capital levels, adverse changes to residential mortgage risk weights, new requirements for common equity capital, inclusion of accumulated other comprehensive income in regulatory capital, the phase out of trust preferred securities, along with the adoption of new capital conservation buffers would reduce the Bank's current capital position and over time could cause the Bank to fail to meet minimum regulatory requirements. These positions are subject to volatility due to changes in interest rates and credit spreads. The current positive balance is a product of the continued ultra low interest rate environment, which could change in the future. Rapid increases in interest rates and credit spreads could reverse the gain position and force the Corporation's accumulated other comprehensive income to become negative and have an adverse impact on the Bank's regulatory capital. Although there is a phase-in period in the proposed rules, other factors such as the ultra-low interest rate environment, fragile economic recovery, possible recession, and further constraints on profitability by regulators could impact the Bank's ability to meet the new regulatory minimums once the phase-in periods have ended.

The Corporation is a holding company and depends on its subsidiaries for dividends, distributions and other payments.

The Corporation is a legal entity separate and distinct from the Bank and other subsidiaries. Its principal source of cash flow, including cash flow to pay dividends to its shareholders, is dividends from the Bank. There are statutory and regulatory limitations on the payment of dividends by the Bank to the Corporation, as well as by the Corporation to its shareholders. Federal Reserve regulations affect the ability of the Bank to pay dividends and other distributions and to make loans to the Corporation. If the Bank is unable to make dividend payments to the Corporation and sufficient capital is not otherwise available, we may not be able to make dividend payments to our common shareholders.

The Corporation holds certain intangible assets that could be classified as impaired in the future. If these assets are considered to be either partially or fully impaired in the future, our earnings and the book values of these assets would decrease.

The Corporation is required to test its goodwill and core deposit intangible assets for impairment on a periodic basis. The impairment testing process considers a variety of factors, including the current market price of its common stock, the estimated net present value of its assets and liabilities, and information concerning the terminal valuation of similarly situated insured depository institutions. If an impairment determination is made in a future reporting period, our earnings and the book value of these intangible assets would be reduced by the amount of the impairment. If an impairment loss is recorded, it will have little or no impact on the tangible book value of our common shares or our regulatory capital levels, but such an impairment loss could significantly restrict the Bank from paying a dividend to the Corporation.

We may not be able to attract and retain skilled people.

Our success depends, in large part, on our ability to attract and retain key people. Competition for the best people in most activities in which we engage can be intense and we may not be able to hire people or to retain them. The unexpected loss of services of one or more of our key personnel could have a material adverse impact on the business because we would lose the employees' skills, knowledge of the market, and years of industry experience and may have difficulty promptly finding qualified replacement personnel.

Our controls and procedures may fail or be circumvented, which may result in a material adverse effect on our business.

Management regularly reviews and updates our internal controls, disclosure controls and procedures, and corporate governance policies and procedures. Any system of controls, however well designed and operated, is based in part on certain assumptions and can provide only reasonable, not absolute, assurances that the objectives of the system are met. Under rules of the SEC promulgated under Section 404 of the Sarbanes-Oxley Act of 2002, we were required to furnish a report by our management on our internal controls over financial reporting in our Form 10-K for the fiscal year ended December 31, 2013. In the course of our assessment of the effectiveness of our internal controls over financial reporting as of December 31, 2013 in connection with the preparation of the 2013 audited financial statements and our annual report on Form 10-K for 2013, we identified a material weakness in our internal controls over financial reporting related to the identification and evaluation of troubled debt restructurings as of December 31, 2013. The material weakness did not result in a misstatement in the Corporation's quarterly or annual financial statements for 2013. However, as a result of the material weakness, management has concluded that the Corporation did not maintain effective internal controls over financial reporting as of December 31, 2013.

Our independent registered public accounting firm also identified a material weakness in our internal controls over financial reporting as stated in its Audit Report citing a deficiency noted above. We have begun the process of remediating the deficiency noted above. The material weakness in our internal controls over financial reporting, as described in Item 9A, "Controls and Procedures" and in the Audit Report, of our Annual Report on Form 10-K for the year ended December 31, 2013, as well as any other weakness or deficiencies that may exist or hereafter arise or be identified, could harm our business and operating results, and could result in adverse publicity and a loss in investor confidence in the accuracy and completeness of our financial reports, which in turn could have a material adverse effect on our stock price. If the weakness is not properly remediated, it could adversely affect our ability to report our financial results on a timely and accurate basis.

The Corporation continually encounters technological change and the failure to understand and adapt to these changes could adversely affect our business.

The banking industry is undergoing rapid technological changes with frequent introductions of new technology-driven products and services. The Corporation's future success will depend, in part, on the ability to address the needs of customers by using technology to provide products and services that will satisfy customer demands for convenience as well as to create additional efficiencies in operations. Many competitors have substantially greater resources to invest in technological improvements. There can be no assurance that the Corporation will be able to effectively implement new technology-driven products and services or be successful in marketing such products and services to customers. Failure to successfully keep pace with technological change affecting the financial services industry could have a material adverse impact on our business and, in turn, our financial condition and results of operations.

The Corporation is subject to security and operational risks relating to its use of technology.

Despite instituted safeguards, the Corporation cannot be certain that all of its systems are entirely free from vulnerability to attack or other technological difficulties or failures. The Corporation relies on the services of a variety of vendors to meet its data processing and communication needs. If information security is breached or other technology difficulties or failures occur, information may be lost or misappropriated, services and operations may be interrupted and the Corporation could be exposed to claims from customers. Any of these results could have a material adverse effect on the Corporation's business, financial condition, results of operations or liquidity.

Provisions of our certificate of incorporation, bylaws, as well as New York law and certain banking laws, could delay or prevent a takeover of us by a third party.

Provisions of the Corporation’s certificate of incorporation and bylaws, New York law, and state and federal banking laws, including regulatory approval requirements, could delay, defer or prevent a third party from acquiring the Corporation, despite the possible benefit to the Corporation’s shareholders, or otherwise adversely affect the market price of the Corporation’s common stock. These provisions include: a two-thirds affirmative vote of all outstanding shares of Corporation stock for certain business combinations; a supermajority shareholder vote of 75% of outstanding stock for business combinations involving 10% shareholders; the election of directors to staggered terms of three years; and advance notice requirements for nominations for election to the Corporation’s board of directors and for proposing matters that shareholders may act on at a shareholder meeting. In addition, the Corporation is subject to New York law, which among other things prohibits the Corporation from engaging in a business combination with any interested stockholder for a period of five years from the date the person became an interested stockholder unless certain conditions are met. These provisions may discourage potential takeover attempts, discouraging bids for the Corporation’s common stock at a premium over market price or adversely affect the market price of, and the voting and other rights of the holders of the Corporation’s common stock. These provisions could also discourage proxy contests and make it more difficult for shareholders to elect directors other than candidates nominated by the Board.

The risks presented by acquisitions could adversely affect our financial condition and results of operations.

The business strategy of the Corporation has included and may continue to include growth through acquisition from time to time. Any future acquisitions will be accompanied by the risks commonly encountered in acquisitions. These risks may include, among other things: our ability to realize anticipated cost savings, the difficulty of integrating operations and personnel, the loss of key employees, the potential disruption of our or the acquired company’s ongoing business in such a way that could result in decreased revenues, the inability of our management to maximize our financial and strategic position, the inability to maintain uniform standards, controls, procedures and policies, and the impairment of relationships with the acquired company’s employees and customers as a result of changes in ownership and management.

Severe weather and other natural disasters can affect the Corporation's business.

Our main office and our branch offices can be affected by natural disasters such as severe storms and flooding. These kinds of events could interrupt our operations, particularly our ability to deliver deposit and other retail banking services to our customers and as a result, our business could suffer serious harm. While we maintain adequate insurance against property and casualty losses arising from most natural disasters, and we have successfully overcome the challenges caused by past flooding in Central New York, there can be no assurance that we will be as successful if and when disasters occur.

Our accounting policies and estimates are critical to how we report our financial condition and results of operations, and any changes to such accounting policies and estimates could materially affect how we report our financial condition and results of operations.

Management has identified certain accounting policies as being critical because they require management's judgment to ascertain the valuations of assets, liabilities, commitments and contingencies. A variety of factors could affect the ultimate value that is obtained either when earning income, recognizing an expense, recovering an asset, valuing an asset or liability or reducing a liability. We have established detailed policies and control procedures that are intended to ensure that these critical accounting estimates and judgments are well controlled and applied consistently. In addition, these policies and procedures are intended to ensure that the process for changing methodologies occurs in an appropriate manner. Because of the uncertainty surrounding our judgments and the estimates pertaining to these matters, actual outcomes may be materially different from amounts previously estimated. For example, because of the inherent uncertainty of estimates, management cannot provide any assurance that the Bank will not significantly increase its allowance for loan losses if actual losses are more than the amount reserved. Any increase in its allowance for loan losses or loan charge-offs could have a material adverse effect on our financial condition and results of operations. In addition, we cannot guarantee that we will not be required to adjust accounting policies or restate prior financial statements.

Further, from time to time, the Financial Accounting Standards Board and SEC change the financial accounting and reporting standards that govern the preparation of our financial statements. The ongoing economic recession has resulted in increased scrutiny of accounting standards by legislators and our regulators, particularly as they relate to fair value accounting principles. In addition, ongoing efforts to achieve convergence between GAAP and International Financial Reporting Standards may result in changes to GAAP. These changes can be hard to predict and can materially impact how we record and report our financial condition and results of operations. In some cases, we could be required to apply a new or revised standard retroactively, resulting in our restating prior period financial statements or otherwise adversely affecting our financial condition or results of operations.

There may be claims and litigation pertaining to fiduciary responsibility.

From time to time as part of the Corporation's normal course of business, customers make claims and take legal action against the Corporation based on its actions or inactions related to the fiduciary responsibilities of the Wealth Management Group Services segment. If such claims and legal actions are not resolved in a manner favorable to the Corporation, they may result in financial liability and/or adversely affect the market perception of the Corporation and its products and services. This may also impact customer demand for the Corporation's products and services. Any financial liability or reputation damage could have a material adverse effect on the Corporation's business, which, in turn, could have a material adverse effect on its financial condition and results of operations.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

The Corporation and the Bank currently conduct all their business activities from the Bank's main office in Elmira, New York, 34 full-service branch locations in a twelve county area, owned office space adjacent to the Bank's main office in Elmira, New York and ten off-site automated teller facilities (“ATMs”), all of which are located on leased property. The main office is a six-story structure located at One Chemung Canal Plaza, Elmira, New York, in the downtown business district. The main office consists of approximately 59,342 square feet of space, of which 745 square feet is occupied by the Corporation's subsidiary CFS Group, with the remaining 58,597 square feet entirely occupied by the Bank. The combined square footage of the 34 branch banking facilities totals approximately 177,000 square feet. The office building adjacent to the main office was acquired in 1995 and consists of approximately 33,186 square feet of which 30,766 square feet are occupied by operating departments of the Bank and 2,420 square feet are leased. The leased automated teller facility spaces total approximately 500 square feet. The Bank operates fourteen of its facilities (Auburn, Bath, Binghamton, Cortland, Clifton Park, Community Corners, Ithaca, Latham, Oakdale Mall, Slingerlands, Tioga, Vestal, and Albany-Washington Ave. and Wolf Rd Offices) and ten ATM’s (Collegetown Bagels, Corning Community College, Elmira College, Elmira/Corning Regional Airport, E-Z Food Mart, Hardinge Inc., Ithaca College, Lansing Market, Schuyler Hospital, and Quality Beverage) under lease arrangements. The rest of its offices, including the main office and the adjacent office building, are owned by the Bank. All properties owned or leased by the Bank are considered to be in good condition.

The Corporation holds no real estate in its own name.

ITEM 3. LEGAL PROCEEDINGS

The Bank is a party in two legal proceedings involving its Wealth Management Group. In both proceedings, the Bank, as trustee pursuant to written trust instruments, has sought judicial settlement of trust accounts in the New York Surrogate’s Court for Chemung County. Individuals who are beneficiaries under the trusts have filed formal objections and/or demand letters with the Court in both of these accounting proceedings, objecting to the final settlement of the trust accounts. The objectants primarily assert that the Bank acted imprudently by failing to diversify the trusts’ investments and they claim $9.6 million and $24.1 million, consisting of damages and disallowed trustee’s commissions, plus unspecified legal fees in the respective proceedings. These proceedings are pending in the Surrogate’s Court. While the outcome of litigation is not predictable the Bank believes that the claims are without merit and is vigorously defending them. As of December 31, 2013, no amount has been accrued for potential losses related to these proceedings as a potential loss is not considered probable or reasonably estimable in the opinion of management.

In the normal course of business, there are various outstanding claims and legal proceedings involving the Corporation or its subsidiaries. Except for the above matter, we believe that we are not a party to any pending legal, arbitration, or regulatory proceedings that could have a material adverse impact on our financial results or liquidity.

ITEM 4. MINE SAFETY DISCLOSURES

None

PART II

ITEM 5. MARKET FOR THE REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

The Corporation's stock is traded on the NASDAQ Global Market under the symbol "CHMG".

The table below shows the price ranges for the Corporation's common stock during each of the indicated quarters. Prior to November 16, 2012, the information is based upon actual transactions reported by brokerage firms that maintain a market for the Corporation's common stock and other transactions known to management. On November 14, 2012, the Corporation filed a Form 8-K with the SEC announcing that shares of its common stock would begin trading on the NASDAQ Global Market effective with the opening of trading on November 16, 2012. Since November 16, 2012, through December 31, 2013, the information is based upon the high and low sales prices reported by the NASDAQ Global Market.

Common Stock Market Prices and Dividends Paid
During the Past Two Years

December 31, 2013	High	Low	Dividends
4th Quarter	$36.00	$30.23	$ 0.26
3rd Quarter	35.85	30.31	0.26
2nd Quarter	34.53	30.18	0.26
1st Quarter	33.99	28.41	0.00
December 31, 2012			
4th Quarter	$32.50	$23.51	$ 0.50
3rd Quarter	25.70	23.55	0.25
2nd Quarter	25.99	24.76	0.25
1st Quarter	26.00	22.65	0.25

Under New York law, the Corporation may pay dividends on our common stock either: (i) out of surplus, so that the Corporation's net assets remaining after such payment equal the amount of its stated capital, or (ii) if 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. Our payment of dividends on our common stock is dependent, in large part, upon receipt of dividends from the Bank, which is subject to certain restrictions which may limit its ability to pay us dividends. See Item 1, "Business – Regulation and Supervision-The Bank-Payment of Dividends" for an explanation of legal limitations on the Bank's ability to pay dividends.

As of February 28, 2014, there were 1,226 registered holders of record of the Corporation's stock, which includes 608 Non Objecting Beneficial Owners ("NOBO") shares held in street name.

The table below sets forth the information with respect to purchases made by the Corporation of our common stock during the quarter ended December 31, 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 or

			or programs	programs
10/1/13-10/31/13	-	$ -	-	121,906
11/1/13-11/30/13	-	$ -	-	121,906
12/1/13-12/31/13	-	$ -	-	121,906
Quarter ended 12/31/13	-	$ -	-	121,906

(1) On December 19, 2012, the Corporation's Board of Directors approved a stock repurchase plan authorizing the purchase of up to 125,000 shares of the Corporation's outstanding common stock. Purchases may be made from time to time on the open market or in private negotiated transactions and will be at the discretion of management. For the year ending December 31, 2013, a total of 3,094 shares had been purchased under this plan.

STOCK PERFORMANCE GRAPH

The following graph compares the yearly change in the cumulative total shareholder return on the Corporation's common stock against the cumulative total return of the NASDAQ Stock Market (U.S. Companies), NASDAQ Bank Stocks Index and SNL $1B - $5B Bank Index for the period of five years commencing December 31, 2008.

[]

	Period Ending					
Index	12/31/08	12/31/09	12/31/10	12/31/11	12/31/12	12/31/13
Chemung Financial Corporation	100.00	108.84	125.64	132.26	181.22	213.90
NASDAQ Composite	100.00	145.36	171.74	170.38	200.63	281.22
NASDAQ Bank	100.00	83.70	95.55	85.52	101.50	143.84
SNL Bank $1B-$5B	100.00	71.68	81.25	74.10	91.37	132.87

The cumulative total return includes (1) dividends paid and (2) changes in the share price of the Corporation's common stock and assumes that all dividends were reinvested. The above graph assumes that the value of the investment in Chemung Financial Corporation and each index was $100 on December 31, 2008.

The Total Returns Index for NASDAQ Stock Market (U.S. Companies) and Bank Stocks indices were obtained from SNL Financial LC, Charlottesville, VA.

ITEM 6. SELECTED FINANCIAL DATA

The following tables present selected financial data as of and for the years ended December 31, 2013, 2012, 2011, 2010 and 2009. The selected financial data is derived from our audited consolidated financial statements.

The selected financial data should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our audited consolidated financial statements and related notes.

SUMMARIZED BALANCE SHEET DATA AT DECEMBER 31, (in thousands)	2013	2012	2011	2010	2009
Total assets	$1,476,143	$1,248,160	$1,216,260	$958,327	$975,552
Loans	995,866	893,517	796,915	613,684	595,853
Investment securities	352,511	245,434	289,182	231,260	243,143
FHLBNY and FRBNY stock	4,482	4,710	5,509	3,329	3,281
Deposits	1,263,370	1,044,734	998,493	786,359	801,063
Securities sold under agreements to repurchase	32,701	32,711	37,107	44,775	54,263
FHLBNY advances	25,243	27,225	43,344	20,000	20,000
Shareholders' equity	138,578	131,115	125,929	97,409	90,086

SUMMARIZED EARNINGS DATA FOR THE YEARS ENDED DECEMBER 31, (in thousands)		2013		2012		2011		2010		2009
Net interest income	$	46,631	$	46,842	$	43,915	$	34,530	$	33,155
Provision for loan losses		2,755		828		958		1,125		2,450
Net interest income after provision for loan losses	$	43,876		46,014		42,957		33,405		30,705
Other operating income:										
Wealth management group fee income		7,344		6,827		6,710		10,497		8,089
Securities gains, net		(13)		301		1,108		451		785
Trust Preferred impairment		-		-		(67)		(393)		(2,242)
Net gains on sales of loans held for sale		503		484		179		242		259
Other income		10,242		9,576		9,534		8,848		8,819
Total other operating income		18,076		17,188		17,464		19,645		15,710
Other operating expenses		49,399		46,795		44,850		37,843		39,321
Income before income tax expense		12,553		16,407		15,571		15,207		7,094
Income tax expense		3,822		5,385		5,033		5,105		1,861
Net income	$	8,731	$	11,022	$	10,538	$	10,102	$	5,233

2013	2012	2011	2010	2009	2008

SELECTED PER SHARE DATA ON SHARES OF COMMON STOCK AT OR FOR THE YEARS ENDED DECEMBER 31,							% Change 2012 To 2013	Compounded Annual Growth 5 Years
Earnings per share (1)	$ 1.87	$ 2.38	$ 2.40	$ 2.80	$ 1.45	$ 2.32	-21.4%	-4.2%
Dividends declared	1.04	1.00	1.00	1.00	1.00	1.00	0.4%	0.8%
Tangible book value (2)	23.63	22.40	21.07	22.90	20.74	18.96	5.5%	4.5%
Market price at 12/31	34.17	29.89	22.75	22.30	21.25	20.40	14.3%	10.9%
Weighted average shares outstanding (in thousands)	4,660	4,641	4,383	3,607	3,603	3,594	0.4%	5.3%

(1) Earnings per share is computed by dividing net income by the weighted average number of common shares outstanding. There is no difference between basic and diluted earnings per share.

(2) Tangible book value is total shareholders' equity minus goodwill and other intangible assets, net.

SELECTED RATIOS AT OR FOR THE YEARS ENDED DECEMBER 31,	2013	2012	2011	2010	2009
Return on average assets	0.67%	0.88%	0.90%	1.02%	0.56%
Return on average equity	6.50%	8.41%	8.77%	10.64%	6.13%
Dividend yield at year end	3.08%	4.20%	4.40%	4.48%	4.71%
Dividend payout	41.04%	51.84%	38.50%	34.84%	67.21%
Total capital to risk adjusted assets	12.10%	13.10%	13.28%	14.54%	13.22%
Tier I capital to risk adjusted assets	10.57%	11.68%	11.84%	12.92%	11.61%
Tier I leverage ratio	8.08%	8.74%	8.27%	8.72%	7.89%
Average equity to average assets	10.28%	10.46%	10.23%	9.60%	9.19%
Year-end equity to year-end assets ratio	9.39%	10.50%	10.35%	10.16%	9.23%
Loans to deposits	78.83%	85.53%	79.81%	78.04%	74.38%
Allowance for loan losses to total loans	1.28%	1.17%	1.21%	1.55%	1.67%
Allowance for loan losses to non-performing loans	150.11%	172.96%	70.97%	89.62%	168.65%
Non-performing assets to total assets	0.61%	0.53%	1.19%	1.18%	0.67%
Net interest rate spread	3.72%	3.90%	3.86%	3.53%	3.49%
Net interest margin	3.85%	4.07%	4.07%	3.81%	3.89%
Efficiency ratio (1)	74.77%	71.30%	71.21%	68.35%	78.40%

(1) Efficiency ratio is operating expenses adjusted for amortization of intangible assets and stock donations divided by net interest income (before provision for loan losses) plus other operating income adjusted for non-taxable gains on stock donations. The efficiency ratio is not adjusted for expenses related to mergers and acquisitions.

The following tables summarize the Corporation's unaudited net income and basic earnings per share at each quarter end for the years 2013 and 2012 (in thousands of dollars except per share data):

	2013 Quarter Ended			
UNAUDITED QUARTERLY DATA	Mar. 31	June 30	Sept. 30	Dec. 31
Interest and dividend income	$ 12,748	$ 12,333	$ 12,510	$ 13,073
Interest expense	1,031	1,005	993	1,003
Net interest income	11,717	11,328	11,517	12,070
Provision for loan losses	431	450	874	1,000
Net interest income after provision for loan losses	11,286	10,878	10,643	11,070
Total other operating income	4,022	4,475	4,351	5,229
	11,725	11,392	11,813	14,471

Total other operating expenses								
Income before income tax expense		3,583		3,961		3,181		1,828
Income tax expense		1,171		1,306		1,002		343
Net Income	$	2,412	$	2,655	$	2,179	$	1,485
Basic and diluted earnings per share	$	0.52	$	0.57	$	0.46	$	0.32

				2012 Quarter Ended				
UNAUDITED QUARTERLY DATA		Mar. 31		June 30		Sept. 30		Dec. 31
Interest and dividend income	$	13,540	$	12,765	$	13,015	$	12,757
Interest expense		1,508		1,385		1,225		1,116
Net interest income		12,032		11,380		11,790		11,641
Provision for loan losses		477		52		225		74
Net interest income after provision for loan losses		11,555		11,328		11,565		11,567
Total other operating income		4,890		4,112		3,992		4,192
Total other operating expenses		10,931		11,881		11,340		12,642
Income before income tax expense		5,514		3,559		4,217		3,117
Income tax expense		1,899		1,115		1,383		987
Net Income	$	3,615	$	2,444	$	2,834	$	2,130
Basic and diluted earnings per share	$	0.78	$	0.53	$	0.61	$	0.46

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION

To assist the reader, the Corporation has provided the following list of commonly used acronyms and abbreviations included in Management's Discussion and Analysis of Financial Condition and Results of Operations.

CDO: Collateralized Debt Obligation	GAAP: U.S. generally accepted accounting principles
FASB: Financial Accounting Standards Board	OTTI: Other-Than-Temporary Impairment
FDIC: Federal Deposit Insurance Corporation	PCI: Purchased Credit Impaired
FHLBNY: Federal Home Loan Bank of New York	SEC: Securities and Exchange Commission
FRBNY: Federal Reserve Bank of New York	TDR: Troubled Debt Restructurings

The purpose of this discussion is to focus on information about the financial condition and results of operations of Chemung Financial Corporation (the "Corporation"). Reference should be made to the accompanying consolidated financial statements and footnotes, and the selected financial data appearing elsewhere in this report for an understanding of the following discussion and analysis.

This discussion contains forward-looking statements within the meaning of Section 27A of the Securities Act and Section 21E of the Exchange Act. The Corporation intends its forward-looking statements to be covered by the safe harbor provisions for forward-looking statements in these sections. All statements regarding the Corporation's expected financial position and operating results, the Corporation's business strategy, the Corporation's financial plans, forecasted demographic and economic trends relating to the Corporation's industry and similar matters are forward-looking statements. These statements can sometimes be identified by the Corporation's use of forward-looking words such as "may," "will," "anticipate," "estimate," "expect," or "intend." The Corporation cannot promise that its expectations in such forward-looking statements will turn out to be correct. The Corporation's actual results could be materially different from expectations because of various factors, including changes in economic conditions or interest rates, credit risk, difficulties in managing the Corporation's growth, competition, changes in law or the regulatory environment, including the Dodd-Frank Act, and changes in general business and economic trends. Information concerning these and other factors can be found in the Corporation's periodic filings with the SEC, including the discussion under the heading "Item 1A. Risk Factors" in this form 10-K. These filings are available publicly on the SEC's web site at http://www.sec.gov, on the Corporation's web site at http://www.chemungcanal.com or upon request from the Corporate Secretary at (607) 737-3746. Except as otherwise required by law, the Corporation undertakes no obligation to publicly update or revise its forward-looking statements, whether as a result of new information, future events or otherwise.

Overview

The Corporation has been a financial holding company since 2000, and the Bank was established in 1833 and CFS Group, Inc. in 2001. Through the Bank and CFS Group, Inc., the Corporation provides a wide range of financial services, including demand, savings and time deposits, commercial, residential and consumer loans, letters of credit, wealth management services, employee benefit plans, securities and insurance brokerage services. The Bank relies substantially on a foundation of locally generated deposits.

The parent-only company has minimal results of operations. The Bank derives its income primarily from interest and fees on loans, interest on investment securities, Wealth Management Group fee income and fees received in connection with deposit and other services. The Bank's operating expenses are interest expense paid on deposits and borrowings, salaries and employee benefit plans and general operating expenses.

2013 Highlights

- In the fourth quarter, the Bank completed the acquisition of six branch offices from Bank of America located in Cayuga, Cortland, Seneca and Tompkins counties in New York. As part of the transaction, the Corporation acquired $177.7 million in deposits and $1.2 million in loans and incurred $1.4 million of pre-tax branch acquisition costs.

- Net income for 2013 was $8.7 million, or $1.87 per share, compared with $11.0 million, or $2.38 per share, for 2012, a decrease of $2.3 million, or 20.8%.

- Returns on average assets and average equity for 2013 were 0.67% and 6.50%, respectively, compared with 0.88% and 8.41%, respectively, for 2012.

- Net interest margin for 2013 was 3.85%, down from 4.07% for 2012.

- The non-performing assets to total assets ratio was 0.61% at December 31, 2013 compared with 0.53% at December 31, 2012.

- Book value per share was $29.67 at December 31, 2013 compared with $28.20 at December 31, 2012, an increase of $1.47, or 5.2%. Tangible book value per share was $23.63 at December 31, 2013 compared with $22.40 at December 31, 2012, an increase of $1.23 or 5.5%.

- As a result of the branch acquisition, the tangible equity to tangible assets ratio decreased to 7.62% at December 31, 2013 compared with 8.53% at December 31, 2012.

Critical Accounting Policies, Estimates and Risks and Uncertainties

Critical accounting policies include the areas where the Corporation has made what it considers to be particularly difficult, subjective or complex judgments concerning estimates, and where these estimates can significantly affect the Corporation's financial results under different assumptions and conditions. The Corporation prepares its financial statements in conformity with GAAP. As a result, the Corporation is required to make certain estimates, judgments and assumptions that it believes are reasonable based upon the information available at that time. These estimates, judgments and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the periods presented. Actual results could be different from these estimates.

Management 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 probable incurred credit losses inherent in the loan portfolio, and the material effect that such judgments can have on the Corporation's 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 would need to be increased. For example, if historical loan loss experience significantly worsened or if current economic conditions significantly deteriorated, additional provisions for loan losses would be required to increase the allowance. In addition, the assumptions and estimates used in the internal reviews of the Corporation's non-performing loans and potential problem loans, and the associated evaluation of the related collateral coverage for these loans, has a significant impact on the overall analysis of the adequacy of the allowance for loan losses. Real estate values in the Corporation’s market area did not increase dramatically in the prior several years, and, as a result, any declines in real estate values have been modest. While management has concluded that the current evaluation of collateral values is reasonable under the circumstances, if collateral evaluations were significantly lowered, the Corporation's allowance for loan losses policy would also require additional provisions for loan losses.

Management also considers the accounting policy relating to OTTI of investment securities to be a critical accounting policy. The determination of whether a decline in market value is other-than-temporary is necessarily a matter of subjective judgment. The timing and amount of any realized losses reported in the Corporation's financial statements could vary if management's conclusions were to change as to whether other-than-temporary impairment exists. The Corporation assesses whether it intends to sell, or it is more likely than not that it will be required to sell a security in an unrealized loss position before recovery of its amortized cost basis. If either of these criteria is met, the entire difference between amortized cost and fair value is recognized through a charge to earnings. For those securities that do not meet the aforementioned criteria, such as those that management has determined to be other-than-temporarily impaired, the amount of impairment charged to earnings is limited to the amount related to credit losses, while impairment related to other factors is recognized in other comprehensive income. The Corporation uses an OTTI evaluation model to compare the present value of expected cash flows to the previous estimate to determine if there are adverse changes in cash flows during the quarter.

Management also considers the accounting policy relating to the valuation of goodwill and other intangible assets to be a critical accounting policy. The initial carrying value of goodwill and other intangible assets is determined using estimated fair values developed from various sources and other generally accepted valuation techniques. Estimates are based upon financial, economic, market and other conditions as they existed as of the date of a particular acquisition. These estimates of fair value are the results of judgments made by the Corporation based upon estimates that are inherently uncertain and changes in the assumptions upon which the estimates were based may have a significant impact on the resulting estimates. In addition to the initial determination of the carrying value, on an ongoing basis management must assess whether there is any impairment of goodwill and other intangible assets that would require an adjustment in carrying value and recognition of a loss in the consolidated statement of income.

Financial Condition

Summary

Consolidated assets at December 31, 2013 totaled $1.476 billion, an increase of $227.9 million or 18.3% since December 31, 2012. The growth was due primarily to increases of $106.3 million in investment securities available for sale and $102.4 million, or 11.5%, in total portfolio loans. The increase in portfolio loans was due to strong growth of $64.5 million in commercial loans and $42.4 million in consumer loans.

Total liabilities increased $220.5 million to $1.338 billion at December 31, 2013, due primarily to an increase of $218.6 million in deposits. The growth in deposits was due primarily to increases of $177.7 million from the branch acquisition and $40.9 million in organic deposit growth. Total shareholders’ equity was $138.6 million at December 31, 2013, an increase of $7.5 million from December 31, 2012, due primarily to the Corporation’s net income of $8.7 million and a $3.0 million reduction in accumulated other comprehensive loss, partially offset by declared dividends of $4.8 million.

The market value of total assets under management or administration in the Corporation’s Wealth Management Group was $1.888 billion at December 31, 2013 compared with $1.735 billion at December 31, 2012, an increase of $153.0 million, or 8.8%.

Balance Sheet Comparisons

Table 1 contains selected average balance sheet information for each year in the six-year period ended December 31, 2013 (in millions of dollars):

TABLE 1. SELECTED AVERAGE BALANCE SHEET INFORMATION

Average Balance Sheet	2013	2012	2011	2010	2009	2008	% Change 2012 to 2013	Compounded Annual Growth 5 Years
Total Assets	$1,306.4	$1,253.7	$1,175.0	$ 988.6	$ 928.8	$ 837.5	4.2%	9.3%
Earning Assets (1)	1,209.7	1,150.4	1,078.4	905.5	852.4	757.3	5.2%	9.8%
Loans (2)	942.9	844.2	741.0	590.6	586.7	561.6	11.7%	10.9%
Investments (3)	266.8	306.2	337.4	314.9	265.7	195.7	-12.9%	6.4%
Deposits	1,090.5	1,042.7	965.2	817.6	752.4	649.7	4.6%	10.9%
Borrowings (4)	69.5	70.7	81.3	68.4	79.2	87.2	-1.7%	-4.4%
Shareholders' Equity	134.3	131.1	120.2	94.9	85.4	89.2	2.4%	8.5%

(1) Average earning assets include securities available for sale and securities held to maturity based on amortized cost, loans net of deferred origination fees and costs and unearned income, interest-bearing deposits, FHLBNY stock, FRBNY stock and federal funds sold.
(2) Average loans, net of deferred origination fees and costs, and unearned income.
(3) Average balances for investments include securities available for sale and securities held to maturity, based on amortized cost, FHLBNY stock, FRBNY stock, federal funds sold and interest-bearing deposits.
(4) Average borrowings include FHLBNY advances and securities sold under agreements to repurchase.

Table 2 contains selected period-end balance sheet information for each year in the six-year period ended December 31, 2013 (in millions of dollars):

TABLE 2. SELECTED PERIOD-END BALANCE SHEET INFORMATION

Ending Balance Sheet	2013	2012	2011	2010	2009	2008	% Change 2012 to 2013	Compounded Annual Growth 5 Years
Total Assets	$1,476.1	$1,248.2	$1,216.3	$ 958.3	$ 975.6	$ 838.3	18.3%	12.0%
Earning Assets (1)	1,372.9	1,154.7	1,116.3	892.4	900.9	770.4	18.9%	12.2%
Loans (2)	995.9	893.5	796.9	613.7	595.9	565.2	11.5%	12.0%
Allowance for loan losses	12.8	10.4	9.7	9.5	10.0	9.1	22.5%	7.01%
Investments (3)	377.0	261.2	319.4	278.7	305.0	205.2	44.4%	12.9%
Deposits	1,263.4	1,044.7	998.5	786.4	801.1	656.9	20.9%	14.0%

Borrowings (4)	57.9	59.9	80.5	64.8	74.3	83.4	-3.3%	-7.0%
Shareholders' Equity	138.6	131.1	125.9	97.4	90.1	83.0	5.7%	10.8%

(1) Earning assets include securities available for sale, at estimated fair value and securities held to maturity based on amortized cost, loans net of deferred origination fees and costs and unearned income, interest-bearing deposits, FHLBNY stock, FRBNY stock and federal funds sold.
(2) Loans, net of deferred origination fees and costs, and unearned income.
(3) Investments include securities available for sale, at estimated fair value, securities held to maturity, at amortized cost, FHLBNY stock, FRBNY stock, federal funds sold and interest-bearing deposits.
(4) Borrowings include FHLBNY advances and securities sold under agreements to repurchase.

Cash and Cash Equivalents

Total cash and cash equivalents increased $11.4 million since December 31, 2012, due primarily to increases of $9.0 million in interest-bearing deposits in other financial institutions and $2.4 million in cash and due from financial institutions. The increases were due to additional cash from the branch acquisition that was not used to help fund the increase in investment securities and portfolio loans. The Corporation continues to evaluate alternative investment of these funds with caution, given the low interest rate environment.

Securities

The Corporation's Funds Management Policy includes an investment policy that in general, requires debt securities purchased for the bond portfolio to carry a minimum agency rating of "A". After an independent credit analysis is performed, the policy also allows the Corporation to purchase local municipal obligations that are not rated. The Corporation intends to maintain a reasonable level of securities to provide adequate liquidity and in order to have securities available to pledge to secure public deposits, repurchase agreements and other types of transactions. Fluctuations in the fair value of the Corporation's securities relate primarily to changes in interest rates.

Marketable securities are classified as Available for Sale, while investments in local municipal obligations are generally classified as Held to Maturity. The composition of the available for sale segment of the securities portfolio is summarized in Table 3 as follows (in thousands of dollars):

TABLE 3. SECURITIES AVAILABE FOR SALE

	2013			2012		
Securities Available for Sale	Amortized Cost	Estimated Fair Value	Unrealized Gains (Losses)	Amortized Cost	Estimated Fair Value	Unrealized Gains (Losses)
Obligations of U.S. Government and U.S Government sponsored enterprises	$187,098	$188,106	$ 1,008	$138,041	$141,591	$ 3,550
Mortgage-backed securities, residential	104,069	104,357	288	29,592	31,515	1,923
Collateralized mortgage obligations	1,001	1,015	14	3,495	3,543	48
Obligations of states and political Subdivisions	37,339	38,376	1,037	39,175	40,815	1,640
Corporate bonds and notes	2,879	2,946	67	11,412	11,652	240
SBA loan pools	1,471	1,488	17	1,683	1,724	41
Trust preferred securities	1,898	2,033	135	2,519	2,471	(48)
Corporate stocks	444	7,695	7,251	736	6,375	5,639
Totals	$336,199	$346,016	$ 9,817	$226,653	$239,686	$13,033

The available for sale segment of the securities portfolio totaled $346.0 million at December 31, 2013, an increase of $106.3 million, or 44.4%, from $239.7 million at December 31, 2012. The increase resulted primarily from purchases of $174.0 million, partially offset by sales and calls of $18.1 million, and maturities and principal collected of $44.0 million. The increase in securities available for sale was funded from the deposits acquired in the branch acquisition.

The held to maturity segment of the securities portfolio consists of obligations of political subdivisions in the Corporation's market areas. These securities totaled $6.5 million at December 31, 2013, an increase of $0.8 million, or 13.0%, from $5.7 million at December 31, 2012. The increase resulted primarily from purchases of $6.4 million, partially offset by maturities and principle collected of $5.7 million.

Non-marketable equity securities at December 31, 2013 include shares of FRBNY stock and FHLBNY stock, carried at their cost of $1.7 million and $2.8 million, respectively. The fair value of these securities is assumed to approximate their cost. The investment in these stocks is regulated by regulatory policies of the respective institutions.

Table 4 sets forth the carrying amounts and maturities of available for sale and held to maturity debt securities at December 31, 2013 and the weighted average yields of such securities (all yields are calculated on the basis of the amortized cost and weighted for the scheduled maturity of each security, except mortgage-backed securities which are based on the average life at the projected prepayment speed of each security). Federal tax equivalent adjustments have not been made in calculating yields on municipal obligations (in thousands of dollars):

TABLE 4. MATURIES AND YIELDS OF AVAILABLE FOR SALE AND HELD TO MATURITY SECURITIES

	Maturing							
	Within One Year		After One, But Within Five Years		After Five, But Within Ten Years		After Ten Years	
	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
Obligations of U.S. Government and U.S. Government sponsored enterprises	$ 10,289	1.38 %	$ 162,945	1.56 %	$ 14,872	2.23%	$ -	-
Mortgage-backed securities, Residential	670	3.78 %	68,951	2.29 %	34,670	2.18%	65	2.40%
Collateralized mortgage obligations	874	2.35 %	141	4.67 %	-	-	-	-
Obligations of states and political subdivisions	11,966	2.09 %	28,252	2.61 %	3,629	3.00%	-	-
Corporate bonds and notes	1,385	2.94 %	1,323	4.04 %	238	3.25%	-	-
SBA loan pools	-	-	341	1.46 %	1,147	1.85%	-	-
Trust preferred securities	2,034	8.93 %	-	- %	-	-	-	-%
Total	$ 27,218	2.40 %	$ 261,953	1.88 %	$ 54,556	2.24%	$ 65	2.40%

Management evaluates securities for OTTI on a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. For the years ended December 31, 2013 and 2012, the Corporation had no OTTI charges. During the fourth quarter of 2013, the Corporation sold one CDO consisting of a pool of trust preferred securities that had an amortized cost of $0.6 million. The CDO was sold for $0.6 million, resulting in a slight loss. The CDO was sold in light of the uncertainty surrounding the recently released rules contained in the "Volcker Rule" provision of the Dodd-Frank Act regarding the ability of banks to hold these types of securities and based on current market conditions. In addition to the CDO that was sold in the fourth quarter of 2013, the remaining CDO was liquidated and the Corporation will record approximately $0.5 million in other income during the first quarter of 2014. The Corporation does not own any other CDOs in its investment securities portfolio. For more detailed information on OTTI, see Footnote (3), “Securities” in the Notes to Consolidated Financial Statements.

Loans

The Corporation has reporting systems to monitor: (i) loan originations and concentrations, (ii) delinquent loans, (iii) non-performing assets, including non-performing loans, troubled debt restructurings, other real estate owned, (iv) impaired loans, and (v) potential problem loans. Management reviews these systems on a regular basis.

Table 5 shows the Corporation's loan composition by segment and percentage of total loans at the end of each of the last five years (in thousands of dollars):

TABLE 5. LOANS

	December 31,									
	2013	%	2012	%	2011	%	2010	%	2009	%
Commercial and agricultural	$145,362	14.6	$133,851	15.0	$142,209	17.8	$114,697	18.7	$118,303	19.9
Commercial mortgages	373,147	37.5	320,198	35.9	264,589	33.2	133,070	21.7	123,669	20.7
Residential mortgages	195,997	19.7	200,475	22.4	193,600	24.3	173,468	28.3	162,447	27.3
Indirect consumer loans	164,846	16.5	130,573	14.6	97,165	12.2	98,941	16.1	94,122	15.8
Consumer loans	116,514	11.7	108,420	12.1	99,352	12.5	93,508	15.2	97,312	16.3
Total	$995,866	100.0	$893,517	100.0	$796,915	100.0	$613,684	100.0	$595,853	100.0

Portfolio loans totaled $995.9 million at December 31, 2013, an increase of $102.4 million, or 11.5%, from $893.5 million at December 31, 2012. The increase in portfolio loans was due to strong growth of $64.5 million, or 14.2%, in commercial loans and $42.4 million, or 17.7%, in consumer loans. The growth in commercial loans was due primarily to an increase of $51.7 million in commercial loans in the Capital Bank division in the Albany, New York region. The growth in consumer loans was primarily due to increases of $34.2 million in indirect consumer loans and $8.9 million in home equity loans. The Corporation conducted a marketing campaign for direct consumer loans during the second and third quarters of 2013.

Residential mortgage loans totaled $196.0 million at December 31, 2013, a decrease of $4.5 million, or 2.2%, from December 31, 2012. In addition, during 2013, $18.8 million of residential mortgages were sold in the secondary market to Freddie Mac, with an additional $0.7 million of residential mortgages sold to the State of New York Mortgage Agency.

The Corporation anticipates that future growth in portfolio loans will continue to be in commercial mortgages and indirect consumer loans.

Loan concentrations are considered to exist when there are amounts loaned to a multiple number of borrowers engaged in similar activities which would cause them to be similarly impacted by economic or other conditions. The Corporation’s concentration policy limits the volume of commercial loans to any one specific industry. Specific industries are identified using the North American Industry Classification System ("NAICS") codes. The volume of commercial loans, with the exception of commercial mortgages, to any one specific industry is limited to Tier 1 capital plus the allowance for loan losses. The volume of commercial mortgages is limited to three times the total of Tier 1 capital plus the allowance for loan losses. The Corporation is in compliance with the concentration policy limits.

The Corporation also monitors specific NAICS industry classifications of commercial loans to indentify concentrations greater than 10.0% of total loans. At December 31, 2013 and 2012, commercial loans to borrowers involved in the real estate, and real estate rental and lending businesses were 31.1% and 27.7% of total loans, respectively. No other concentration of loans existed in the commercial loan portfolio in excess of 10.0% of total loans as of December 31, 2013 and 2012.

Table 6 shows the maturity of only commercial and agricultural loans and commercial mortgages outstanding as of December 31, 2013. Also provided are the amounts due after one year, classified according to the sensitivity to changes in interest rates (in thousands of dollars):

TABLE 6. LOAN AMOUNTS CONTRACTUALLY DUE AFTER DECEMBER 31, 2013

	Within One Year	After One But Within Five Years	After Five Years	Total
Commercial, agricultural and commercial mortgages	$70,130	$ 98,949	$349,430	$518,509
Loans maturing after one year with:				
Fixed interest rates	$24,334	$ 71,177	$ 111,412	$ 206,923
Variable interest rates	45,796	27,772	238,018	311,586
Total	$70,130	$ 98,949	$349,430	$518,509

Non-Performing Assets

Non-performing assets consist of non-accrual loans, non-accrual troubled debt restructurings and other real estate owned that has been acquired in partial or full satisfaction of loan obligations or upon foreclosure.

Past due status on all loans is based on the contractual terms of the loan. It is generally the Corporation's policy that a loan 90 days past due be placed in non-accrual status unless factors exist that would eliminate the need to place a loan in this status. A loan may also be designated as non-accrual at any time if payment of principal or interest in full is not expected due to deterioration in the financial condition of the borrower. At the time loans are placed in non-accrual status, the accrual of interest is discontinued and previously accrued interest is reversed. All payments received on non-accrual loans are applied to principal. Loans are considered for return to accrual status when they become current as to principal and interest and remain current for a period of six consecutive months or when, in the opinion of management, the Corporation expects to receive all of its original principal and interest. In the case of non-accrual loans where a portion of the loan has been charged off, the remaining balance is kept in non-accrual status until the entire principal balance has been recovered.

Table 7 summarizes the Corporation's non-performing assets, excluding purchased credit impaired ("PCI") loans acquired in the acquisition of FOFC (in thousands of dollars):

TABLE 7. NON-PERFORMING ASSETS

December 31,	2013	2012	2011	2010	2009
Non-accrual loans	$ 7,456	$ 5,667	$ 9,554	$ 6,805	$ 5,703
Non-accrual troubled debt restructurings	1,061	365	4,057	3,793	207
Total non-performing loans	8,517	6,032	13,611	10,598	5,910
Other real estate owned	538	565	898	741	649
Total non-performing assets	$ 9,055	$ 6,597	$ 14,509	$ 11,339	$ 6,559
Ratio of non-performing loans to total loans	0.86 %	0.68%	1.71%	1.73%	0.99%
Ratio of non-performing assets to total assets	0.61%	0.53%	1.19%	1.18%	0.67%
Ratio of allowance for loan losses to non-performing loans	150.01%	172.96%	70.97%	89.62%	168.65%
Accruing loans past due 90 days or more (1)	1,473	4,484	7,304	11	517
Accruing troubled debt restructurings (1)	6,831	5,364	-	659	7,377

(1) These loans are not included in nonperforming assets above.

Table 8 shows interest income on non-accrual and troubled debt restructured loans for the indicated years ended December 31 (in thousands of dollars):

TABLE 8. INTEREST INCOME ON NON-ACCRUAL AND TROUBLED DEBT RESTRUCTURED LOANS

	2013	2012	2011
Interest income that would have been recorded under original terms	$ 541	$ 666	$ 1,009
Interest income recorded during the period	$ 421	$ 12	$ 34

Non-Performing Loans

The recorded investment in non-performing loans at December 31, 2013, totaled $8.5 million compared to $6.0 million at year-end 2012, an increase $2.5 million. The increase in non-performing loans was due to increases of $1.8 million in non-accrual loans and $0.7 million in non-accrual TDRs. Non-performing commercial loans increased $1.6 million and non-performing residential mortgages increased $0.9 million.

The recorded investment in accruing loans 90 days or more past due totaled $1.5 million at December 31, 2013, compared with $4.5 million at year-end 2012, a decrease of $3.0 million. This decrease was due to a decrease of $3.0 million in acquired construction loans not considered by management to be PCI loans, which for a variety of reasons are 90 days or more past their stated maturity dates. These loans totaled $1.5 million at December 31, 2013. However, the borrowers continue to make required interest payments. Additionally, these loans carry third party credit enhancements, and based on the strength of those credit enhancements, the Corporation has not identified these loans as PCI loans and expects to incur no losses on these loans.

Not included in the non-performing loan totals are loans acquired in the April 2011 acquisition of FOFC and its wholly-owned subsidiary, Capital Bank, which the Corporation had identified as PCI loans totaled $9.7 million and $10.7 million at December 31, 2013 and 2012, respectively. The PCI loans are accounted for under separate accounting guidance, Accounting Standards Codification ("ASC") Subtopic 310-30, "Receivables - Loans and Debt Securities Acquired with Deteriorated Credit Quality" as disclosed in Note 4 of the financial statements.

Troubled Debt Restructurings

The Corporation works closely with borrowers that have financial difficulties to identify viable solutions that minimize the potential for loss. In that regard, the Corporation modified the terms of select loans to maximize their collectability. The modified loans are considered TDRs under current accounting guidance. Modifications generally involve short-term deferrals of principal and/or interest payments, reductions of scheduled payment amounts, interest rates or principal of the loan, and forgiveness of accrued interest. As of December 31, 2013, the Corporation had $1.1 million of non-accrual TDRs compared with $0.4 million as of December 31, 2012. The increase in non-accrual TDRs was primarily in the commercial loan segment of the loan portfolio. As of December 31, 2013, the Corporation had $6.8 million of accruing TDRs compared with $5.3 million as of December 31, 2012. The increase in accruing TDRs was primarily in the commercial loan segment of the loan portfolio.

Impaired Loans

Impaired loans at December 31, 2013 totaled $13.9 million, including TDRs of $7.9 million, compared with $12.7 million at December 31, 2012, including TDRs of $5.7 million. Not included in the impaired loan totals are loans acquired in the FOFC acquisition which the Corporation has identified as PCI loans, as these loans are accounted for under ASC Subtopic 310-30 as noted under the above discussion of non-performing loans. The increase of $1.2 million in impaired loans resulted principally from an increase in impaired commercial loans. Included in the impaired loan total at December 31, 2013, are loans totaling $2.0 million for which impairment allowances of $1.0 million have been specifically allocated to the allowance for loan losses. As of December 31, 2012, the impaired loan total included $0.8 million of loans for which specific impairment allowances of $0.2 million were allocated to the allowance for loan losses. The increase in the amount of impaired loans for which specific allowances were allocated to the allowance for loan losses was due primarily to an increase in impaired commercial loans.

The majority of the Corporation's impaired loans are secured and measured for impairment based on collateral evaluations. It is the Corporation's policy to obtain updated appraisals, by independent third parties, on loans secured by real estate at the time a loan is determined to be impaired. An impairment measurement is performed based upon the most recent appraisal on file to determine the amount of any specific allocation or charge-off. In determining the amount of any specific allocation or charge-off, the Corporation will make adjustments to reflect the estimated costs to sell the property. Upon receipt and review of the updated appraisal, an additional measurement is performed to determine if any adjustments are necessary to reflect the proper provisioning or charge-off. Impaired loans are reviewed on a quarterly basis to determine if any changes in credit quality or market conditions would require any additional allocation or recognition of additional charge-offs. Real estate values in the Corporation's market area had not increased dramatically in the prior several years and, as a result, declines in real estate values have been modest. Non-real estate collateral may be valued using (i) an appraisal, (ii) net book value of the collateral per the borrower’s financial statements, or (iii) aging reports, that may be adjusted based on management’s knowledge of the client and client’s business. If market conditions warrant, future appraisals are obtained for both real estate and non-real estate collateral.

Allowance for Loan Losses

The allowance is an amount that management believes will be adequate to absorb probable incurred losses on existing loans. The allowance is established based on management's evaluation of the probable inherent losses in our portfolio in accordance with GAAP, and is comprised of both specific valuation allowances and general valuation allowances.

A loan is classified as impaired when, based on current information and events, it is probable that the Corporation will be unable to collect both the principal and interest due under the contractual terms of the loan agreement. Specific valuation allowances are established based on management's analyses of individually impaired loans. Factors considered by management in determining impairment include payment status, evaluations of the underlying collateral, expected cash flows, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. If a loan is determined to be impaired and is placed on nonaccrual status, all future payments received are applied to principal and a portion of the allowance is allocated so that the loan is reported, net, at the present value of estimated future cash flows using the loan's existing rate or at the fair value of collateral if repayment is expected solely from the collateral.

The general component covers non-impaired loans and is based on historical loss experience adjusted for current factors. Loans not impaired but classified as substandard and special mention use a historical loss factor on a rolling five year history of net losses. For all other unclassified loans, the historical loss experience is determined by portfolio class and is based on the actual loss history experienced by the Corporation over the most recent two years. This actual loss experience is supplemented with other qualitative factors based on the risks present for each portfolio class. These qualitative factors include consideration of the following: (1) lending policies and procedures, including underwriting standards and collection, charge-off and recovery policies, (2) national and local economic and business conditions and developments, including the condition of various market segments, (3) loan profiles and volume of the portfolio, (4) the experience, ability, and depth of lending management and staff, (5) the volume and severity of past due, classified and watch-list loans, non-accrual loans, troubled debt restructurings, and other modifications (6) the quality of the Bank's loan review system and the degree of oversight by the Bank's Board of Directors, (7) collateral related issues: secured vs. unsecured, type, declining valuation environment and trend of other related factors, (8) the existence and effect of any concentrations of credit, and changes in the level of such concentrations, (9) the effect of external factors, such as competition and legal and regulatory requirements, on the level of estimated credit losses in the Bank's current portfolio and (10) the impact of the global economy.

The allowance for loan losses is increased through a provision for loan losses charged to operations. Loans are charged against the allowance for loan losses when management believes that the collectability of all or a portion of the principal is unlikely. Management's evaluation of the adequacy of the allowance for loan losses is performed on a periodic basis and takes into consideration such factors as the credit risk grade assigned to the loan, historical loan loss experience and review of specific impaired loans. While management uses available information to recognize losses on loans, future additions to the allowance may be necessary based on changes in economic conditions. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Corporation's allowance for loan losses. Such agencies may require the Corporation to recognize additions to the allowance based on their judgments about information available to them at the time of their examination.

Prior to December 31, 2012, the Corporation utilized the sum of all allowance amounts derived as described above, combined with a reasonable unallocated allowance, as the primary indicator of the appropriate level of allowance for loan losses. During the fourth quarter of 2012, the Corporation refined its allowance calculation whereby it "allocated" the portion of the allowance that was previously deemed to be unallocated allowance. This refined allowance calculation included specific allowance allocations for qualitative factors including (i) concentrations of credit, (ii) general economic and business conditions, (iii) trends that could affect collateral values and (iv) expectations regarding the current business cycle. The Corporation may also consider other qualitative factors in future periods for additional allowance allocations, including, among other factors, (1) credit quality trends (including trends in non-performing loans expected to result from existing conditions), (2) seasoning of the loan portfolio, (3) specific industry conditions affecting portfolio segments, (4) the Corporation's expansion into new markets and (5) the offering of new loan products.

Table 9 summarizes the Corporation's allocation of the allowance for loan losses and percent of loans by category to total loans for each year in the five-year period ended December 31, 2013 (in thousands of dollars):

TABLE 9. ALLOCATION OF ALLOWANCE FOR LOAN LOSSES

Balance at end of period applicable to:	2013	%	2012	%	2011	%	2010	%	2009	%
Commercial and agricultural	$ 1,979	14.6	$ 1,708	15.0	$3,143	17.8	$2,118	18.6	$3,133	19.9
Commercial mortgages	6,243	37.5	4,428	35.9	2,570	33.2	2,575	21.7	3,073	20.7
Residential mortgages	1,517	19.7	1,565	22.4	1,310	24.3	1,302	28.3	1,125	27.3
Consumer loans	3,037	28.2	2,706	26.7	2,193	24.7	2,727	31.4	2,636	32.1
	12,776	100.0	10,407	100.0	9,216	100.0	8,722	100.0	9,967	100.0
Unallocated	-	N/A	26	N/A	443	N/A	776	N/A	-	N/A
Total	$ 12,776	100.0	$10,433	100.0	$9,659	100.0	$9,498	100.0	$9,967	100.0

The allowance for loan losses was $12.8 million at December 31, 2013, up from $10.4 million at December 31, 2012. The ratio of allowance for loan losses to total loans was 1.28% at December 31, 2013, compared to 1.17% at December 31, 2012. The increase in the allowance for loan losses was due principally to the establishment of $0.9 million in additional specific reserves on three commercial loans, loan portfolio growth and allowances for the growth after consideration of the factors discussed above, and higher net charge-offs.

Table 10 summarizes the Corporation's loan loss experience for each year in the five-year period ended December 31, 2013 (in thousands of dollars, except ratio data):

TABLE 10. SUMMARY OF LOAN LOSS EXPERIENCE

	Years Ended December 31,				
	2013	2012	2011	2010	2009
Allowance for loan losses at beginning of year	$ 10,433	$ 9,659	$9,498	$9,967	$9,106
Reclassification of acquired loan discount		124	-	-	-
Charge-offs:					
Commercial and agricultural	186	181	686	817	92
Commercial mortgages	44	335	19	471	297
Real estate mortgages	124	83	67	83	30
Consumer loans	1,082	645	678	795	1,400
Home equity	57	29	48	45	23
Total	1,493	1,273	1,498	2,211	1,842
Recoveries:					
Commercial and agricultural	537	802	423	414	68
Commercial mortgages	98	55	41	15	15
Real estate mortgages	65	-	45	-	-
Consumer loans	375	228	190	188	170
Home Equity	6	10	2	-	-
Total	1,081	1,095	701	617	253
Net charge-offs	412	178	797	1,594	1,589
Provision charged to operations	2,755	828	958	1,125	2,450
Allowance for loan losses at end of year	$ 12,776	$10,433	$9,659	$9,498	$9,967
Ratio of net charge-offs during year to average loans outstanding	.04 %	.02 %	.11 %	.27 %	.27 %
Ratio of allowance for loan losses to total loans outstanding	1.28 %	1.17 %	1.21 %	1.55 %	1.67 %

Net charge-offs for 2013 were $0.4 million compared with $0.2 million for 2012. The ratio of net charge-offs to average loans outstanding was 0.04% for 2013 compared to 0.02% for 2012. The increase in net charge-offs was due primarily to an increase of $0.4 million in consumer loan charge-offs, partially offset by a decline of $0.3 million in commercial mortgage charge-offs.

Other Real Estate Owned

At December 31, 2013, other real estate owned ("OREO") totaled $0.5 million compared to $0.6 million at December 31, 2012.

Other Assets

The $4.3 million increase in other assets was due primarily to an improvement in the funded status of the Corporation's pension plan, partially offset by a decline in prepaid FDIC insurance premiums.

Deposits

Deposits totaled $1.263 billion at December 31, 2013, compared with $1.045 billion at December 31, 2012, an increase of $218.6 million, or 20.9%. The growth was primarily due to $177.7 million from the branch acquisition and $40.9 million in organic deposit growth. At December 31, 2013, demand deposit and money market accounts comprised 65.5% of total deposits compared with 60.7% at December 31, 2012. Sorted by public, commercial and consumer sources, the growth in deposits was due primarily to increases of $154.8 million in consumer accounts, $36.2 million in public funds and $31.4 million in commercial accounts.

In addition to consumer, commercial and public deposits, other sources of funds include brokered deposits. Brokered deposits include funds obtained through brokers, and the Bank's participation in the Certificate of Deposit Account Registry Service ("CDARS") program. The CDARS program involves a network of financial institutions that exchange funds among members in order to ensure FDIC insurance coverage on customer deposits above the single institution limit. Using a sophisticated matching system, funds are exchanged on a dollar-for-dollar basis, so that the equivalent of an original deposit comes back to the originating institution. Deposits obtained through brokers were $5.0 million and $8.8 million as of December 31, 2013 and 2012, respectively. Deposits obtained through the CDARS program were $35.7 million and $8.1 million as of December 31, 2013 and 2012, respectively. The increase in CDARS deposits was due to the Corporation offering the CDARS program to local municipalities during 2013.

The Corporation's deposit strategy is to fund the Bank with stable, low-cost deposits, primarily checking account deposits and other low interest-bearing deposit accounts. A checking account is the driver of a banking relationship and consumers consider the bank where they have their checking account as their primary bank. These customers will typically turn to their primary bank first when in need of other financial services. Strategies that have been developed and implemented to generate these deposits include: (i) acquire deposits by entering new markets through de novo branching, (ii) an annual checking account marketing campaign, (iii) training branch employees to identify and meet client financial needs with Bank products and services, (iv) link business and consumer loans to primary checking account at the Bank, (v) aggressively promote direct deposit of client's payroll checks or benefit checks and (vi) constantly monitor the Corporation's pricing strategies to ensure competitive products and services.

The Corporation also considers brokered deposits to be an element of its deposit strategy and anticipates that it will continue using brokered deposits as a secondary source of funding to support growth.

Information regarding deposits is included in Note 7 to the consolidated financial statements appearing elsewhere in this report.

Borrowings

FHLBNY term advances decreased $2.0 million during 2013. As a result of the increase in deposits, the Corporation decided not to replace FHLBNY advances that matured.

For each of the three years ended December 31, 2013, 2012 and 2011, respectively, the average outstanding balance of borrowings that mature in one year or less did not exceed 30% of shareholders' equity.

Information regarding securities sold under agreements to repurchase and FHLBNY advances is included in notes 8 and 9 to the consolidated financial statements appearing elsewhere in this report.

Liquidity and Capital Resources

Liquidity management involves the ability to meet the cash flow requirements of deposit clients, borrowers, and the operating, investing and financing activities of the Corporation. The Corporation uses a variety of resources to meet its liquidity needs. These include short term investments, cash flow from lending and investing activities, core-deposit growth and non-core funding sources, such as time deposits of $100,000 or more, securities sold under agreements to repurchase and other borrowings.

The Corporation is a member of the FHLBNY which allows it to access borrowings which enhance management's ability to satisfy future liquidity needs. Based on available collateral and current advances outstanding, the Corporation was eligible to borrow up to a total of $73.1 million and $104.5 million at December 31, 2013 and 2012, respectively. The Corporation also had a total of $28.0 million of unsecured lines of credit with four different financial institutions, all of which was available at December 31, 2013 and 2012.

During 2013, cash and cash equivalents increased $11.4 million. The major sources of cash during 2013 included $170.9 million received from the branch acquisition, $22.8 million provided by operating activities, $67.9 million in proceeds from sales, maturities, calls and principal reductions on securities and $40.9 million in organic deposit growth. These proceeds were used primarily to fund purchases of securities totaling $180.5 million, a $101.5 million net increase in loans, payment of cash dividends in the amount of $3.6 million and purchases of fixed assets totaling $3.7 million.

During 2012, cash and cash equivalents decreased $12.7 million. The major sources of cash during 2012 included $24.6 million provided by operating activities, proceeds from sales, maturities, calls and principal reductions on securities totaling $124.5 million and a $46.2 million increase in deposits. These proceeds were used primarily to fund purchases of securities totaling $82.2 million, a $96.6 million net increase in loans, a $16.1 million decrease in FHLBNY term advances, a decrease in securities sold under agreements to repurchase totaling $4.4 million, the payment of cash dividends in the amount of $5.7 million and purchases of fixed assets totaling $3.7 million.

Shareholders' Equity

Total shareholders' equity was $138.6 million at December 31, 2013, compared with $131.1 million at December 31, 2012, an increase of $7.5 million, or 5.7%. The increase was due primarily to net income of $8.7 million and a $3.0 million reduction in accumulated other comprehensive loss, partially offset by declared dividends of $4.8 million. The total shareholders' equity to total assets ratio was 9.39% at December 31, 2013 compared with 10.50% at December 31, 2012. As a result of the branch acquisition, the tangible equity to tangible assets ratio decreased to 7.62% at December 31, 2013, from 8.53% at December 31, 2012.

The Corporation and the Bank are subject to capital adequacy guidelines of the Federal Reserve which establish a framework for the classification of financial holding companies and financial institutions into five categories: well-capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized. As of December 31, 2013, both the Corporation's and the Bank's capital ratios were in excess of those required to be considered well-capitalized under regulatory capital guidelines. A comparison of the Corporation's and the Bank's actual capital ratios to the ratios required to be adequately or well-capitalized at December 31, 2013 and 2012, is included in note 17 to the consolidated financial statements appearing elsewhere in this report. For more information regarding current capital regulations see Part I-"Business-Supervision and Regulation-Regulatory Capital."

Cash dividends declared during 2013 totaled $4.8 million or $1.04 per share compared to $4.6 million or $1.00 per share in 2012 and $4.3 million and $1.00 per share in 2011. Dividends declared during 2013 amounted to 54.7% of net income compared to 41.5% and 41.0% of net income for 2012 and 2011, respectively. Management seeks to continue generating sufficient capital internally, while continuing to pay adequate dividends to the Corporation's shareholders.

When shares of the Corporation become available in the market, we may purchase them after careful consideration of the Corporation's liquidity and capital positions. Purchases may be made from time to time on the open market or in privately negotiated transactions at the discretion of management. On November 16, 2011, the Corporation's Board of Directors approved a one year extension of the stock repurchase program that had been initially approved on November 18, 2009 and extended for one year on November 17, 2010. The extension authorized the purchase of up to 90,000 shares of the Corporation's outstanding common stock, including those shares purchased during the first two years of the plan. From November 18, 2009 through the expiration of this program on November 16, 2012, a total of 68,564 shares were purchased. Under the expired plan in 2012, the Corporation purchased 25,320 shares at an average cost of $24.96 per share totaling $0.6 million. On December 19, 2012, the Board of Directors approved a new stock repurchase plan under which the Corporation may repurchase up to 125,000 shares. During 2013, the Corporation purchased 3,094 shares at a total cost of $93 thousand under the new plan. No shares were purchased under the new plan in 2012.

Off-Balance Sheet Arrangements

In the normal course of operations, the Corporation engages in a variety of financial transactions that, in accordance with GAAP are not recorded in the financial statements. The Corporation is also a party to certain financial instruments with off balance sheet risk such as commitments under standby letters of credit, unused portions of lines of credit and commitments to fund new loans. The Corporation's policy is to record such instruments when funded. These transactions involve, to varying degrees, elements of credit, interest rate and liquidity risk. Such transactions are generally used by the Corporation to manage clients' requests for funding and other client needs.

Table 11 shows the Corporation's off-balance sheet arrangements as of December 31, 2013 (in thousands of dollars):

TABLE 11. COMMITMENT MATURITY BY PERIOD

	Total	Less than 1 Year	1 to 3 Years	3 to 5 Years	More than 5 Years
Standby letters of credit	$ 17,290	$ 13,453	$ 3,446	$ 96	295
Unused portions of lines of credit (1)	131,581	131,581	-	-	-
Commitments to fund new loans	28,943	28,943	-	-	-
Total	$ 177,814	$ 173,977	$ 3,446	$ 96	$ 295

(1) Not included in this total are unused portions of home equity lines of credit, credit card lines and consumer overdraft protection lines of credit, since no contractual maturity dates exist for these types of loans. Commitments to outside parties under these lines of credit were $39,605, $12,925 and $5,141, respectively, at December 31, 2013.

Contractual Obligations

Table 12 shows the Corporation's contractual obligations under long-term agreements as of December 31, 2013 (in thousands of dollars). Note references are to the Notes of the Consolidated Financial Statements:

TABLE 12. CONTRACTUAL OBLIGATIONS

			Payments Due by Period		
	Total	Less than 1 Year	1 to 3 Years	3 to 5 Years	More than 5 Years
Time Deposits (Note 7)	$ 244,491	$ 178,903	$ 53,114	$ 10,740	$ 1,734
Federal Home Loan Bank advances (Note 9)	25,243	5,942	10,000	9,301	-
Securities sold under agreements to repurchase (Note 8)	32,701	12,701	-	20,000	-
Operating leases	11,969	1,665	2,966	2,355	4,983
Other	7,166	1,543	2,704	2,133	786
Total (1)	$ 321,570	$ 200,754	$ 68,784	$ 44,529	$ 7,503

(1) Not included in the above total is the Corporation's obligation regarding the Pension Plan and Other Benefit Plans. Please refer to Part IV Item 15 Note 11 for information regarding these obligations at December 31, 2013.

Results of Operations 2013 vs. 2012

Net Income

Net income for 2013 was $8.7 million, a decrease of $2.3 million, or 20.8%, compared with $11.0 million for 2012. Earnings per share for 2013 was $1.87 compared with $2.38 for 2012. Return on average assets and return on average equity for 2013 were 0.67% and 6.50%, respectively, compared with 0.88% and 8.41%, respectively, for 2012.

The decline in 2013 earnings was due primarily to increases of $1.9 million in the provision for loan losses and $2.6 million in non-interest expense, which included $1.4 million in pre-tax branch acquisition costs. Net interest income decreased $0.2 million in 2013. These items were partially offset by a reduction of $1.6 million in income taxes and an increase of $0.9 million in non-interest income. The increase in non-interest income was due primarily to increases of $0.5 million in Wealth Management Group fee income, $0.5 million in services charges on deposit accounts and a gain of $0.5 million from the branch acquisition. These items were offset by the 2012 pre-tax casualty gain of $0.8 million from insurance reimbursements related to the September 2011 flooding of the Owego and Tioga offices.

Net Interest Income

Net interest income, which is the difference between the income we receive on interest-earning assets, such as loans and securities and the interest we pay on interest-bearing liabilities, such as deposits and borrowings, is the largest contributor to our earnings.

For 2013, net interest income totaled $46.6 million, a slight decrease of $0.2 million, or 0.5%, compared with $46.8 for 2012, and the net interest margin was 3.85% for 2013 compared with 4.07% for 2012. The decline in net interest income was due primarily to margin compression evidenced by a 34 basis point decrease in the yield on interest-earning assets, partially offset by a 16 basis point decline in the cost of funds and an increase of $59.3 million in average earning assets. The decline in net interest margin was due primarily to yields on interest-earning assets decreasing at a faster rate than the cost of interest-bearing liabilities. The decrease in yield on interest-earning assets was attributable to lower loan yields as loans continue to reprice at current market rates. In addition, the Corporation anticipated a decline in the yield on interest-earning assets due in part to its investment of cash from the branch acquisition into investment securities.

For 2013, total average funding liabilities, including non-interest-bearing demand deposits, increased $46.5 million, or 4.2%, to $1.160 billion compared to 2012. The growth was primarily due to increases of $49.6 million in average savings and money market deposits and $18.4 million in demand deposits, partially offset by a decrease of $26.9 million in time deposits. While average interest-bearing liabilities increased $28.1 million, or 3.4%, interest expense decreased $1.2 million, or 22.9%, as the average cost of interest-bearing liabilities decreased 16 basis points to 0.47%.

Provision for Loan Losses

For 2013 the provision for loan loss expense totaled $2.8 million compared to $0.8 million for 2012. The increase was due principally to the establishment of $0.9 million in additional specific reserves on three commercial loans, loan portfolio growth and net charge-offs.

Non-Interest Income

Non-interest income for 2013 was $18.1 million compared with $17.2 million for 2012, an increase of $0.9 million, or 5.2%. The increase was due primarily to a gain of $0.5 million from the branch acquisition and increases of $0.5 million in Wealth Management Group fee income and $0.5 million in service charges on deposit accounts. These items were partially offset by reductions of $0.8 million in casualty gains from insurance reimbursements related to the September 2011 flooding of the Owego and Tioga offices and $0.3 million in net gain on securities transactions.

Current assets under management or administration of the Corporation's Wealth Management Group include investment, trust and retirement-related business lines. The market value of total assets under management or administration in the Wealth Management Group were $1.888 billion at December 31, 2013, compared with $1.735 billion at December 31, 2012, an increase of $153.0 million, or 8.8%. As a result, Wealth Management Group fee income increased for 2013, as the Wealth Management Group's efforts were focused on programs that include a private banking program with financial planning capabilities, to serve the financial needs of high net worth individuals, and an enhanced retirement services program to increase the number of plans under management and fee income.

Non-Interest Expense

Non-interest expense for 2013 was $49.4 million compared with $46.8 million for 2012, an increase of $2.6 million, or 5.6%. Excluding $1.4 million in pre-tax branch acquisition costs from 2013, non-interest expense increased $1.2 million, or 2.7% for 2013. This increase was due primarily to increases of $0.4 million in salaries and wages, $0.3 million in pension and other employee benefits, $0.3 million in net occupancy expense and $0.3 million in data processing costs. These items were partially offset by a decrease of $0.5 million in professional services related to consultant fees.

Included in the increase in salaries and wages was $0.1 million related to the branch acquisition, and the remainder to compensation expense related to merit increases and incentive compensation. The increase in pension and other employee benefits was primarily due to higher pension and retirement costs. The increase in net occupancy was due primarily to higher depreciation and rent expense, both related to the Bank of America branch acquisition. The increase in data processing expenses was primarily due to higher software maintenance fees and telephone data lines related to the branch acquisition.

Income Taxes

Income tax expense for 2013 was $3.8 million compared with $5.4 million for 2012, a decrease of $1.6 million, or 29.0%. Income tax expense reflects an effective tax rate of 30.4% for 2013 compared with 32.8% for 2012, due primarily to lower pre-tax income and an increase in the relative percentage of tax exempt income to pre-tax income.

Results of Operations 2012 vs. 2011

Net Income

Net income for 2012 was $11.0 million, an increase of $0.5 million, or 4.6%, compared with $10.5 million for 2011. Earnings per share for 2012 was $2.38 compared with $2.40 for 2011. Return on average assets and return on average equity for 2012 were 0.88% and 8.41%, respectively, compared with 0.90% and 8.77%, respectively, for 2011.

The improvement in 2012 earnings was due primarily to a $3.0 million increase in net interest income and a $2.2 million decrease in pre-tax one-time merger transaction costs, both related to the FOFC acquisition in April 2011. In addition, the Corporation recognized $0.8 million in pre-tax casualty gains from insurance reimbursements related to the September 2011 flooding of the Owego and Tioga offices. These items were partially offset by increases of $1.8 million in salaries and wages, $0.8 million in pension and other employee benefits, $0.5 million in data processing expenses, $0.5 million in professional services, $0.4 million in income taxes and a $0.8 million reduction in net gains on securities transactions.

Net Interest Income

Net interest income, which is the difference between the income we receive on interest-earning assets, such as loans and securities and the interest we pay on interest-bearing liabilities, such as deposits and borrowings, is the largest contributor to our earnings.

For 2012, net interest income totaled $46.8 million, an increase of $3.0 million, or 6.7%, compared with $43.9 for 2011, and the net interest margin remained level with the prior year at 4.07%. The increase in net interest income reflects a higher level of average earning assets due in large part to the FOFC acquisition, organic growth in the Albany region and a 21 basis point decrease in the cost of average interest-bearing liabilities, partially offset by a 17 basis point decrease in the yield on average earning assets. Average earning assets increased $72.0 million, or 6.7%, as an increase in average loans totaling $103.3 million was partially offset by a $27.1 million decrease in average interest-bearing deposits in other financial institutions. Included in the growth in average loans and investment securities are the Capital Bank division's assets for a full year in 2012 compared with nine months in 2011. Due to the increase in average earning assets, total interest and dividend income increased $1.4 million, or 2.8%, despite a 17 basis point decrease in yield to 4.53%.

For 2012, total average funding liabilities, including non-interest-bearing demand deposits, increased $67.0 million, or 6.4%, to $1.113 billion compared to 2011. The growth was primarily due to an increase of $77.5 million in average deposits, partially offset by a decrease of $10.6 million in borrowings. Average non-interest bearing deposits increased $40.6 million and average interest-bearing deposits increased $36.9 million. The increase in average interest-bearing deposits was reflected principally in a $65.8 million increase in average IMMA balances and a $16.8 million increase in average NOW accounts. These increases were partially offset by a $38.2 million decrease in average time deposits and a $7.5 million decrease in average savings balances. While average interest-bearing liabilities increased $26.3 million, or 3.3%, interest expense decreased $1.5 million, or 22.1%, as the average cost of interest-bearing liabilities decreased 21 basis points to 0.64%.

Provision for Loan Losses

For 2012 the provision for loan loss expense totaled $0.8 million compared to $1.0 million for 2011. The decrease was due principally to the improvement in the volume of non-performing loans, resulting in a reduction in allocations to the allowance for loan losses related to these loans, which was offset in part by loan portfolio growth and allowances for this growth after consideration of the factors discussed above.

Non-Interest Income

Non-interest income for 2012 was $17.2 million compared with $17.5 million for 2011. The slight decline was primarily due to decreases of $0.8 million in net gain on securities transactions and $0.6 million in revenue from the Corporation's equity investment in Cephas Capital Partners, L.P. ("Cephas"). The decrease in revenue from Cephas was due in large part to a gain recognized during the first quarter of 2011 on the exercise of stock warrants held in one of their investments. These items were partially offset by $0.8 million in casualty gains from insurance reimbursements related to the September 2011 flooding of the Owego and Tioga offices and a $0.3 million increase in net gain on sale of loans held for sale.

Current assets under management or administration of the Corporation's Wealth Management Group include investment, trust and retirement-related business lines. However, consistent with the banking industry as a whole, the Wealth Management Group experienced a decline in trust-related business over the last several years while investment and retirement-related business lines have grown. As a result, Wealth Management Group fee income for 2012 had only a small increase compared to 2011. The challenge for the Wealth Management Group is to grow assets under management and fee income under the current weak economic conditions. The Wealth Management Group's efforts will be focused on programs that include a private banking program with financial planning capabilities, to serve the financial needs of high net worth individuals, and an enhanced retirement services program to increase the number of plans under management and fee income.

Non-Interest Expense

Non-interest expense for 2012 was $46.8 million compared with $44.8 million for 2011, an increase of $2.0 million, or 4.6%. Excluding $2.3 million in merger related expenses from 2011, non-interest expense increased $4.3 million, or 10.1% for 2012. This increase was primarily due to increases of $1.8 million in salaries and wages, $0.8 million in pension and other employee benefits, $0.5 million in data processing expenses and $0.5 million in professional services. The increase in salaries and wages was primarily due to the operation of the Capital Bank division for twelve months during 2012 compared with nine months during 2011, and additional compensation expense related to merit increases and incentive compensation. The increase in pension and other employee benefits was primarily due to higher pension costs, health benefits and payroll taxes. The increase in data processing expenses was primarily due to higher hardware and software maintenance fees and check card processing costs that included conversion costs for a new processor. The increase in professional services was due primarily to consultant fees.

Income Taxes

For 2012, a $0.4 million increase in income tax expense reflects a $0.8 million increase in pre-tax income, and an increase in the effective tax rate to 32.8% from 32.3%, due primarily to a decrease in the relative percentage of tax exempt income to pre-tax income.

Table 13 sets forth certain information related to the Corporation's average consolidated balance sheets and its consolidated statements of income for the years indicated and reflects the average yield on assets and average cost of liabilities for the years indicated. For the purpose of the table below, non-accruing loans are included in the daily average loan amounts outstanding. Daily balances were used for average balance computations. Investment securities are stated at amortized cost. No tax equivalent adjustments have been made in calculating yields on obligations of states and political subdivisions.

TABLE 13. AVERAGE BALANCES AND YIELDS

Distribution of Assets, Liabilities and Shareholders' Equity, Interest Rates and Interest Differential Year Ended December 31,

(In thousands of dollars)	2013			2012			2011		
Assets	Average Balance	Interest	Yield/ Rate	Average Balance	Interest	Yield/ Rate	Average Balance	Interest	Yield/Rate
Earning assets:									
Loans	$ 942,908	$45,136	4.79%	$ 844,255	$45,298	5.37%	$ 740,950	$43,181	5.83%
Taxable securities	209,676	4,391	2.09%	214,616	5,357	2.50%	215,481	5,874	2.73%
Tax-exempt securities	42,253	1,101	2.61%	48,653	1,268	2.61%	52,004	1,379	2.65%
Interest-bearing deposits	14,836	36	0.24%	42,884	153	0.36%	69,983	214	0.31%
Total earning assets	1,209,673	50,664	4.19%	1,150,408	52,076	4.53%	1,078,418	50,648	4.70%
Non-earning assets:									
Cash and due from banks	23,739			24,369			22,706		
Premises and equipment, net	25,606			24,806			24,336		
Other assets	46,752			50,854			47,300		
Allowance for loan losses	(11,212)			(10,425)			(9,742)		
AFS adjustment to fair value	11,809			13,713			12,028		
Total	$1,306,367			$1,253,725			$1,175,046		
Liabilities and Shareholders' Equity									
Interest-bearing liabilities:									
Now deposits	$ 96,392	91	0.09%	$ 89,759	95	0.11%	$ 72,953	84	0.11%
Savings and insured money market deposits	462,592	833	0.18%	413,023	828	0.20%	354,746	825	0.23%
Time deposits	229,426	1,426	0.62%	256,291	2,258	0.88%	294,467	3,376	1.15%
Federal Home Loan Bank advances and securities sold under agreements to repurchase	69,498	1,683	2.42%	70,716	2,053	2.90%	81,297	2,448	3.01%
Total interest-bearing liabilities	857,908	4,033	0.47%	829,789	5,234	0.63%	803,463	6,733	0.84%

Non-interest-bearing liabilities:									
Demand deposits	302,046			283,654			243,017		
Other liabilities	12,128			9,163			8,341		
Total liabilities	$1,172,082			$1,122,606			$1,054,821		
Shareholders' equity	134,285			131,119			120,225		
Total	$1,306,367			$1,253,725			$1,175,046		
Net interest income		$46,631			$46,842			$43,915	
Net interest rate spread			3.72%			3.90%			3.86%
Net interest margin			3.85%			4.07%			4.07%

48

CHANGES DUE TO VOLUME AND RATE

Net interest income can be analyzed in terms of the impact of changes in rates and volumes. Table 14 illustrates the extent to which changes in interest rates and in the volume of average interest-earning assets and interest-bearing liabilities have affected the Corporation's interest income and interest expense during the periods indicated. Information is provided in each category with respect to (i) changes attributable to changes in volume (changes in volume multiplied by prior rate); (ii) changes attributable to changes in rates (changes in rates multiplied by prior volume); and (iii) the net changes. For purposes of this table, changes that are not due solely to volume or rate changes have been allocated to these categories based on the respective percentage changes in average volume and rate. Due to the numerous simultaneous volume and rate changes during the periods analyzed, it is not possible to precisely allocate changes between volume and rates. In addition, average earning assets include non-accrual loans and no tax equivalent adjustments were made.

TABLE 14. RATE/VOLUME ANALYSIS OF NET INTEREST INCOME

	2013 vs. 2012 Increase/(Decrease)			2012 vs. 2011 Increase/(Decrease)		
Interest income (in thousands)	Total Change	Due to Volume	Due to Rate	Total Change	Due to Volume	Due to Rate
Loans	$ (162)	$ 4,996	$ (5,158)	$ 2,117	$ 5,716	$ (3,599)
Taxable investment securities	(966)	(121)	(845)	(517)	(24)	(493)
Tax-exempt investment securities	(167)	(167)	-	(111)	(88)	(23)
Interest-bearing deposits	(117)	(79)	(38)	(61)	(93)	32
Total interest income	$ (1,412)	$ 4,629	$ (6,041)	$ 1,428	$ 5,511	$ (4,083)
Interest expense (in thousands)						
Interest-bearing demand deposits	$ (4)	$ 7	$ (11)	$ 11	$ 18	$ (7)
Savings and insured money market deposits	5	94	(89)	3	125	(122)
Time deposits	(833)	(219)	(614)	(1,118)	(402)	(716)
FHLBNY advances and securities sold under agreements to repurchase	(369)	(34)	(335)	(395)	(310)	(85)
Total interest expense	(1,201)	(152)	(1,049)	(1,499)	(569)	(930)
Net interest income	$ (211)	$ 4,781	$ (4,992)	$ 2,927	$ 6,080	$ (3,153)

ADOPTION OF NEW ACCOUNTING STANDARDS

For a discussion of the impact of accounting standards adopted during 2013, please see Note 1 to the Corporation's consolidated financial statements that commence on page F-9.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest Rate Risk

Management considers interest rate risk to be the most significant market risk for the Corporation. Market risk is the risk of loss from adverse changes in market prices and rates. Interest rate risk is the exposure to adverse changes in the net income of the Corporation as a result of changes in interest rates.

The Corporation’s primary earnings source is net interest income, which is affected by changes in the level of interest rates, the relationship between rates, the impact of interest rate fluctuations on asset prepayments, the level and composition of deposits and liabilities, and credit quality of earning assets.

The Corporation’s objectives in its asset and liability management are to maintain a strong, stable net interest margin, to utilize its capital effectively without taking undue risks, to maintain adequate liquidity, and to reduce vulnerability of its operations to changes in interest rates. The Corporation's Asset/Liability Committee (“ALCO”) has the strategic responsibility for setting the policy guidelines on acceptable exposure to interest rate risk. These guidelines contain specific measures and limits regarding the risks, which are monitored on a regular basis. The ALCO is made up of the president and chief executive officer, the chief financial officer, the asset liability management officer, and other officers representing key functions.

Interest rate risk is the risk that net interest income will fluctuate as a result of a change in interest rates. It is the assumption of interest rate risk, along with credit risk, that drives the net interest margin of a financial institution. For that reason, the ALCO has established tolerance limits based upon a 200-basis point change in interest rates, with appropriate floors set for interest-bearing liabilities. At December 31, 2013, it is estimated that an immediate 200-basis point decrease in interest rates would negatively impact the next 12 months net interest income by 10.29% and an immediate 200-basis point increase would negatively impact the next 12 months net interest income by 8.71%. Both are within the Corporation's policy guideline of 15%. Given the overall low level of current interest rates and the unlikely event of a 200-basis point decline from this point, management additionally modeled an immediate 100-basis point decline and an immediate 300-basis point increase in interest rates. When applied, it is estimated these scenarios would result in negative impacts to net interest income of 4.58% and 13.09%, respectively.

A related component of interest rate risk is the expectation that the market value of the Corporation’s capital account will fluctuate with changes in interest rates. This component is a direct corollary to the earnings-impact component: an institution exposed to earnings erosion is also exposed to shrinkage in market value. At December 31, 2013, it is estimated that an immediate 200-basis point decrease in interest rates would negatively impact the market value of the Corporation’s capital account by 6.63% and an immediate 200-basis point increase in interest rates would negatively impact the market value by 5.09%. Both are within the Corporation’s policy guideline of 15%. Management also modeled the impact to the market value of the Corporation’s capital with an immediate 100-basis point decline and an immediate 300-basis point increase in interest rates, based on the current interest rate environment. When applied, it is estimated these scenarios would result in negative impacts to the market value of the Corporation’s capital of 3.44% and 8.02%, respectively.

Management does recognize the need for certain hedging strategies during periods of anticipated higher fluctuations in interest rates and the Funds Management Policy provides for limited use of certain derivatives in asset liability management. These strategies were not employed during 2013.

Credit Risk

The Corporation manages credit risk consistent with state and federal laws governing the making of loans through written policies and procedures; loan review to identify loan problems at the earliest possible time; collection procedures (continued even after a loan is charged off); an adequate allowance for loan losses; and continuing education and training to ensure lending expertise. Diversification by loan product is maintained through offering commercial loans, 1-4 family mortgages, and a full range of consumer loans.

The Corporation monitors its loan portfolio carefully. The Loan Committee of the Corporation's Board of Directors is designated to receive required loan reports, oversee loan policy, and approve loans above authorized individual and Senior Loan Committee lending limits. The Senior Loan Committee, consisting of the President and Chief Executive Officer, Chief Administrative and Risk Officer (non-voting member), business client division manager, retail client division manager, commercial loan manager, consumer loan manager, mortgage loan manager, and the President and commercial loan manager of the Capital Bank division, implements the Board-approved loan policy.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The financial statements listed in Part III, Item 15 are filed as part of this report and appear on pages F-1 through F-57.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

Item 9A. CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures

The Corporation's management, with the participation of our President and Chief Executive Officer, who is the Corporation's principal executive officer, and our Treasurer and Chief Financial Officer, who is the Corporation's principal financial officer, has evaluated the effectiveness of the Corporation's disclosure controls and procedures as of December 31, 2013. Based upon that evaluation, the President and Chief Executive Officer and the Treasurer and Chief Financial Officer have concluded that the Corporation's disclosure controls and procedures are not effective as a result of the material weakness that existed in the Corporation’s internal control over financial reporting as described in Management’s Report on Internal Control over Financial Reporting below.

(b) Management's Report on Internal Control over Financial Reporting

We, as members of management of the Corporation, are responsible for establishing and maintaining adequate internal control over financial reporting. The Corporation's internal control over financial reporting is a process designed to provide reasonable assurance to the Corporation's management and Board of Directors regarding the reliability of financial reporting and the preparation of the Corporation's financial statements for external purposes in accordance with U.S. generally accepted accounting principles. Internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Corporation, (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States of America, and that receipts and expenditures of the Corporation are being made only in accordance with authorizations of management and directors of the Corporation, and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Corporation's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

As of December 31, 2013 management assessed the effectiveness of the Corporation's internal control over financial reporting based on the criteria for effective internal control over financial reporting established in the "1992 Internal Control-Integrated Framework," issued by the Committee of Sponsoring Organizations (COSO) of the Treadway Commission. Based on the assessment, we identified a material weakness in the identification and evaluation of troubled debt restructurings as of December 31, 2013. The process surrounding the identification of troubled debt restructurings is to include the completion of a checklist which guides the identification process for all loans modified, renewed or extended which meet certain credit grade and principal balance criteria. A control to identify all loans which may be subject to a checklist had not been implemented. A key control has been implemented and will be tested for effectiveness in 2014.

This material weakness did not result in a misstatement in the Corporation’s quarterly or annual financial statements for 2013. However, as a result of this material weakness, management has concluded that the Corporation did not maintain effective internal control over financial reporting as of December 31, 2013.

Crowe Horwath LLP, an independent registered public accounting firm, which audited the Corporation's 2013 consolidated financial statements included in this report, has issued an attestation report on the effectiveness of the Corporation's internal control over financial reporting.

(c) Changes in Internal Control over Financial Reporting

Except for the material weakness described above, there have been no changes in the Corporation's internal control over financial reporting during the most recent quarter ended December 31, 2013 that have materially affected, or that are reasonably likely to materially affect, the Corporation's internal control over financial reporting.

(d) Remediation of Material Weakness in Internal Control over Financial Reporting

In response to the material weakness, management will improve its process of identifying and evaluating troubled debt restructurings in order to remediate the material weakness. Currently, management of the Corporation anticipates providing additional guidance and strengthening processes regarding the identification and evaluation of troubled debt restructurings, within our loan underwriting and credit administration functions, and providing additional training to our loan underwriting and credit administration staff.

These improvements are targeted at strengthening the Corporation’s internal control over financial reporting and to remediate the material weakness. The Corporation remains committed to a strong internal control environment.

/s/ Ronald M. Bentley	/s/ Karl F. Krebs
Ronald M. Bentley	Karl F. Krebs
President and Chief Executive Officer	Chief Financial Officer and Treasurer
March 14, 2014	March 14, 2014

Item 9B. OTHER INFORMATION

None.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Information responsive to this Item 10 is incorporated herein by reference to the Corporation's definitive proxy statement for its 2014 Annual Meeting of Shareholders, which will be filed with the SEC within 120 days after the Corporation’s 2013 fiscal year end.

ITEM 11. EXECUTIVE COMPENSATION

Information responsive to this Item 11 is incorporated herein by reference to the Corporation's definitive proxy statement for its 2014 Annual Meeting of Shareholders, which will be filed with the SEC within 120 days after the Corporation’s 2013 fiscal year end.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT, AND RELATED STOCKHOLDER MATTERS

Information responsive to this Item 12 is incorporated herein by reference to the Corporation's definitive proxy statement for its 2014 Annual Meeting of Shareholders, which will be filed with the SEC within 120 days after the Corporation’s 2013 fiscal year end.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

Information responsive to this Item 13 is incorporated herein by reference to the Corporation's definitive proxy statement for its 2014 Annual Meeting of Shareholders, which will be filed with the SEC within 120 days after the Corporation’s 2013 fiscal year end.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

Information responsive to this Item 14 is incorporated herein by reference to the Corporation's definitive proxy statement for its 2014 Annual Meeting of Shareholders, which will be filed with the SEC within 120 days after the Corporation’s 2013 fiscal year end.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a) (1) The following consolidated financial statements of the Corporation appear on pages F-1 through F-57 of this report and are incorporated in Part II, Item 8:

Report of Independent Registered Public Accounting Firm-Crowe Horwath LLP

Consolidated Financial Statements
- Consolidated Balance Sheets as of December 31, 2013 and 2012
- Consolidated Statements of Income for the three years ended December 31, 2013
- Consolidated Statements of Comprehensive Income for the three years ended December 31, 2013
- Consolidated Statements of Shareholders' Equity for the three years ended December 31, 2013
- Consolidated Statements of Cash Flows for the three years ended December 31, 2013
- Notes to Consolidated Financial Statements

(2) Financial statement schedules have been omitted because they are not applicable or the required information is shown in the Consolidated Financial Statements or the Notes thereto under Item 8, "Financial Statements and Supplementary Data".

(b) The following exhibits are either filed with this Form 10-K or are incorporated herein by reference. The Corporation's Securities Exchange Act file number is 000-13888.

Exhibit	The following exhibits are either filed with this Form 10-K or are incorporated herein by reference:
3.1	Certificate of Incorporation of Chemung Financial Corporation dated December 20, 1984. (Filed as Exhibit 3.1 to Registrant's Form 10-K filed with the SEC on March 13, 2008 and incorporated herein by reference).
3.2	Certificate of Amendment to the Certificate of Incorporation of Chemung Financial Corporation, dated March 28, 1988. (Filed as Exhibit 3.2 to Registrant's Form 10-K for the year ended December 31, 2007, filed with the SEC on March 13, 2008 and incorporated herein by reference).
3.3	Certificate of Amendment to the Certificate of Incorporation of Chemung Financial Corporation, dated May 13, 1998. (Filed as Exhibit 3.4 of the Registrant’s Form 10-K for the year ended December 31, 2005 and filed with the SEC on March 15, 2006 and incorporated herein by reference).
3.4	Amended and Restated Bylaws of the Registrant, as amended to February 26, 2014. (Filed as Exhibit 3.1 to the Registrant’s Current Report on Form 8-K filed with the SEC on March 4, 2014 and incorporated herein by reference).
4.1	Specimen Stock Certificate. (Filed as Exhibit 4.1 to Registrant's Form 10-K for the year ended December 31, 2002 and incorporated herein by reference).
10.1	Change of Control Agreement dated September 20, 2006 between Chemung Canal Trust Company and Ronald M. Bentley, President & COO. (Filed as Exhibit 10.1 to Registrant's Form 10-Q for the quarter ended September 30, 2006

	and incorporated herein by reference).
10.2	Executive Severance Agreement dated September 20, 2006 between Chemung Canal Trust Company and Ronald M. Bentley, President & COO. (Filed as Exhibit 10.2 to Registrant's Form 10-Q for the quarter ended September 30, 2006 and incorporated herein by reference).
10.3	Amended and Restated Deferred Directors' Fee Plan. (Filed as Exhibit 10.3 of the Registrant's Form 10-K for the year ended December 31, 2005 and incorporated herein by reference).
10.4	Amended and Restated Chemung Financial Corporation Restricted Stock Plan (Filed as Appendix A to the Registrant's Definitive Proxy Statement on Schedule A filed on April 1, 2013 and incorporated herein by reference).

Exhibit	
10.9	Change of Control Agreement dated August 23, 2007 between Chemung Canal Trust Company and Melinda A. Sartori, Executive Vice President. (Filed as Exhibit 10.9 to Registrant's Form 10-K filed with the SEC on March 13, 2008 and incorporated herein by reference).
10.11	Change of Control Agreement dated January 19, 2011 between Chemung Canal Trust Company and Richard G. Carr, Executive Vice President. (Filed as Exhibit 10.11 to Registrant’s Form 10-K filed with the SEC on March 16, 2011 and incorporated herein by reference).
10.12	Change of Control Agreement dated January 19, 2011 between Chemung Canal Trust Company and Louis C. DiFabio, Executive Vice President. (Filed as Exhibit 10.12 to Registrant’s Form 10-K filed with the SEC on March 16, 2011 and incorporated herein by reference).
10.14	Change of Control Agreement dated April 8, 2011 between Chemung Canal Trust Company and Anders M. Tomson, President Capital Bank Division. (Filed as Exhibit 10.14 to Registrant’s Form 10-Q filed with the SEC on May 13, 2011 and incorporated herein by reference).
10.16	Change of Control Agreement dated November 7, 2011 between Chemung Canal Trust Company and Karen R. Makowski, Executive Vice President and Chief Administration and Risk Officer. (Filed as Exhibit 10.16 to Registrant’s Form 10-K on March 28, 2012 and incorporated herein by reference).
10.17	Change of Control Agreement dated October 16, 2013 between Chemung Canal Trust Company and Karl F. Krebs, Executive Vice President and Chief Financial Officer. (Filed as Exhibit 10.1 to Registrant’s Form 8-K filed with the SEC on October 17, 2013 and incorporated herein by reference).
10.18	Amended and Restated Directors' Compensation Plan (Filed as Appendix A to the Registrant’s Definitive Proxy Statement on Schedule 14A filed on March 30, 2012 and incorporated herein by reference).
10.19	Amended and Restated Incentive Compensation Plan Filed as (Filed as Appendix A to the Registrant’s Definitive Proxy Statement on Schedule 14A filed on March 30, 2012 and incorporated herein by reference).
21	Subsidiaries of the Registrant.*
23	Consent of Crowe Horwath LLP, Independent Registered Public Accounting Firm.*
31.1	Certification of President Chief Executive Officer of the Registrant pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934.*
31.2	Certification of Treasurer and Chief Financial Officer of the Registrant pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934.*
32.1	Certification of President and Chief Executive Officer of the Registrant pursuant to Rule 13a-14(b) under the Securities Exchange Act of 1934 and 19 U.S.C. §1350.*
32.2	Certification of Treasurer and Chief Financial Officer of the Registrant pursuant to Rule 13a-14(b) under the Securities Exchange Act of 1934 and 19 U.S.C. §1350.*
101.INS	Instance Document
101.SCH	XBRL Taxonomy Schema*
101.CAL	XBRL Taxonomy Calculation Linkbase*
101.DEF	XBRL Taxonomy Definition Linkbase*

101.LAB	XBRL Taxonomy Label Linkbase*
101.PRE	XBRL Taxonomy Presentation Linkbase*
	*Filed herewith.

CHEMUNG FINANCIAL CORPORATION

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS
Pages F-1 to F-57

	Page
Report of Independent Registered Public Accounting Firm-Crowe Horwath LLP	F-1
Consolidated Financial Statements	
Consolidated Balance Sheets as of December 31, 2013 and 2012	F-2
Consolidated Statements of Income for the three years ended December 31, 2013	F-3
Consolidated Statements of Comprehensive Income for the three years ended December 31, 2013	F-4
Consolidated Statements of Shareholders' Equity for the three years ended December 31, 2013	F-5
Consolidated Statements of Cash Flows for the three years ended December 31, 2013	F-7
Notes to Consolidated Financial Statements	F-8

Report of Independent Registered Public Accounting Firm

Board of Directors and Shareholders
Chemung Financial Corporation
Elmira, New York

We have audited the accompanying consolidated balance sheets of Chemung Financial Corporation as of December 31, 2013 and 2012, and the related consolidated statements of income, comprehensive income, shareholders' equity and cash flows for each of the years ended December 31, 2013, 2012 and 2011. We also have audited Chemung Financial Corporation's internal control over financial reporting as of December 31, 2013, based on criteria established in the 1992 Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Chemung Financial Corporation's management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting as disclosed in Item 9A. Our responsibility is to express an opinion on these financial statements and an opinion on Chemung Financial Corporation's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of the Company's annual or interim financial statements will not be prevented or detected on a timely basis. The following material weakness has been identified and included in the accompanying Management's Report on Internal Control over Financial Reporting as disclosed in Item 9A. Procedures and controls related to the identification of modified loans as troubled debt restructurings are not operating effectively. The process surrounding the identification of troubled debt restructurings is to include the completion of a checklist which guides the identification process for all loans modified, renewed or extended which meet certain credit grade and principal balance criteria. A control to identify all loans which may be subject to a checklist had not been implemented. This material weakness was considered in determining the nature, timing, and extent of audit tests applied in our audit of the 2013 financial statements, and this matter did not affect our opinion on those financial statements.

In our opinion, because of the effects of the material weakness described above, Chemung Financial Corporation has not maintained effective internal control over financial reporting as of December 31, 2013, based on criteria established in the 1992 Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Chemung Financial Corporation as of December 31, 2013 and 2012, and the results of its operations and its cash flows for the years ended December 31, 2013, 2012 and 2011, in conformity with accounting principles generally accepted in the United States of America.

/s/ Crowe Horwath LLP
Livingston, New Jersey
March 14, 2014

CHEMUNG FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

	YEARS ENDED DECEMBER 31, 2013	2012
ASSETS		
Cash and due from financial institutions	$ 31,600,112	$ 29,239,309
Interest-bearing deposits in other financial institutions	20,009,352	11,001,912
Total cash and cash equivalents	51,609,464	40,241,221
Trading assets, at fair value	366,255	348,241
Securities available for sale, at estimated fair value	346,015,906	239,685,763
Securities held to maturity, estimated fair value of $6,929,549 December 31, 2013 and $6,421,486 at December 31, 2012	6,494,924	5,748,453
Federal Home Loan Bank and Federal Reserve Bank Stock, at cost	4,481,750	4,710,300
Loans, net of deferred origination fees and costs, and unearned income	995,865,764	893,516,941
Allowance for loan losses	(12,775,568)	(10,432,650)
Loans, net	983,090,196	883,084,291
Loans held for sale	694,840	1,057,309
Premises and equipment, net	30,039,174	25,484,385
Goodwill	21,824,443	21,824,443
Other intangible assets, net	6,377,077	5,143,820
Bank owned life insurance	2,795,612	2,711,681
Accrued interest and other assets	22,353,812	18,119,801
Total assets	$ 1,476,143,453	$ 1,248,159,708
LIABILITIES AND SHAREHOLDERS' EQUITY		
Deposits:		
Non-interest-bearing	$ 351,222,057	$ 300,610,463
Interest-bearing	912,147,604	744,123,551
Total deposits	1,263,369,661	1,044,734,014
Securities sold under agreements to repurchase	32,701,223	32,710,650
Federal Home Loan Bank term advances	25,242,628	27,225,363
Dividends payable	1,194,522	-
Accrued interest payable and other liabilities	15,057,425	12,374,744
Total liabilities	1,337,565,459	1,117,044,771

Shareholders' equity:		
Common stock, $.01 par value per share, 10,000,000 shares authorized; 5,310,076 issued at December 31, 2013 and December 31, 2012	53,101	53,101
Additional-paid-in capital	45,398,182	45,357,073
Retained earnings	111,031,089	107,078,182
Treasury stock, at cost (707,674 shares at December 31, 2013; 728,680 shares at December 31, 2012)	(18,059,559)	(18,566,490)
Accumulated other comprehensive income (loss)	155,181	(2,806,929)
Total shareholders' equity	138,577,994	131,114,937
Total liabilities and shareholders' equity	$1,476,143,453	$1,248,159,708

See accompanying notes to consolidated financial statements.

CHEMUNG FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME

	YEARS ENDED DECEMBER 31		
	2013	2012	2011
Interest and Dividend Income:			
Loans, including fees	$45,135,158	$45,297,943	$ 43,180,698
Taxable securities	4,391,292	5,357,179	5,874,019
Tax exempt securities	1,100,494	1,268,242	1,378,753
Interest-bearing deposits	36,285	152,891	214,529
Total interest and dividend income	50,663,229	52,076,255	50,647,999
Interest Expense:			
Deposits	2,349,793	3,181,608	4,284,574
Borrowed funds	824,238	1,058,547	1,073,016
Securities sold under agreements to repurchase	858,479	994,227	1,375,361
Total interest expense	4,032,510	5,234,382	6,732,951
Net interest income	46,630,719	46,841,873	43,915,048
Provision for loan losses	2,754,726	827,567	958,333
Net interest income after provision for loan losses	43,875,993	46,014,306	42,956,715
Other operating income:			
Wealth management group fee income	7,344,045	6,826,976	6,709,685
Service charges on deposit accounts	4,706,137	4,240,908	4,281,808
Net gains on securities transactions	16,379	300,516	1,108,091
Other-than-temporary loss on investment securities:			
Total impairment losses	(29,025)	-	(67,400)
Loss recognized in other comprehensive income	-	-	-
Net impairment loss recognized in earnings	(29,025)	-	(67,400)
Net gain on sales of loans held for sale	502,718	484,006	179,096
Casualty gains	-	790,248	-
Net gains (losses) on sales of other real estate owned	27,695	(44,648)	91,533
Gain from bargain purchase	469,929	-	-
Income from bank owned life insurance	83,931	86,577	88,389
Other	4,954,795	4,503,158	5,071,385
Total other operating income	18,076,604	17,187,741	17,462,587
Other operating expenses:			
Salaries and wages	19,365,106	18,917,724	17,136,433
Pension and other employee benefits	5,939,205	5,623,861	4,796,994
Net occupancy expenses	5,501,492	5,163,865	5,015,936
Furniture and equipment expenses	2,326,134	2,205,166	2,118,544
Data processing expense	4,750,184	4,420,953	3,915,841
Professional services	928,228	1,442,644	949,779
Amortization of intangible assets	921,413	1,046,720	1,041,193
Marketing and advertising expense	1,033,200	1,068,494	1,037,416

Other real estate owned expenses	194,065	328,182	104,829
FDIC insurance	866,053	807,493	967,254
Loan expense	779,405	788,473	607,732
Merger and acquisition related expenses	1,386,789	30,145	2,255,169
Other	5,407,970	4,951,605	4,901,277
Total other operating expenses	49,399,244	46,795,325	44,848,397
Income before income tax expense	12,553,353	16,406,722	15,570,905
Income tax expense	3,822,297	5,384,482	5,033,150
Net income	$ 8,731,056	$ 11,022,240	$ 10,537,755
Weighted average shares outstanding	4,659,685	4,640,912	4,382,843
Basic and diluted earnings per share	$ 1.87	$ 2.38	$ 2.40

See accompanying notes to consolidated financial statements.

CHEMUNG FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	YEARS ENDED DECEMBER 31 2013	2012	2011
Net income	$ 8,731,056	$11,022,240	$10,537,755
Other comprehensive income:			
Unrealized holding (losses) gains on securities available for sale	(3,228,298)	410,834	4,797,422
Reclassification adjustment for other-than-temporary losses realized in net income	29,025	-	-
Reclassification adjustment losses (gains) realized in net income	(16,379)	(300,516)	(1,108,091)
Net unrealized (losses) gains	(3,215,652)	110,318	3,689,331
Tax effect	1,236,097	(74,583)	(1,363,289)
Net of tax amount	(1,979,555)	35,735	2,326,042
Change in funded status of defined benefit pension plan and other benefit plans:			
Net gain (loss) arising during the period	6,486,975	(3,624,214)	(6,908,392)
Reclassification adjustment for amortization of prior service costs	(83,144)	(83,144)	(67,127)
Reclasification adjustment for amortization of net actuarial loss	1,623,567	1,431,064	715,885
Total before tax effect	8,027,398	(2,276,294)	(6,259,634)
Tax effect	(3,085,733)	875,008	2,389,739
Net of tax amount	4,941,665	(1,401,286)	(3,869,895)
Total other comprehensive income (loss)	2,962,110	(1,365,551)	(1,543,853)
Comprehensive income	$ 11,693,166	$ 9,656,689	$ 8,993,902

See accompanying notes to consolidated financial statements.

CHEMUNG FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

	Common Stock	Additional Paid-in Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Total
Balances at December 31, 2010	$ 43,001	$ 22,022,122	$ 94,407,620	$ (19,166,655)	$ 102,475	$ 97,408,563
Net income	-	-	10,537,755	-	-	10,537,755
Other comprehensive loss	-	-	-	-	(1,543,853)	(1,543,853)
Restricted stock awards	-	28,141	-	-	-	28,141
Distribution of 286 shares of treasury stock for directors' deferred compensation plan	-	(7,364)	-	7,310	-	(54)
Distribution of 8,834 shares of treasury stock granted for employee restricted stock awards	-	(226,360)	-	225,350	-	(1,010)
Forfeit of 1,087 shares restricted stock	-	27,762	-	(27,762)	-	-
Restricted stock units for directors' deferred compensation plan	-	80,083	-	-	-	80,083
Cash dividends declared ($1.00 per share)	-	-	(4,316,475)	-	-	(4,316,475)
Distribution of 10,378 shares of treasury stock for directors' compensation	-	(33,831)	-	265,262	-	231,431
Distribution of 2,392 shares of treasury stock for employee compensation	-	(6,140)	-	61,140	-	55,000
Sale of 9,500 shares of treasury stock	-	(25,090)	-	242,610	-	217,520
Purchase of 21,426 shares of treasury stock	-	-	-	(501,299)	-	(501,299)
Issuance of 1,009,942 shares related to FOFC	10,100	23,723,538	-	-	-	23,733,638

merger						
Balances at December 31, 2011	$ 53,101	$ 45,582,861	$ 100,628,900	$ (18,894,044)	$ (1,441,378)	$ 125,929,440
Net income	-	-	11,022,240	-	-	11,022,240
Other comprehensive loss	-	-	-	-	(1,365,551)	(1,365,551)
Restricted stock awards	-	79,510	-	-	-	79,510
Distribution of 3,240 shares of treasury stock for directors' deferred compensation plan	-	(81,747)	-	82,588	-	841
Distribution of 10,760 shares of treasury stock granted for employee restricted stock awards, net	-	(274,196)	-	274,196	-	-
Restricted stock units for directors' deferred compensation plan	-	86,717	-	-	-	86,717
Cash dividends declared ($1.00 per share)	-	-	(4,572,958)	-	-	(4,572,958)
Distribution of 10,238 shares of treasury stock for directors' compensation	-	(28,121)	-	261,069	-	232,948
Distribution of 3,453 shares of treasury stock for employee compensation	-	(8,052)	-	88,052	-	80,000
Sale of 10,100 shares of treasury stock	-	101	-	257,449	-	257,550
Purchase of 25,468 shares of treasury stock	-	-	-	(635,800)	-	(635,800)
Balances at December 31, 2012	$ 53,101	$ 45,357,073	$ 107,078,182	$ (18,566,490)	$ (2,806,929)	$ 131,114,937

CHEMUNG FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(continued)	Common Stock	Additional Paid-in Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Total
Balances at December 31, 2012	$ 53,101	$ 45,357,073	$ 107,078,182	$ (18,566,490)	$ (2,806,929)	$ 131,114,937
Net income	-	-	8,731,056	-	-	8,731,056
Other comprehensive income	-	-	-	-	2,962,110	2,962,110
Restricted stock awards	-	130,920	-	-	-	130,920
Distribution of 3,356 shares of treasury stock for directors' deferred compensation plan	-	(74,623)	-	85,578	-	10,955
Distribution of 8,087 shares of treasury stock granted for employee restricted stock awards, net	-	(206,380)	-	206,380	-	-
Restricted stock units for directors' deferred compensation plan	-	98,815	-	-	-	98,815
Cash dividends declared ($1.04 per share)	-	-	(4,778,149)	-	-	(4,778,149)
Distribution of 7,969 shares of treasury stock for directors' compensation	-	13,896	-	203,050	-	216,946
Distribution of 4,116 shares of treasury stock for employee compensation	-	7,278	-	104,876	-	112,154
Forfeit 1,797 shares of restricted stock	-	60,685	-	(60,685)	-	-

awards						
Sale of 2,369 shares of treasury stock	-	10,518	-	60,362	-	70,880
Purchase of 3,094 shares of treasury stock	-	-	-	(92,630)	-	(92,630)
Balances at December 31, 2013	$ 53,101	$ 45,398,182	$ 111,031,089	$ (18,059,559)	$ 155,181	$ 138,577,994

See accompanying notes to consolidated financial statements.

CHEMUNG FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Years Ended December 31,		
CASH FLOWS FROM OPERATING ACTIVITIES:	2013	2012	2011
Net income	$ 8,731,056	$ 11,022,240	$ 10,537,755
Adjustments to reconcile net income to net cash provided by operating activities:			
Amortization of intangible assets	921,413	1,046,720	1,041,193
Deferred income tax (benefit) expense	(120,590)	646,899	3,416,135
Provision for loan losses	2,754,726	827,567	958,333
Depreciation and amortization of fixed assets	3,236,034	2,946,499	2,861,644
Amortization of premiums on securities, net	2,279,939	1,827,055	1,394,115
Gains on sales of loans held for sale, net	(502,718)	(484,006)	(179,096)
Proceeds from sales of loans held for sale	20,075,670	15,684,266	7,778,633
Loans originated and held for sale	(19,210,483)	(15,862,142)	(7,507,967)
Gain on bargain purchase	(469,929)	-	-
Net (gains) losses on sale of other real estate owned	(27,695)	44,648	(91,533)
Net gains on trading assets	(42,756)	(26,880)	(2,506)
Net gains on securities transactions	(16,379)	(300,516)	(1,108,091)
Net impairment loss recognized on investment securities	29,025	-	67,400
Proceeds from sales of trading assets	111,541	96,498	19,938
Purchase of trading assets	(86,799)	(123,478)	(311,813)
(Increase) decrease in other assets	(6,213,191)	6,083,953	(9,890,546)
Decrease in prepaid FDIC Assessment	1,969,526	732,777	164,744
Decrease in accrued interest payable	(107,535)	(347,519)	(287,822)
Expense related to restricted stock units for directors' deferred compensation plan	98,815	86,717	80,083
Expense related to employee stock compensation	112,154	80,000	55,000
Expense related to employee restricted stock awards	130,920	79,510	28,141
Increase in other liabilities	9,403,504	587,817	231,811
Income from bank owned life insurance	(83,931)	(86,577)	(88,389)
Net cash provided by operating activities	22,972,317	24,562,048	9,167,162

CASH FLOWS FROM INVESTING ACTIVITIES:			
Proceeds from sales and calls of securities available for sale	18,149,995	90,870,086	88,741,210
Proceeds from maturities and principal collected on securities available for sale	44,045,818	29,341,503	31,200,076
Proceeds from maturities and principal collected on securities held to maturity	5,702,678	4,295,975	3,965,483
Purchases of securities available for sale	(174,034,193)	(80,443,763)	(127,405,986)
Purchases of securities held to maturity	(6,449,149)	(1,732,507)	(4,562,281)
Purchase of Federal Home Loan Bank and Federal Reserve Bank stock	(16,124,350)	(26,250)	(1,002,500)
Redemption of Federal Home Loan Bank and Federal Reserve Bank stock	16,352,900	825,300	400,350
Purchases of premises and equipment	(3,709,531)	(3,668,479)	(2,551,969)
Cash paid Fort Orange Financial Corp. acquisition	-	-	(8,137,816)
Cash received Fort Orange Financial Corp. acquisition	-	-	33,284,995
Cash received acquisition of Bank of America branches	173,672,561	-	-
Cash paid Bank of America branches	(2,768,276)	-	-
Proceeds from sale of other real estate owned	155,116	796,446	327,087
Net increase in loans	(101,481,327)	(97,115,130)	(19,322,219)
Net cash used by investing activities	(46,487,758)	(56,856,819)	(5,063,570)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Net increase in demand deposits, interest-bearing demand accounts, savings accounts, and insured money market accounts	67,565,921	86,541,575	55,243,997
Net decrease in time deposits	(27,084,698)	(40,300,400)	(43,578,345)
Net decrease in securities sold under agreements to repurchase	(9,427)	(4,396,192)	(18,236,546)
Repayments of Federal Home Loan Bank long term advances	(1,982,735)	(16,118,555)	(910,246)
Purchase of treasury stock	(92,630)	(635,800)	(501,299)
Sale of treasury stock	70,880	257,550	217,520
Cash dividends paid	(3,583,627)	(5,714,039)	(4,056,597)
Net cash provided (used) by financing activities	34,883,684	19,634,139	(11,821,516)
Net increase (decrease) in cash and cash equivalents	11,368,243	(12,660,632)	(7,717,924)
	40,241,221	52,901,853	60,619,777

Cash and cash equivalents, beginning of period			
Cash and cash equivalents, end of period	$ 51,609,464	$ 40,241,221	$ 52,901,853

Supplemental disclosure of cash flow information:			
Cash paid during the year for:			
Interest	$ 4,162,532	$ 5,642,945	$ 6,782,999
Income Taxes	$ 5,303,670	$ 1,732,411	$ 5,110,847
Supplemental disclosure of non-cash activity:			
Transfer of loans to other real estate owned	$ 102,970	$ 618,302	$ 533,976
Dividends declared, not yet paid	$ 1,194,522	$ -	$ -

See accompanying notes to consolidated financial statements.

CHEMUNG FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2013, 2012 and 2011

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

To assist the reader, the Corporation has provided the following list of commonly used acronyms and abbreviations included in the Notes to Consolidated Financial Statements.

FASB: Financial Accounting Standards Board	OTTI: Other-than-temporary impairment
FDIC: Federal Deposit Insurance Corporation	PCI: Purchased credit impaired
FHLBNY: Federal Home Loan Bank of New York	SEC: Securities and Exchange Commission
GAAP: U.S. generally accepted accounting principles	CDO: Collateralized Debt Obligation

ORGANIZATION

Chemung Financial Corporation (the "Corporation"), through its wholly owned subsidiaries, Chemung Canal Trust Company (the "Bank") and CFS Group, Inc., provides a wide range of banking, financing, fiduciary and other financial services to its clients. The Corporation is subject to the regulations of certain federal and state agencies and undergoes periodic examinations by those regulatory agencies.

BASIS OF PRESENTATION

The accompanying consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America and include the accounts of the Corporation and its subsidiaries. All significant intercompany balances and transactions are eliminated in consolidation.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions based on available information. These estimates and assumptions affect the amounts reported in the financial statements and disclosures provided, and actual results could differ. The allowance for loan losses, fair value of financial instruments, other-than-temporary impairment of investment securities and goodwill and other intangibles are particularly subject to change.

SECURITIES

Management determines the appropriate classification of securities at the time of purchase. If management has the intent and the Corporation has the ability at the time of purchase to hold securities until maturity, they are classified as held to maturity and carried at amortized cost. Securities to be held for indefinite periods of time or not intended to be held to maturity are classified as available for sale and carried at fair value. Unrealized holding gains and losses on securities classified as available for sale are excluded from earnings and are reported as accumulated other comprehensive income (loss) in shareholders' equity, net of the related tax effects, until realized. Realized gains and losses are determined using the specific identification method.

Management evaluates securities for OTTI on at least a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. For securities in an unrealized loss position, management considers the extent and duration of the unrealized loss, and the financial condition and near-term prospects of the issuer. Management also assesses whether it intends to sell, or it is more likely than not that it will be required to sell, a security in an unrealized loss position before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the entire difference between amortized cost and fair value is recognized as impairment through earnings. For debt securities that do not meet the aforementioned criteria, the amount of impairment is split into two components as follows: 1) OTTI related to credit loss, which must be recognized in the income statement and 2) OTTI related to other factors, which is recognized in other comprehensive income. The credit loss is defined as the difference between the present value of the cash flows expected to be collected and the amortized cost basis. For equity securities, the entire amount of impairment is recognized through earnings.

In order to determine OTTI for purchased beneficial interests that, on the purchase date, were not highly rated, the Corporation compares the present value of the remaining cash flows as estimated at the preceding evaluation date to the current expected remaining cash flows. OTTI is deemed to have occurred if there has been an adverse change in the remaining expected future cash flows.

Premiums and discounts are amortized or accreted over the life of the related security as an adjustment of yield using the interest method. Dividend and interest income is recognized when collected.

FEDERAL HOME LOAN BANK AND FEDERAL RESERVE BANK STOCK

The Bank is a member of both the FHLBNY and the FRBNY. FHLBNY members are required to own a certain amount of stock based on the level of borrowings and other factors, while FRBNY members are required to own a certain amount of stock based on a percentage of the Bank’s capital stock and surplus. FHLBNY and FRBNY stock are carried at cost and classified as non-marketable equities and periodically evaluated for impairment based on ultimate recovery of par value. Cash dividends are reported as income.

BANK OWNED LIFE INSURANCE

Bank Owned Life Insurance ("BOLI") is recorded at the amount that can be realized under the insurance contracts at the balance sheet date, which is the cash surrender value adjusted for other charges or other amounts due that are probable at settlement. Changes in the cash surrender value are recorded in other income.

LOANS HELD FOR SALE

Certain mortgage loans are originated with the intent to sell. Loans held for sale are recorded at the lower of cost or fair value in the aggregate. Loans held for sale, as well as the commitments to sell the loans that are originated for sale, are regularly evaluated for changes in fair value. If necessary, a valuation allowance is established with a charge to income for unrealized losses attributable to a change in market rates.

LOANS

Loans are stated at the amount of unpaid principal balance net of deferred origination fees and costs and unearned income. Additionally, recorded investment in loans includes interest receivable on loans. The Corporation has the ability and intent to hold its loans for the foreseeable future. The Corporation’s loan portfolio, including acquired loans, is comprised of the following segments: (i) commercial and agricultural, (ii) commercial mortgages, (iii) residential mortgages, and (iv) consumer loans.

Commercial and agricultural loans primarily consist of loans to small to mid-sized businesses in the Corporation’s market area in a diverse range of industries. These loans are typically made on the basis of the borrower’s ability to make repayment from the cash flow of the borrower’s business. Commercial mortgage loans are generally non-owner occupied commercial properties or owner occupied commercial real estate with larger balances. Repayment of these loans is often dependent upon the successful operation and management of the properties and the businesses occupying the properties, as well as on the collateral securing the loan. Residential mortgage loans are generally made on the basis of the borrower’s ability to make repayment from their employment and other income, but are secured by real property. Consumer loans include home equity lines of credit and home equity loans, which exhibit many of the same characteristics as residential mortgages. Indirect and other consumer loans are typically secured by depreciable assets, such as automobiles or boats, and are dependent on the borrower’s continuing financial stability.

Interest on loans is accrued and credited to operations using the interest method. Past due status is based on the contractual terms of the loan. The accrual of interest is generally discontinued and previously accrued interest is reversed when loans become 90 days delinquent. Loans may also be placed on non-accrual status if management believes such classification is otherwise warranted. All payments received on non accrual loans are applied to principal. Loans are returned to accrual status when they become current as to principal and interest and remain current for a period of six consecutive months or when, in the opinion of management, the Corporation expects to receive all of its original principal and interest. Loan origination fees and certain direct loan origination costs are deferred and amortized over the life of the loan as an adjustment to yield, using the interest method.

ACQUIRED LOANS

Non-Impaired Acquired Loans:

Loans acquired are initially recorded at fair value with no carryover of the related allowance for loan losses. After acquisition, losses beyond those estimated in determining the initial fair value are recognized through the allowance for loan losses. Determining fair value of the loans involves estimating the amount and timing of expected principal and interest cash flows to be collected on the loans and discounting those cash flows at a market interest rate.

Purchased Credit Impaired Loans:

Loans acquired that show evidence of credit deterioration since origination are considered purchased credit impaired loans These loans are recorded at the fair value of the amount paid, such that there is no carryover of the seller's allowance for loan losses.

Such purchased loans are accounted for individually. The Corporation estimates the amount and timing of expected cash flows for each purchased loan and the expected cash flows in excess of amount paid is recorded as interest income over the remaining life of the loan (accretable yield). The excess of the loan's contractual principal and interest over expected cash flows is not recorded (nonaccretable difference).

After acquisition, losses are recognized by an increase in the allowance for loan losses. Over the life of the loan expected cash flows continue to be estimated. If the present value of expected cash flows is less than the carrying amount, a reserve is established. If the present value of expected cash flows is greater than the carrying amount, it is recognized as part of future interest income. These loans are charged against the allowance for loan losses when management believes that the collectability of all or a portion of the principal is unlikely.

TROUBLED DEBT RESTRUCTURINGS

Troubled debt restructuring ("TDR") is a formally renegotiated loan in which the Bank, for economic or legal reasons related to a borrower's financial difficulties, grants a concession to the borrower that would not have been granted to the borrower otherwise. Not all loans that are restructured as a TDR are classified as non-accrual before the restructuring occurs. Restructured loans can convert from non-accrual to accrual status when said loans have demonstrated performance, generally evidenced by six months of payment performance in accordance with the restructured terms, or by the presence of other significant items.

ALLOWANCE FOR LOAN LOSSES

The allowance is an amount that management believes will be adequate to absorb probable incurred losses on existing loans. The allowance is established based on management's evaluation of the probable inherent losses in our portfolio in accordance with GAAP, and is comprised of both specific valuation allowances and general valuation allowances.

A loan is classified as impaired when, based on current information and events, it is probable that the Corporation will be unable to collect both the principal and interest due under the contractual terms of the loan agreement. Specific valuation allowances are established based on management's analyses of individually impaired loans. Factors considered by management in determining impairment include payment status, evaluations of the underlying collateral, expected cash flows, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. If a loan is determined to be impaired and is placed on nonaccrual status, all future payments received are applied to principal and a portion of the allowance is allocated so that the loan is reported, net, at the present value of estimated future cash flows using the loan's existing rate or at the fair value of collateral if repayment is expected solely from the collateral.

The general component covers non-impaired loans and is based on historical loss experience adjusted for current factors. Loans not impaired but classified as substandard and special mention use a historical loss factor on a rolling five year history of net losses. For all other unclassified loans, the historical loss experience is determined by portfolio class and is based on the actual loss history experienced by the Corporation over the most recent two years. This actual loss experience is supplemented with other qualitative factors based on the risks present for each portfolio class. These qualitative factors include consideration of the following: (1) lending policies and procedures, including underwriting standards and collection, charge-off and recovery policies, (2) national and local economic and business conditions and developments, including the condition of various market segments, (3) loan profiles and volume of the portfolio, (4) the experience, ability, and depth of lending management and staff, (5) the volume and severity of past due, classified and watch-list loans, non-accrual loans, troubled debt restructurings, and other modifications (6) the quality of the Bank's loan review system and the degree of oversight by the Bank's Board of Directors, (7) collateral related issues: secured vs. unsecured, type, declining valuation environment and trend of other related factors, (8) the existence and effect of any concentrations of credit, and changes in the level of such concentrations, (9) the effect of external factors, such as competition and legal and regulatory requirements, on the level of estimated credit losses in the Bank's current portfolio and (10) the impact of the global economy.

The allowance for loan losses is increased through a provision for loan losses charged to operations. Loans are charged against the allowance for loan losses when management believes that the collectability of all or a portion of the principal is unlikely. Management's evaluation of the adequacy of the allowance for loan losses is performed on a periodic basis and takes into consideration such factors as the credit risk grade assigned to the loan, historical loan loss experience and review of specific impaired loans. While management uses available information to recognize losses on loans, future additions to the allowance may be necessary based on changes in economic conditions. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Corporation's allowance for loan losses. Such agencies may require the Corporation to recognize additions to the allowance based on their judgments about information available to them at the time of their examination.

PREMISES AND EQUIPMENT

Land is carried at cost, while buildings, equipment, leasehold improvements and furniture are stated at cost less accumulated depreciation and amortization. Depreciation is charged to current operations under the straight-line method over the estimated useful lives of the assets, which range from 15 to 50 years for buildings and from 3 to 10 years for equipment and furniture. Amortization of leasehold improvements and leased equipment is recognized on the straight-line method over the shorter of the lease term or the estimated life of the asset.

OTHER REAL ESTATE

Real estate acquired through foreclosure or deed in lieu of foreclosure is recorded at estimated fair value of the property less estimated costs to dispose at the time of acquisition to establish a new carrying value. Write downs from the carrying value of the loan to estimated fair value which are required at the time of foreclosure are charged to the allowance for loan losses. Subsequent adjustments to the carrying values of such properties resulting from declines in fair value are charged to operations in the period in which the declines occur.

INCOME TAXES

The Corporation files a consolidated tax return. Deferred tax assets and liabilities are recognized for future tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, and for unused tax loss carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates to apply to taxable income in the years in which temporary differences are expected to be recovered or settled, or the tax loss carry forwards are expected to be utilized. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance, if needed, reduces deferred tax assets to the amount expected to be realized.

A tax position is recognized as a benefit only if it is "more likely than not" that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than 50% likely of being realized on examination. For tax positions not meeting the "more likely than not" test, no tax benefit is recorded.

WEALTH MANAGEMENT GROUP FEE INCOME

Assets held in a fiduciary or agency capacity for customers are not included in the accompanying consolidated balance sheets, since such assets are not assets of the Corporation. Wealth Management Group income is recognized on the accrual method as earned based on contractual rates applied to the balances of individual trust accounts. The unaudited market value of trust assets under administration total $1.888 billion at December 31, 2013 and $1.735 billion at December 31, 2012.

POSTRETIREMENT BENEFITS

Pension Plan:

The Chemung Canal Trust Company Pension Plan is a non-contributory defined benefit pension plan. The Pension Plan is a “qualified plan” under the IRS Code and therefore must be funded. Contributions are deposited to the Plan and held in trust. The Plan assets may only be used to pay retirement benefits and eligible plan expenses. The plan was amended such that new employees hired on or after July 10, 2010 will not be eligible to participate in the plan, however, existing participants at that time will continue to accrue benefits. The amendment has resulted in a decrease over time in the future benefit obligations of the plan and the corresponding net periodic benefit cost associated with the plan.

Under the Plan, pension benefits are based upon final average annual compensation where the annual compensation is total base earnings paid plus 401(k) salary deferrals. Bonuses, overtime, commissions and dividends are excluded. The normal retirement benefit equals 1.2% of final average compensation (highest consecutive five years of annual compensation in the prior ten years) times years of service (up to a maximum of 25 years), plus 1% of average monthly compensation for each additional year of service (up to a maximum of 10 years), plus .65% of average monthly compensation in excess of covered compensation for each year of credited service up to 35 years. Covered compensation is the average of the social security taxable wage bases in effect for the 35 year period prior to normal social security retirement age. Compensation for purposes of determining benefits under the Plan is reviewed annually.

Defined Contribution Profit Sharing, Savings and Investment Plan:

The Corporation also sponsors a 401(K) defined contribution profit sharing, savings and investment plan which covers all eligible employees with a minimum of 1,000 hours of annual service. The Corporation makes non-discretionary contributions and discretionary matching and profit sharing contributions to the plan based on the financial results of the Corporation. The plan's assets consist of Chemung Financial Corporation common stock, as well as other common and preferred stocks, U.S. Government securities, corporate bonds and notes, and mutual funds. The plan’s expense is the amount of non-discretionary contributions and discretionary matching and profit sharing contributions, and is charged to other expenses in the consolidated statements of income.

Defined Benefit Health Care Plan:

The Corporation sponsors a defined benefit health care plan that provides postretirement medical benefits to employees who meet minimum age and service requirements. This plan was amended effective July 1, 2006. Prior to this amendment, all retirees age 55 or older were eligible for coverage under the Corporation's self-insured health care plan, contributing 40% of the cost of the coverage. Under the amended plan, coverage for Medicare eligible retirees who reside in the Central New York geographic area is provided under a group sponsored plan with Excellus BlueCross BlueShield called Medicare Blue PPO, with the retiree paying 100% of the premium. Excellus BlueCross BlueShield assumes full liability for the payment of health care benefits incurred after July 1, 2006. Current Medicare eligible retirees who reside outside of the Central New York geographic area were eligible for coverage under the Corporation's self insurance plan thru December 31, 2009, contributing 50% of the cost of coverage. Effective January 1, 2010, these out of area retirees were eligible for coverage under a Medicare Supplement Plan C administered by Excellus BlueCross BlueShield, contributing 50% of the premium. Current and future retirees between the ages of 55 and 65, will continue to be eligible for coverage under the Corporation's self insured plan, contributing 50% of the cost of the coverage. Employees who retire after July 1, 2006, and become Medicare eligible will only have access to the Medicare Blue PPO plan. Additionally, effective July 1, 2006, dental benefits were eliminated for all retirees. The cost of the plan is based on actuarial computations of current and future benefits for employees, and is charged to other operating expenses in the consolidated statements of income.

Executive Supplemental Pension Plan:

U.S. laws place limitations on compensation amounts that may be included under the Pension Plan. The Executive Supplemental Pension Plan is provided to executives in order to produce total retirement benefits, as a percentage of compensation that is comparable to employees whose compensation is not restricted by the annual compensation limit. Pension amounts, which exceed the applicable Internal Revenue Service code limitations, will be paid under the Executive Supplemental Pension Plan.

The Executive Supplemental Pension Plan is a “non-qualified plan” under the Internal Revenue Service Code. Contributions to the Plan are not held in trust; therefore, they may be subject to the claims of creditors in the event of bankruptcy or insolvency. When payments come due under the Plan, cash is distributed from general assets. The cost of the plan is based on actuarial computations of current and future benefits for executives, and is charged to other operating expense in the consolidated statements of income.

Defined Contribution Supplemental Executive Retirement Plan:

The Defined Contribution Supplemental Executive Retirement Plan is provided to certain executives to motivate and retain key management employees by providing a nonqualified retirement benefit that is payable at retirement, disability, death and certain other events. The Defined Contribution Supplemental Executive Retirement Plan will deliver a retirement benefit comparable to that received by other executive officers participating in the bank’s Defined Benefit Plan.

The Supplemental Executive Retirement Plan is intended to be an unfunded plan maintained primarily for the purpose of providing deferred compensation benefits for a select group of management or highly compensated employees under Sections 201(2), 301(a)(3) and 401(a)(1) of the Employee Retirement Income Security Act of 1974. The plan’s expense is the Corporation’s annual contribution plus interest credits.

STOCK-BASED COMPENSATION

Restricted Stock Plan:

The Restricted Stock Plan, in effect as of June 16, 2010, is designed to align the interests of the Corporation's executives and senior managers with the interests of the Corporation and its shareholders, to ensure the Corporation's compensation practices are competitive and comparable with those of its peers, and to promote the retention of select management-level employees. Under the terms of the Plan, the Corporation may make discretionary grants of restricted shares of the Corporation's common stock to or for the benefit of employees selected to participate in the Plan. Each officer of the Corporation, other than the Corporation's chief executive officer, is eligible to participate in the Plan. Awards are based on the performance, responsibility and contributions of the employee and are targeted at an average of the peer group. The maximum number of shares of the Corporation's common stock that may be awarded as restricted shares to Plan participants may not exceed fifteen thousand (15,000) per calendar year. Twenty percent of the restricted stock awarded to a participant vests each year commencing with the first anniversary date of the award and is 100 percent vested on the fifth anniversary date. Except in the case of the participant's death, disability, or in the event of a change in control, the participant's unvested shares of unrestricted stock will be forfeited if the participant leaves the employ of the Corporation or the Bank, with or without cause, or if the participant retires prior to attainment of age 65. The plan's expense is recognized as compensation expense ratably over the vesting period for the fair value of the award, measured at the grant date.

Deferred Directors Fee Plan:

A Deferred Directors Fee Plan for non-employee directors provides that directors may elect to defer receipt of all or any part of their fees. Deferrals are either credited with interest compounded quarterly at the Applicable Federal Rate for short-term debt instruments or converted to units, which appreciate or depreciate, as would an actual share of the Corporation's common stock purchased on the deferral date. Cash deferrals will be paid into an interest bearing account and paid in cash. Units will be paid in shares of common stock. All directors' fees are charged to other operating expense in the consolidated statements of income.

Directors' Compensation Plan:

The purpose of the Directors' Compensation Plan is to enable the Corporation to attract and retain persons of exceptional ability to serve as directors and stockholders in enhancing the value of the common stock of the Corporation. The Plan was originally established to provide for the cash payment of an annual retainer and fees to non-employee directors serving on the Board of Directors of the Corporation and the Bank. The Plan was subsequently amended to provide: (i) payment of additional compensation to each non-employee director in shares of the Corporation's common stock in an amount equal to the total cash compensation earned by each non-employee director during the year for service on the Board of Directors of each of the Corporation and the Bank, and for each year of service thereafter, to be distributed from treasury shares in January of the following calendar year; and (ii) payment to the President and CEO of the Corporation and the Bank for his service on the Boards of Directors of the Corporation and the Bank in an amount equal in value to the average cash compensation awarded to non-employee directors who have served twelve (12) months of the previous year. The maximum number of shares of Corporation's common stock that may be granted under the Plan may not exceed twenty thousand (20,000) per year. The Plan was amended, effective January 1, 2012, to provide that the value of a share of common stock granted under the Plan shall be determined as the average of the closing prices of a share of common stock as quoted on the applicable established securities market for each of the prior thirty (30) trading days ending on December 31st of the calendar year. The cost of all cash and stock compensation is charged to other operating expenses in the consolidated statements of income.

Incentive Compensation Plan:

The Incentive Compensation Plan replaces the President and CEO Bonus Plan that was in effect prior to January 1, 2012. The purpose of the Incentive Compensation Plan is to attract and retain highly qualified officers and key employees, and to motivate such persons to serve the Corporation and the Bank and to expend maximum effort to improve the business results and earnings of the Corporation by providing to such persons an opportunity to acquire or increase a direct proprietary interest in the operations and future success of the Corporation. To this end, the Incentive Compensation Plan provides for the discretionary grant of cash and/or unrestricted stock, i.e., common stock of the Corporation that is free of any restrictions, such as restrictions on transferability, to select officers and key employees as designated by the Board in its sole discretion. The maximum number of shares that can be awarded as unrestricted stock under the Incentive Compensation Plan to any individual is ten thousand (10,000) per calendar year; and the maximum amount that may be earned in cash as an Incentive Award in any calendar year by any individual is $300,000. The right of any eligible employee to receive a grant of an incentive award, whether in the form of cash or unrestricted stock, is subject to performance standards that are specified by either the Compensation Committee or the Board. The cost of all cash and unrestricted stock compensation is charged to other operating expenses in the consolidated statements of income.

Non-qualified Deferred Compensation Plan:

The Deferred Compensation Plan allows a select group of management and employees to defer all or a portion of their annual compensation to a future date. Eligible employees are generally highly compensated employees and are designated by the Board from time to time. Investments in the plan are recorded as trading assets and deferred amounts are an unfunded liability of the Corporation. The plan requires deferral elections be made before the beginning of the calendar year during which the participant will perform the services to which the compensation relates. Participants in the Plan are required to elect a form of distribution, either lump sum payment or annual installments not to exceed ten years, and a time of distribution, either a specified age or a specified date. The terms and conditions for the deferral of compensation are subject to the provisions of 409A of the IRS Code. The income from investments and cost of the plan are recorded as other operating income and other operating expenses, respectively, in the consolidated statements of income.

GOODWILL AND INTANGIBLE ASSETS

Goodwill resulting from business combinations prior to January 1, 2009 represents the excess of the purchase price over the fair value of the net assets of businesses acquired. Goodwill resulting from business combinations after January 1, 2009, is generally determined as the excess of the fair value of the consideration transferred, plus the fair value of any noncontrolling interests in the acquiree, over the fair value of the net assets acquired and liabilities assumed as of the acquisition date. Goodwill and intangible assets acquired in a purchase business combination and determined to have an indefinite useful life are not amortized, but tested for impairment at least annually. The Corporation has selected December 31 as the date to perform the annual impairment test. Goodwill is the only intangible asset with an indefinite life on our balance sheet. Intangible assets with definite useful lives are amortized over their estimated useful lives to their estimated residual values. The balances are reviewed for impairment on an ongoing basis or whenever events or changes in business circumstances warrant a review of the carrying value. If impairment is determined to exist, the related write-down of the intangible asset's carrying value is charged to operations. Based on these impairment reviews, the Corporation determined that goodwill and other intangible assets were not impaired at December 31, 2013.

The Corporation's intangible assets with definite useful lives resulted from the purchase of the trust business of Partners Trust Bank in May of 2007, the acquisition of three former M&T Bank branch offices in March 2008, the acquisition of Canton Bancorp, Inc. in May 2009, the acquisition of Fort Orange Financial Corp. in April 2011 and the acquisition of six branches of Bank of America in November of 2013, with balances of $2,719,873, $86,862, $17,547, $1,443,014 and $2,109,781, respectively, at December 31, 2013. The trust business intangible is being amortized to expense over the expected useful life of 15 years. The identifiable core deposit and customer relationship intangibles related to the M&T branch offices, and Canton Bancorp, Inc. acquisitions are being amortized to expense using a 7.25 year accelerated method. The identifiable core deposit related to the branch offices in the Bank of America acquisition is being amortized to expense using a 7 year accelerated method. The identifiable core deposit intangible related to the FOFC acquisition is being amortized using a 10 year sum-of-the-years digits method.

EARNINGS PER COMMON SHARE

Basic earnings per share is net income divided by the weighted average number of common shares outstanding during the period. Issuable shares including those related to directors' restricted stock units and directors' stock compensation are considered outstanding and are included in the computation of basic earnings per share as they are earned. All outstanding unvested share based payment awards that contain rights to nonforfeitable dividends are considered participating securities for this calculation. Restricted stock awards are grants of participating securities. The impact of the participating securities on earnings per share is not material. Earnings per share information is adjusted to present comparative results for stock splits and stock dividends that occur.

COMPREHENSIVE INCOME

Comprehensive income consists of net income and other comprehensive income. Other comprehensive income includes unrealized gains and losses on securities available for sale and changes in the funded status of the Corporation's defined benefit pension plan and other benefit plans, net of the related tax effect, which are also recognized as separate components of equity.

CASH AND CASH EQUIVALENTS

Cash and cash equivalents include cash and amounts due from banks and interest-bearing deposits with other financial institutions.

TRADING ASSETS

Securities that are held to fund a non-qualified deferred compensation plan are recorded at fair value with changes in fair value included in earnings.

SECURITIES SOLD UNDER AGREEMENTS TO REPURCHASE

The Corporation enters into sales of securities under agreements to repurchase. The agreements are treated as financings, and the obligations to repurchase securities sold are reflected as liabilities in the consolidated balance sheets. The amount of the securities underlying the agreements continues to be carried in the Corporation's securities portfolio. The Corporation has agreed to repurchase securities identical to those sold. The securities underlying the agreements are under the Corporation's control.

OTHER FINANCIAL INSTRUMENTS

The Corporation is a party to certain other financial instruments with off-balance sheet risk such as unused portions of lines of credit and commitments to fund new loans. The Corporation's policy is to record such instruments when funded.

SEGMENT REPORTING

The Corporation has identified separate operating segments and internal financial information is primarily reported and aggregated in two lines of business, banking and wealth management services.

RECLASSIFICATION

Amounts in the prior years' consolidated financial statements are reclassified whenever necessary to conform with the current year's presentation.

SUBSEQUENT EVENTS

The Corporation owned one CDO consisting of a pool of trust preferred securities at December 31, 2013. This CDO was liquidated and the Corporation will record in the other operating income category approximately $0.5 million during the first quarter of 2014. The Corporation does not own any other CDO's in its investment securities portfolio.

ADOPTION OF NEW ACCOUNTING STANDARDS

In February 2013, the FASB issued Accounting Standards Update ("ASU") No. 2013-02, "Comprehensive Income (Topic 220) – Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income." ASU 2013-02 amends recent guidance related to the reporting of comprehensive income to enhance the transparency of the reporting of reclassifications out of accumulated other comprehensive income. ASU 2013-02 became effective for the Corporation on January 1, 2013 and did not have a material impact on the Corporation's financial statements. The additional disclosures are included in Note 18 Accumulated Other Comprehensive Income or Loss.

(2) RESTRICTIONS ON CASH AND DUE FROM BANK ACCOUNTS

The Corporation was in compliance with the reserve requirement with the Federal Reserve Bank of New York as of December 31, 2013.

The Corporation also maintains a pre-funded settlement account with a financial institution in the amount of $1,213,000 for electronic funds transaction settlement purposes at December 31, 2013.

(3) SECURITIES

Amortized cost and estimated fair value of securities available for sale at December 31, 2013 and 2012 are as follows:

	2013		2012	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Obligations of U.S. Government and U.S. Government sponsored enterprises	$ 187,098,006	$ 188,106,208	$ 138,041,393	$ 141,591,214
Mortgage-backed securities, residential	104,068,981	104,356,521	29,591,883	31,515,249
Collateralized mortgage obligations	1,000,743	1,014,876	3,494,642	3,543,360
Obligations of states and political subdivisions	37,339,530	38,376,222	39,174,595	40,814,722
Corporate bonds and notes	2,878,813	2,945,807	11,412,167	11,651,635
SBA loan pools	1,470,513	1,487,579	1,682,736	1,724,140
Trust preferred securities	1,898,047	2,033,594	2,519,379	2,470,913
Corporate stocks	444,452	7,695,099	736,495	6,374,530
Total	$ 336,199,085	$ 346,015,906	$ 226,653,290	$ 239,685,763

Gross unrealized gains and losses on securities available for sale at December 31, 2013 and 2012, were as follows:

	2013		2012	
	Unrealized Gains	Unrealized Losses	Unrealized Gains	Unrealized Losses
Obligations of U.S. Government and U.S. Government sponsored enterprises	$ 1,914,660	$ 906,458	$ 3,549,821	$ -
Mortgage-backed securities, residential	1,037,343	749,803	1,923,366	-
Collateralized mortgage obligations	14,133	-	48,718	-
Obligations of states and political subdivisions	1,059,007	22,315	1,641,510	1,383
Corporate bonds and notes	75,672	8,678	239,468	-
SBA loan pools	17,066	-	41,404	-
Trust preferred securities	135,547	-	134,959	183,425
Corporate stocks	7,252,615	1,968	5,645,753	7,718
Total	$ 11,506,043	$ 1,689,222	$ 13,224,999	$ 192,526

The amortized cost and estimated fair value of debt securities available for sale are shown below by expected maturity. Expected maturities may differ from contractual maturities if borrowers have the right to call or prepay obligations with or without call or prepayment penalties. Securities not due at a single maturity date are shown separately:

	December 31, 2013	
	Amortized Cost	Fair Value
Within One Year	$ 23,420,022	$ 23,680,095
After One, But Within Five Years	188,131,675	190,334,668
After Five, But Within Ten Years	17,662,699	17,447,068
After Ten Years	-	-
Mortgage-backed securities, residential	104,068,981	104,356,521
Collateralized mortgage obligations	1,000,743	1,014,876
SBA loan pools	1,470,513	1,487,579
Total	$ 335,754,633	$ 338,320,807

Actual maturities may differ from contractual maturities above because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

The proceeds from sales and calls of securities resulting in gains or losses are listed below:

	2013	2012	2011
Proceeds	$ 2,649,993	$ 26,210,087	$ 35,741,211
Gross gains	$ 16,379	$ 300,516	$ 1,108,091
Tax expense	$ 6,296	$ 115,518	$ 423,191

Amortized cost and estimated fair value of securities held to maturity at December 31, 2013 and 2012 are as follows:

	2013		2012	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Obligations of states and political subdivisions	$ 5,471,505	$ 5,890,122	$ 5,748,453	$ 6,421,486
Time Deposits with other financial institutions	1,023,419	1,039,427	-	-
	$ 6,494,924	$ 6,929,549	$ 5,748,453	$ 6,421,486

Gross unrealized gains and losses on securities held to maturity at December 31, 2013 and 2012, were as follows:

	2013		2012	
	Unrealized Gains	Unrealized Losses	Unrealized Gains	Unrealized Losses
Obligations of states and political subdivisions	$ 418,617	$ -	$ 673,033	$ -
Time deposits with other financial institutions	16,008	-	-	-
Total	$ 434,625	$ -	$ 673,033	$ -

There were no sales of securities held to maturity in 2013 or 2012.

The contractual maturity of securities held to maturity is as follows at December 31, 2013:

	December 31, 2013	
	Amortized Cost	Fair Value
Within One Year	$ 2,361,713	$ 2,394,183
After One, But Within Five Years	2,841,351	3,052,594
After Five, But Within Ten Years	1,291,860	1,482,772
After Ten Years	-	-
Total	$ 6,494,924	$ 6,929,549

The following table summarizes the investment securities available for sale with unrealized losses at December 31, 2013 and December 31, 2012 by aggregated major security type and length of time in a continuous unrealized position:

2013	Less than 12 months		12 months or longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Obligations of U.S. Government and U.S. Government sponsored enterprises	$ 83,839,910	$ 867,495	$ 1,978,200	$ 38,963	$ 85,818,110	$ 906,458
Mortgage-backed securities, residential	63,115,382	749,803	-	-	63,115,382	749,803
Obligations of states and political subdivisions	4,588,521	22,315	-	-	4,588,521	22,315
Corporate bonds and notes	237,792	8,678	-	-	237,792	8,678

Corporate stocks	-	-	1,669	1,968	1,669	1,968
Total temporarily impaired securities	$ 151,781,605	$ 1,648,291	$ 1,979,869	$ 40,931	$ 153,761,474	$ 1,689,222

2012	Less than 12 months Fair Value	Unrealized Losses	12 months or longer Fair Value	Unrealized Losses	Total Fair Value	Unrealized Losses
Obligations of states and political subdivisions	$ -	$ -	$ 430,166	$ 1,383	$ 430,166	$ 1,383
Trust preferred securities	-	-	445,600	183,425	445,600	183,425
Corporate stocks	-	-	45,912	7,718	45,912	7,718
Total temporarily impaired securities	$ -	$ -	$ 921,678	$ 192,526	$ 921,678	$ 192,526

Other-Than-Temporary-Impairment

As of December 31, 2013, the majority of the Corporation's unrealized losses in the investment securities portfolio related to obligations of U.S. Government and U.S. Government sponsored enterprises and mortgage-backed securities. Because the decline in fair value is attributable to changes in interest rates and not credit quality, and because the Corporation does not have the intent to sell these securities and it is not likely that it will be required to sell these securities before their anticipated recovery, the Corporation does not consider these securities to be other-than-temporarily impaired at December 31, 2013.

During the fourth quarter of 2013, the Corporation sold one CDO consisting of a pool of trust preferred securities that had an amortized cost of $600,000. Total proceeds from the sale of this CDO was $600,000 resulting in no gains or losses. The Corporation recognized $29,025 of additional credit loss in OTTI during 2013. This CDO was sold in light of the uncertainty surrounding the recently released rules contained in the "Volcker Rule" regarding the ability of banks to hold these types of securities and based on current market conditions.

The table below presents a roll forward of the cumulative credit losses recognized in earnings for the periods ended December 31, 2013, 2012 and 2013:

	2013	2012	2011
Beginning balance, January 1,	$ 3,506,073	$ 3,506,073	$ 3,438,673
Amounts related to credit loss for which other-than-temporary impairment was not previously recognized	-	-	-
Additions/Subtractions:			
Amounts related to securities for which the company intends to sell or that it will be more likely than not that the company will be required to sell prior to recovery of amortized cost basis	-	-	-
Reductions for increase in cash flows expected to be collected that are recognized over the remaining life of the security	-	-	-
Reductions for previous credit losses realized on securities sold during the year	(1,596,396)	-	-
Increases to the amount related to the credit loss for which other-than-temporary impairment was previously recognized	29,025	-	67,400
Ending balance, December 31,	$ 1,938,702	$ 3,506,073	$ 3,506,073

The remaining cumulative credit loss balance relates to one CDO, which was liquidated during the first quarter of 2014.

The fair value of securities pledged to secure public funds on deposit or for other purposes as required by law was $188,875,494 at December 31, 2013 and $212,257,614 at December 31, 2012.

The table below shows the securities pledged to secure securities sold under agreements to repurchase at December 31, 2013 and 2012:

	2013		2012	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Obligations of U.S. Government and U. S. Government sponsored enterprises	$ 33,745,835	$ 34,369,411	$ 31,888,493	$ 32,812,885
Mortgage-backed securities, residential	11,802,122	12,364,885	16,503,983	17,575,852
Collateralized mortgage obligations	204,842	207,366	756,542	770,625
Total	$ 45,752,799	$ 46,941,662	$ 49,149,018	$ 51,159,362

There are no securities of a single issuer (other than securities of U.S. Government sponsored enterprises) that exceed 10% of shareholders' equity at December 31, 2013 or 2012.

The Corporation has an equity investment in Cephas Capital Partners, L.P. This small business investment company was established for the purpose of providing financing to small businesses in market areas served by the Corporation, including minority-owned small businesses and those that are anticipated to create jobs for the low to moderate income levels in the targeted areas. As of December 31, 2013 and 2012, these investments totaled $956,626 and $1,757,252, respectively, are included in other assets, and are accounted for under the equity method of accounting.

(4) LOANS AND ALLOWANCE FOR LOAN LOSSES

The composition of the loan portfolio, net of deferred origination fees and cost, and unearned income is summarized as follows:

	December 31, 2013	December 31, 2012
Commercial and agricultural:		
Commercial and industrial	$ 144,786,585	$ 133,154,615
Agricultural	575,670	696,666
Commercial mortgages:		
Construction	27,440,372	43,269,303
Commercial mortgages	345,706,661	276,928,123
Residential mortgages	195,996,599	200,475,097
Consumer loans:		
Credit cards	1,756,414	1,851,145
Home equity lines and loans	95,905,130	87,045,421
Indirect consumer loans	164,845,874	130,573,200
Direct consumer loans	18,852,459	19,523,371
Total loans, net of deferred origination fees and costs, and unearned income	$ 995,865,764	$ 893,516,941
Interest receivable on loans	2,597,301	2,383,998
Total recorded investment in loans	$ 998,463,065	$ 895,900,939

Residential mortgages held for sale as of December 31, 2013 and 2012 totaling $694,840 and $1,057,309, respectively, are not included in the above table.

Residential mortgages totaling $145,107,384 at December 31, 2013 and $142,278,166 at December 31, 2012 were pledged under a blanket collateral agreement for the Corporation's line of credit with the FHLBNY.

The Corporation's concentrations of credit risk by loan type are reflected in the preceding table. The concentrations of credit risk with standby letters of credit, committed lines of credit and commitments to originate new loans generally follow the loan classifications in the table above.

The following tables present the activity in the allowance for loan losses by portfolio segment for the years ending December 31, 2013, 2012 and 2011, respectively:

	December 31, 2013					
Allowance for loan losses	Commercial, and Agricultural	Commercial Mortgages	Residential Mortgages	Consumer Loans	Unallocated	Total
Beginning balance:	$ 1,707,596	$ 4,427,698	$ 1,565,571	$ 2,705,639	$ 26,146	$ 10,432,650
Charge Offs:	(186,045)	(44,049)	(124,277)	(1,139,061)	-	(1,493,432)
Recoveries:	537,476	97,953	65,180	381,015	-	1,081,624
	351,431	53,904	(59,097)	(758,046)	-	(411,808)

Net recoveries (charge offs)						
Provision	(80,338)	1,761,394	10,418	1,089,398	(26,146)	2,754,726
Ending balance	$ 1,978,689	$ 6,242,996	$ 1,516,892	$ 3,036,991	$ -	$ 12,775,568

	December 31, 2012					
Allowance for loan losses	Commercial, and Agricultural	Commercial Mortgages	Residential Mortgages	Consumer Loans	Unallocated	Total
Beginning balance:	$ 3,143,373	$ 2,570,149	$ 1,309,649	$ 2,192,729	$ 443,420	$ 9,659,320
Reclassification of acquired loan discount	73,229	50,331	-	-	-	123,560
Charge Offs:	(180,999)	(335,093)	(82,442)	(673,885)	-	(1,272,419)
Recoveries:	802,056	54,637	-	237,929	-	1,094,622
Net recoveries (charge offs)	621,057	(280,456)	(82,442)	(435,956)	-	(177,797)
Provision	(2,130,063)	2,087,674	338,364	948,866	(417,274)	827,567
Ending balance	$ 1,707,596	$ 4,427,698	$ 1,565,571	$ 2,705,639	$ 26,146	$ 10,432,650

Allowance for loan losses	Commercial, and Agricultural	Commercial Mortgages	Residential Mortgages	Consumer Loans	Unallocated	Total
			December 31, 2011			
Beginning balance:	$ 2,118,299	$ 2,575,058	$ 1,301,780	$ 2,727,022	$ 775,972	$ 9,498,131
Charge Offs:	(686,192)	(19,206)	(67,333)	(725,826)	-	(1,498,557)
Recoveries:	423,422	40,717	44,953	192,321	-	701,413
Net (charge offs) recoveries	(262,770)	21,511	(22,380)	(533,505)	-	(797,144)
Provision	1,287,844	(26,420)	30,249	(788)	(332,552)	958,333
Ending balance	$ 3,143,373	$ 2,570,149	$ 1,309,649	$ 2,192,729	$ 443,420	$ 9,659,320

The following tables present the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment method as of December 31, 2013 and December 31, 2012:

Allowance for loan losses	Commercial, and Agricultural	Commercial Mortgages	Residential Mortgages	Consumer Loans	Unallocated	Total
			December 31, 2013			
Ending allowance balance attributable to loans:						
Individually evaluated for impairment	$ 575,995	$ 466,055	$ -	$ 3,972	$ -	$ 1,046,022
Collectively evaluated for impairment	1,402,694	4,407,377	1,497,214	3,033,019	-	10,340,304
Loans acquired with deteriorated credit quality	-	1,369,564	19,678	-	-	1,389,242
Total ending allowance balance	$ 1,978,689	$ 6,242,996	$ 1,516,892	$ 3,036,991	$ -	$ 12,775,568

Allowance for loan losses	Commercial, and Agricultural	Commercial Mortgages	Residential Mortgages	Consumer Loans	Unallocated	Total
			December 31, 2012			
Ending allowance balance attributable to loans:						

Individually evaluated for impairment	$ 133,437	$ 59,201	$ -	$ -	$ -	$ 192,638
Collectively evaluated for impairment	1,459,432	3,533,365	1,565,571	2,705,639	26,146	9,290,153
Loans acquired with deteriorated credit quality	114,727	835,132	-	-	-	949,859
Total ending allowance balance	$ 1,707,596	$ 4,427,698	$ 1,565,571	$ 2,705,639	$ 26,146	$ 10,432,650

	December 31, 2013				
Loans:	Commercial and Agricultural	Commercial Mortgages	Residential Mortgages	Consumer Loans	Total
Loans individually evaluated for impairment	$ 2,945,524	$ 10,702,816	$ 117,278	$ 130,929	$ 13,896,547
Loans collectively evaluated for impairment	142,107,931	354,636,380	196,146,739	281,978,972	974,870,022
Loans acquired with deteriorated credit quality	678,383	8,756,562	261,551	-	9,696,496
Total ending loans balance	$ 145,731,838	$ 374,095,758	$ 196,525,568	$ 282,109,901	$ 998,463,065

	December 31, 2012				
Loans:	Commercial and Agricultural	Commercial Mortgages	Residential Mortgages	Consumer Loans	Total
Loans individually evaluated for impairment	$ 1,907,395	$ 10,620,274	$ 131,909	$ -	$ 12,659,578
Loans collectively evaluated for impairment	131,045,609	301,172,164	200,622,600	239,689,455	872,529,828
Loans acquired with deteriorated credit quality	1,241,418	9,225,847	244,268	-	10,711,533
Total ending loans balance	$ 134,194,422	$ 321,018,285	$ 200,998,777	$ 239,689,455	$ 895,900,939

The following tables present loans individually evaluated for impairment recognized by class of loans as of December 31, 2013 and December 31, 2012, the average recorded investment and interest income recognized by class of loans as of the years ending December 31, 2013 and 2012:

	December 31, 2013			December 31, 2012		
	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated
With no related allowance recorded:						
Commercial and agricultural:						
Commercial and industrial	$ 1,905,782	$ 1,909,412	$ -	$ 2,059,027	$ 1,462,157	$ -
Commercial mortgages:						
Construction	2,329,223	2,318,729	-	5,168,353	5,166,853	-
Commercial mortgages other	7,406,355	7,439,358	-	5,678,565	5,090,399	-
Residential mortgages	117,278	117,278	-	131,909	131,909	-
Consumer loans:						
Home equity lines and loans	70,970	72,730	-	-	-	-
With an allowance recorded:						
Commercial and agricultural:						
Commercial and industrial	1,036,381	1,036,112	575,995	446,330	445,238	133,437
Commercial mortgages:						
Commercial mortgages other	951,241	944,729	466,055	364,423	363,022	59,201
Consumer loans:						
Home equity lines and loans	57,828	58,199	3,972	-	-	-
Total	$ 13,875,058	$ 13,896,547	$ 1,046,022	$ 13,848,607	$ 12,659,578	$ 192,638

	December 31, 2013		December 31, 2012		December 31, 2011	
	Average Recorded Investment	Interest Income Recognized (1)	Average Recorded Investment	Interest Income Recognized (1)	Average Recorded Investment	Interest Income Recognized (1)

With no related allowance recorded:						
Commercial and agricultural:						
Commercial and industrial	$ 1,604,773	$ 71,088	$ 480,755	$ 632	$ 3,029,611	$ 28,796
Commercial mortgages:						
Construction	3,364,173	95,235	73,316	870	20,578	-
Commercial mortgages other	5,990,852	249,459	1,989,795	10,338	2,743,345	4,959
Residential mortgages	124,896	-	105,880	-	250,391	-
Consumer loans:						
Home equity lines & loans	47,472	2,043	29,784	-	-	-
With an allowance recorded:						
Commercial and agricultural:						
Commercial and industrial	719,453	-	1,830,896	-	2,065,263	-
Commercial mortgages:						
Construction	-	-	4,148	-	14,893	-
Commercial mortgages other	866,722	-	872,292	-	1,521,828	-
Residential mortgages	-	-	64,003	-	-	-
Consumer loans:						
Home equity lines and loans	46,520	3,437	-	-	-	-
Direct consumer loans	3,050	-	-	-	-	-
Total	$12,767,911	$421,262	$5,450,869	$ 11,840	$ 9,645,909	$ 33,755

F-25

The following tables present the recorded investment in past due and non-accrual status by class of loans as of December 31, 2013 and December 31, 2012:

December 31, 2013	Current	30-89 Days Past Due	90 Days or more Past Due and accruing	Loans acquired with deteriorated credit quality	Non-Accrual (1)	Total
Commercial and agricultural:						
Commercial and industrial	$ 143,099,999	$ 28,888	$ -	$ 678,383	$ 1,347,435	$ 145,154,705
Agricultural	577,133	-	-	-	-	577,133
Commercial mortgages:						
Construction	24,743,496	-	1,453,180	773,738	539,725	27,510,139
Commercial mortgages other	335,122,887	1,137,897	-	7,982,824	2,342,011	346,585,619
Residential mortgages	187,448,407	5,457,860	-	261,551	3,357,750	196,525,568
Consumer loans:						
Credit cards	1,727,573	9,427	19,414	-	-	1,756,414
Home equity lines and loans	95,348,467	150,238	-	-	635,373	96,134,078
Indirect consumer loans	163,809,750	1,235,404	-	-	249,258	165,294,412
Direct consumer loans	18,830,404	49,155	-	-	45,438	18,924,997
Total	$ 970,708,116	$ 8,068,869	$ 1,472,594	$ 9,696,496	$ 8,516,990	$ 998,463,065

(1) Includes all loans on non-accrual status regardless of the number of days such loans were delinquent as of December 31, 2013.

December 31, 2012	Current	30-89 Days Past Due	90 Days or more Past Due and accruing	Loans acquired with deteriorated credit quality	Non-Accrual (1)	Total
Commercial and agricultural:						
Commercial and industrial	$ 131,404,371	$ 183,269	$ -	$ 1,241,418	$ 666,912	$ 133,495,970
Agricultural	698,452	-	-	-	-	698,452
Commercial mortgages:						

Construction	36,988,222	294,565	4,481,066	1,182,037	434,338	43,380,228
Commercial mortgages other	266,261,798	1,750,806	-	8,043,810	1,581,643	277,638,057
Residential mortgages	194,185,617	4,145,868	-`	244,268	2,423,024	200,998,777
Consumer loans:						
Credit cards	1,847,837	-	3,308	-	-	1,851,145
Home equity lines and loans	86,486,781	211,739	-	-	571,365	87,269,885
Indirect consumer loans	129,789,672	852,818	-	-	335,285	130,977,775
Direct consumer loans	19,481,693	89,619	-	-	19,338	19,590,650
Total	$867,144,443	$7,528,684	$4,484,374	$ 10,711,533	$ 6,031,905	$895,900,939

(1) Includes all loans on non-accrual status regardless of the number of days such loans were delinquent as of December 31, 2012.

Troubled Debt Restructurings:

As of December 31, 2013 and 2012, the Corporation has a recorded investment in troubled debt restructurings of $7,891,734 and $5,728,610, respectively. There were specific reserves of $252,790 allocated for troubled debt restructurings at December 31, 2013 and no specific reserves allocated for troubled debt restructurings at December 31, 2012. As of December 31, 2013, troubled debt restructurings totaling $6,830,550 were accruing interest under the modified terms and $1,061,184 were on non-accrual status. As of December 31, 2012, troubled debt restructurings totaling $5,363,712 were accruing interest under the modified terms and $364,898 were on non-accrual status. The Corporation has committed additional amounts totaling up to $165,000 and $130,000 as of December 31, 2013 and December 31, 2012, respectively, to customers with outstanding loans that are classified as troubled debt restructurings.

During the years ending December 31, 2013 and 2012, the terms of certain loans were modified as troubled debt restructurings. The modification of the terms of such loans included one or a combination of the following: reduced scheduled payments for greater than 3 months or an extension of the maturity date at a stated rate of interest lower than the current market rate for new debt with similar risk.

The following table presents loans by class modified as troubled debt restructurings that occurred during the years ending December 31, 2013 and 2012:

December 31, 2013	Number of Loans		Pre-Modification Outstanding Recorded Investment		Post-Modification Outstanding Recorded Investment
Troubled debt restructurings:					
Commercial and agricultural:					
Commercial and industrial	5	$	1,342,690	$	1,342,690
Commercial mortgages:					
Construction	1		325,957		325,957
Commercial mortgage other	1		133,000		133,000
Consumer loans:					
Home equity lines and loans	3		134,225		134,255
Total	10	$	1,935,872	$	1,935,872

December 31, 2012	Number of Loans		Pre-Modification Outstanding Recorded Investment		Post-Modification Outstanding Recorded Investment
Troubled debt restructurings:					
Commercial and agricultural:					
	4	$	1,307,188	$	1,307,188

Commercial and industrial					
Commercial mortgages:					
Construction	1		251,448		251,448
Commercial mortgage other	3		3,871,779		3,871,779
Total	8	$	5,430,415	$	5,430,415

The troubled debt restructurings described above increased the allowance for loan losses by $107,727 and resulted in no charge offs during the year ended December 31, 2013. The troubled debt restructurings described above did not increase the allowance for loan losses and resulted in no charge offs during the year ending December 31, 2012.

There were no payment defaults on any loans previously modified as troubled debt restructurings during the years ended December 31, 2013 or December 31, 2012, within twelve months following the modification. A loan is considered to be in payment default once it is 90 days contractually past due under the modified terms.

Credit Quality Indicators

The Corporation establishes a risk rating at origination for all commercial loans. The main factors considered in assigning risk ratings include, but are not limited to: historic and future debt service coverage, collateral position, operating performance, liquidity, leverage, payment history, management ability, and the customer's industry. Commercial relationship managers monitor all loans in their respective portfolios for any changes in the borrower's ability to service their debt and affirm the risk ratings for the loans at least annually.

For the retail loans, which include lines of credit, installment, mortgage, and home equity loans, once a loan is properly approved and closed, the Corporation evaluates credit quality based upon loan repayment.

The Corporation uses the risk rating system to identify criticized and classified loans. Commercial relationships within the criticized and classified risk ratings are analyzed quarterly. The Corporation uses the following definitions for criticized and classified loans (which are consistent with regulatory guidelines):

Special Mention – Loans classified as special mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or the institution's credit position as some future date.

Substandard – Loans classified as substandard are inadequately protected by the current net worth and paying capability of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

Doubtful – Loans classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

Loans not meeting the criteria above that are analyzed individually as part of the above described process are considered to be not rated loans. Based on the analyses performed as of December 31, 2013 and December 31, 2012, the risk category of the recorded investment of loans by class of loans is as follows:

	December 31, 2013					
	Not Rated	Pass	Loans acquired with deteriorated credit quality	Special Mention	Substandard	Doubtful
Commercial and agricultural:						
Commercial and industrial	$ -	$133,614,964	$ 678,383	$ 5,116,316	$ 4,724,318	$1,020,725
Agricultural	-	577,133	-	-	-	-
Commercial mortgages:						
Construction	-	23,087,004	773,738	2,783,848	865,549	-

Commercial mortgage other	-	313,955,960	7,982,824	13,611,331	11,035,504	-
Residential mortgages	192,995,108	-	261,551	-	3,268,909	-
Consumer loans:						
Credit cards	1,756,414	-	-	-	-	-
Home equity lines and loans	95,421,822	-	-	-	712,256	-
Indirect consumer loans	165,045,154	-	-	-	249,257	-
Direct consumer loans	18,879,559	-	-	-	45,438	-
Total	$474,098,057	$471,235,061	$9,696,496	$21,511,495	$20,901,231	$1,020,725

F-28

	December 31, 2012					
	Not Rated	Pass	Loans acquired with deteriorated credit quality	Special Mention	Substandard	Doubtful
Commercial and agricultural:						
Commercial and industrial	$ -	$121,145,761	$1,241,418	$ 8,008,002	$2,606,529	$494,260
Agricultural	-	698,452	-	-	-	-
Commercial mortgages:						
Construction	-	34,882,896	1,182,037	5,153,918	2,161,377	-
Commercial mortgage other	-	247,793,150	8,043,810	11,974,716	9,826,381	-
Residential mortgages	198,336,641	-	244,268	-	2,417,868	-
Consumer loans:						
Credit cards	1,851,145	-	-	-	-	-
Home equity lines and loans	86,615,392	-	-	-	654,493	-
Indirect consumer loans	130,642,490	-	-	-	335,285	-
Direct consumer loans						