BERKSHIRE HILLS BANCORP INC
Form 10-K
March 18, 2013
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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, 2012
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: 000-51584

BERKSHIRE HILLS BANCORP, INC.

(Exact name of registrant as specified in its charter)

Delaware	**04-3510455**

(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
24 North Street, Pittsfield, Massachusetts	**01201**
(Address of principal executive offices)	(Zip Code)

Registrant s telephone number, including area code: **(413) 443-5601**

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

Title of each class	Name of Exchange on which registered
Common stock, par value $0.01 per share	**New York Stock Exchange**

Securities registered pursuant to Section 12(g) of the Act: **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 the registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of the 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 the definition of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

(Check one)

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 Act). Yes o No x

The aggregate market value of the voting and non-voting common equity held by non-affiliates was approximately $476 million, based upon the closing price of $22.00 as quoted on the NASDAQ Global Select Market as of the last business day of the registrant s most recently completed second fiscal quarter.

The number of shares outstanding of the registrant s common stock as of March 14, 2013 was 25,348,594.

DOCUMENTS INCORPORATED BY REFERENCE: Portions of the Proxy Statement for the 2013 Annual Meeting of Stockholders are incorporated by reference in Part III of this Form 10-K.

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PART I

ITEM 1. BUSINESS

FORWARD-LOOKING STATEMENTS

Certain statements contained in this document that are not historical facts may constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (referred to as the Securities Act), and Section 21E of the Securities Exchange Act of 1934, as amended (referred to as the Securities Exchange Act), and are intended to be covered by the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. You can identify these statements from the use of the words may, will, should, could, would, pla potential, estimate, project, believe, intend, anticipate, expect, target and similar expressions. These forward-looking statements are significant risks, assumptions and uncertainties, including among other things, changes in general economic and business conditions, increased competitive pressures, changes in the interest rate environment, legislative and regulatory change, changes in the financial markets, and other risks and uncertainties disclosed from time to time in documents that Berkshire Hills Bancorp files with the Securities and Exchange Commission. Additionally, actual results from recent business combinations could differ materially from expected results, including difficulties in achieving cost savings from the merger or in achieving such cost savings within the expected time frame, along with difficulties in achieving targeted revenues from the merged operations. You should not place undue reliance on forward-looking statements, which reflect our expectations only as of the date of this report. We do not assume any obligation to revise forward-looking statements except as may be required by law.

GENERAL

Berkshire Hills Bancorp (Berkshire or the Company) is headquartered in Pittsfield, Massachusetts. Berkshire Hills Bancorp, Inc. is a Delaware corporation and the holding company for the Berkshire Bank (the Bank) and Berkshire Insurance Group (BIG). Established in 1846, the Bank is one of Massachusetts oldest and largest independent banks and is the largest banking institution based in Western Massachusetts.

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The Company profiles itself as follows:

During 2012, Berkshire transferred the listing of its common shares from NASDAQ to the New York Stock Exchange while retaining the trading symbol BHLB . At year-end 2012, Berkshire s closing stock price was $23.86 and 25.1 million common shares were outstanding. Berkshire is a regional bank and financial services company providing the service capabilities of a larger institution and the local focus and responsiveness as a local partner to its communities. The Company seeks to distinguish itself based on the following attributes:

- **Strong growth from organic, de novo, product and acquisition strategies**

- **Positive operating leverage elevating long term profitability**

- **Solid capital, core funding and risk management culture**

- **Experienced executive team focused on earnings and stockholder value**

- **Distinctive brand and culture as America s Most Exciting Bank**

- **Diversified integrated financial service revenues**

- **Positioned to be regional consolidator in attractive markets**

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The Bank operates under the brand America s Most Exciting Bank® and portrays its brand and culture as follows:

The Bank has 75 full-service banking offices and 10 lending offices in its New England and upstate New York footprint, which extends along Interstate 90 from Boston to Syracuse, and along Interstate 91 from Hartford into Vermont. The Bank s operations include those acquired as a result of four bank mergers in the last two years:

- Rome Bancorp, Inc. (Rome) in April 2011, headquartered in Rome, NY
- Legacy Bancorp, Inc. (Legacy) in July 2011, headquartered in Pittsfield, MA
- The Connecticut Bank and Trust Company (CBT) in April 2012, headquartered in Hartford, CT

- Beacon Federal Bancorp, Inc. (Beacon) in October 2012, headquartered in Syracuse, NY

The Bank s operations also include mortgage operations from Greenpark Mortgage Corporation (Greenpark) acquired in April 2012, headquartered in Needham, MA.

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The Bank serves the following regions:

- **Western New England**, with 27 banking offices, including the Company s headquarters in Pittsfield, MA. This region includes Berkshire County, MA, which is the Company s traditional market, where it has a leading market share in many of its product lines. This region also includes Southern Vermont, and many of the region s branches are in communities close to Route 7, which runs north/south through the valleys to the west of the Berkshire Hills and Green Mountains. This region is within commuting range of both Albany, New York and Springfield, Massachusetts and is known throughout the world as a tourist and recreational destination area, with vacation and second home traffic from New York City. The Pittsfield 2011 MSA GDP totaled $5 billion. At year-end 2012, the Company had approximately $1.3 billion in loans and $1.6 billion in deposits in its Western New England Market.

- **New York,** with 27 banking offices serving the Albany Capital District and Central New York. The Albany area represents a de novo expansion by the Company begun in 2005. Albany is the state capital and is part of New York s Tech Valley which is gaining prominence as a world technology hub including leading edge nanotechnology initiatives representing a blend of private enterprise and public investment. The Company s presence in this area is largely due to its de novo branch expansion, including four offices opened in 2012. The Company s Central New York area includes operations in the Rome/Utica MSA, which were acquired with the Rome merger, together with operations in the Syracuse MSA, which were acquired with the Beacon merger. The Albany/Schenectady 2011 MSA GDP was $41 billion, and the Rome/Utica/Syracuse total 2011 MSA GDP was $37 billion. At year-end 2012, including Beacon operations on a pro forma basis, Berkshire had approximately $1.4 billion in loans and $1.6 billion in deposits in the New York region. This included balances in two Tennessee branches which were part of the Beacon operations. Loans and deposits in these two branches were each less than $0.1 billion.

- **Hartford/Springfield,** with 20 banking offices serving the market along the Connecticut River in this region, which is the second largest economic area in New England. The Bank s operations here include operations acquired with the CBT merger in 2012. This region is centrally located between Boston and New York City at the crossroads of Interstate 91, which traverses the length of New England and Interstate 90, which traverses the width of Massachusetts. This region also has easy access to Bradley International Airport, which is a major airport serving central New England. The Hartford/Springfield combined 2011 MSA GDP was $107 billion. At year-end 2012, Berkshire had approximately $0.8 billion in loans and $0.8 billion in deposits in this region.

- **Eastern Massachusetts,** with ten lending offices and one branch office located in towns west and north of Boston. Eastern Massachusetts is the largest economic area in New England, and the Company s banking operations extend to Worcester which is within the commuting and commerce area of Boston. The Bank s Asset Based Lending Group is headquartered in this region, and serves middle market businesses throughout the Company s footprint. At year-end 2012, including the Beacon branch on a pro forma basis and all asset based loans, Berkshire had approximately $0.5 billion in loans and $0.1 billion in deposits in this region. Loans include residential mortgage loans in Eastern Massachusetts acquired from secondary market sources.

These regions are viewed as having favorable demographics and provide an attractive regional niche for the Bank to distinguish itself from larger super-regional banks and smaller community banks while serving its regional market area. The Company s markets have experienced less exposure to speculative development, real estate inflation, and subprime lending activities compared to many other regions of the country. As a result of its growth, the Company has increased and diversified its revenues both geographically and by product type and this has improved its flexibility in pursuing

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growth opportunities as they arise. The Company s regions have competitive economic strengths in precision manufacturing, distribution, technology, health care, and education which are expected to continue to support above average personal incomes and wealth. The Company believes it has attractive long term growth prospects because of the Bank s positioning as one of the leading regional banks in its markets with the ability to serve retail and commercial customers with a strong product set and responsive local management. The Company also has a goal to deepen its wallet share as a result of its focused cross sales program across its various business lines including insurance and wealth management. As a result of its bank acquisitions, the Company has a limited amount of loan and deposit business located outside of its New England and New York regional market which is not viewed as material to its condition, operations, and strategies.

In addition to business acquisitions, Berkshire s expansion has been based on team and talent recruitment. In 2012, this included the recruitment of the Eastern Massachusetts mortgage banking team, the recruitment of new commercial banking leadership in Hartford and Syracuse, and the integration of the Central/Eastern commercial team recruited in December 2011. The Company also pursues organic growth through ongoing business development, de novo branching, and product development. The Bank promotes itself as America s Most Exciting Bank®. It has set out to change the financial service experience. Its vision is to excel as a high performing market leader with the right people, attitude, and energy providing an engaging and exciting customer and team member experience. This brand and culture statement is expected to drive customer engagement, loyalty, market share and profitability. Similarly, this focus on performance underlies Berkshire s strong growth, improved efficiency, investment in infrastructure, and solid execution of acquisition due diligence and integration.

The Company offers a wide range of deposit, lending, insurance, and wealth management products to retail, commercial, not-for-profit, and municipal customers in its market areas. The Company s product offerings also include retail and commercial electronic banking, commercial cash management, and commercial interest rate swaps. The Company stresses a culture of teamwork and performance excellence to produce customer satisfaction to support its strategic growth and profitability. The Company utilizes Six Sigma tools to improve operational effectiveness and efficiency. The Company converted its core banking systems to a new scalable technology platform in 2012, with goals to enhance service, efficiency, reliability, customer relationship management, distribution channels, product quality, and revenue generation. The systems provide deeper and more granular customer and operational data that Berkshire expects to mine in order to better inform its strategic direction and business execution.

The Company has recruited executives with experience in regional bank management and has augmented its management team as it has expanded into a diversified regional financial services provider. The Company has invested in its infrastructure in order to position itself for further growth as a regional consolidator with an objective of filling in and expanding its footprint in its New England and New York markets. The Company completed four bank acquisitions in 2011 and 2012 which contributed strongly to accretion in earnings per share and which were absorbed while the Company also accreted tangible book value per share based on strong internal capital generation.

COMPANY WEBSITE AND AVAILABILITY OF SECURITIES AND EXCHANGE COMMISSION FILINGS

Information regarding the Company is available through the Investor Relations tab at www.berkshirebank.com. The Company s annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and any amendments to those reports filed pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 are available free of charge at www.sec.gov and at www.berkshirebank.com under the Investor Relations tab. Information on the website is not incorporated by reference and is not a part of this annual report on Form 10-K.

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COMPETITION

The Company is subject to strong competition from banks and other financial institutions and financial service providers. Its competition includes national and super-regional banks such as Bank of America, TD Bank, Citizens Bank, Sovereign Bank, and Key Bank which have substantially greater resources and lending limits. Non-bank competitors include credit unions, brokerage firms, insurance providers, financial planners, and the mutual fund industry. New technology is reshaping customer interaction with financial service providers and the increase of Internet-accessible financial institutions increases competition for the Company s customers. The Company generally competes on the basis of customer service, relationship management, and the fair pricing of loan and deposit products and wealth management and insurance services. The location and convenience of branch offices is also a significant competitive factor, particularly regarding new offices. The Company does not rely on any individual, group, or entity for a material portion of its deposits.

LENDING ACTIVITIES

General. The Bank originates loans in the four basic portfolio categories discussed below. Lending activities are limited by federal and state laws and regulations. Loan interest rates and other key loan terms are affected principally by the Bank s asset/liability strategy, loan demand, competition, and the supply of money available for lending purposes. These factors, in turn, are affected by general and economic conditions, monetary policies of the federal government, including the Federal Reserve, legislative tax policies and governmental budgetary matters. Most of the Bank s loans are made in its market areas and are secured by real estate located in its market areas. Lending is therefore affected by activity in these real estate markets. Loan portfolios acquired in business combinations include national commercial real estate loans acquired with Legacy and Tennessee commercial loans acquired with Beacon. The Company is reducing these acquired portfolios. The Bank does not engage in subprime lending activities targeted towards borrowers in high risk categories. The Bank monitors and manages the amount of long-term fixed-rate lending volume. Adjustable-rate loan products generally reduce interest rate risk but may produce higher loan losses in the event of sustained rate increases. In 2012, the Bank acquired residential mortgage banking operations in Eastern Massachusetts which primarily originate residential mortgages for sale. Excluding mortgage banking operations, the Bank retains most of the loans it originates, although the Bank generally sells its longer-term, fixed-rate, one to four-family residential loans and sometimes buys and sells participations in some commercial loans.

Loan Portfolio Analysis. The following table sets forth the year-end composition of the Bank s loan portfolio in dollar amounts and as a percentage of the portfolio at the dates indicated. Further information about the composition of the loan portfolio is contained in the Loans footnote in the consolidated financial statements.

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Item 1 - Table 1 - Loan Portfolio Analysis

(In millions)	2012 Amount	2012 Percent of Total	2011 Amount	2011 Percent of Total	2010 Amount	2010 Percent of Total	2009 Amount	2009 Percent of Total	2008 Amount	2008 Percent of Total
Residential mortgages	$ 1,324.3	33%	$ 1,020.4	34%	$ 645.0	30%	$ 609.0	31%	$ 677.2	34%
Commercial mortgages	1,413.5	35	1,156.2	39	925.6	43	851.8	43	805.5	40
Commercial business	600.1	15	410.3	14	286.1	13	186.0	10	178.9	9
Total commercial loans	2,013.6	50	1,566.5	53	1,211.7	56	1,037.8	53	984.4	49
Consumer	650.7	17	369.6	13	285.5	14	314.8	16	345.5	17
Total loans	$ 3,988.6	100%	$ 2,956.5	100%	$ 2,142.2	100%	$ 1,961.6	100%	$ 2,007.1	100%
Allowance for loan losses	(33.2)		(32.4)		(31.9)		(31.8)		(22.9)	
Net loans	$ 3,955.4		$ 2,924.1		$ 2,110.3		$ 1,929.8		$ 1,984.2	

Residential Mortgages. The Bank offers fixed-rate and adjustable-rate residential mortgage loans with maturities of up to 30 years that are fully amortizing with monthly loan payments. Residential mortgages are generally underwritten according to the Federal National Mortgage Association (Fannie Mae) or the Federal Home Loan Mortgage Association (Freddie Mac) guidelines for loans they designate as A or A- (these are referred to as conforming loans). Private mortgage insurance is generally required for loans with loan-to-value ratios in excess of 80%. The Bank also originates loans above conforming loan amount limits, referred to as jumbo loans, which are generally conforming to secondary market guidelines for these loans. The Bank does not offer subprime mortgage lending programs.

The Bank generally sells most of its newly originated fixed rate mortgages. It also monitors its interest rate risk position and sometimes may decide to purchase or sell seasoned mortgage loans in the secondary mortgage market. The Bank is approved as a direct seller to Fannie Mae, retaining the servicing rights. Beginning in 2012, the Bank sells the majority of its mortgages to national institutional secondary market investors on a servicing released basis. Sales of mortgages generally involve customary representations and warranties and are nonrecourse in the event of borrower default. The Bank is also an approved originator of loans for sale to the Federal Housing Administration (FHA), U.S. Department of Veteran Affairs (VA), and state housing agency programs.

The Bank offers adjustable rate (ARM) mortgages which do not contain interest-only or negative amortization features. After an initial term of six months to ten years, the rates on these loans generally reset every year based upon a contractual spread or margin above the average yield on U.S. Treasury securities. ARM loan interest rates may rise as interest rates rise, thereby increasing the potential for default. At year-end 2012, the Bank s adjustable rate mortgage portfolio totaled $363 million. The Bank also originates loans to individuals for the construction and acquisition of personal residences. These loans generally provide fifteen-month construction periods followed by a permanent mortgage loan, and follow the Bank s normal mortgage underwriting guidelines.

Commercial Mortgages. The Bank originates commercial mortgages on properties used for business purposes such as small office buildings, industrial, healthcare, lodging, recreation, or retail facilities. This portfolio also includes commercial 1-4 family and multifamily properties.

Loans may generally be made with amortizations of up to 25 years and with interest rates that adjust periodically (primarily from short-term to five years). Most commercial mortgages are originated with final maturities of ten years or less. The Bank generally requires that borrowers have debt service coverage ratios (the ratio of available cash flows before debt service to debt service) of at least 1.25 times. Loans at origination may be made up to 80% of appraised value. Generally, commercial mortgages require personal guarantees by the principals. Credit enhancements in the form of additional collateral or guarantees are normally considered for start-up businesses without a qualifying cash flow history.

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Commercial mortgages generally involve larger principal amounts and a greater degree of risk than residential mortgages. They also often provide higher lending spreads. Because repayment is often dependent on the successful operation or management of the properties, repayment of such loans may be affected by adverse conditions in the real estate market or the economy. The Bank seeks to minimize these risks through strict adherence to its underwriting standards and portfolio management processes.

The Bank offers interest rate swaps to certain larger commercial mortgage borrowers. These swaps allow the Bank to originate a mortgage based on short-term LIBOR rates and allow the borrower to swap into a longer term fixed rate. The Bank simultaneously sells an offsetting back-to-back swap to an investment grade national bank so that it does not retain this fixed-rate risk. The Bank also records fee income on these interest rate swaps based on the terms of the offsetting swaps with the bank counterparties.

The Bank originates construction loans to builders and commercial borrowers in and around its markets. Construction loans finance the acquisition and/or improvement of commercial and residential properties. The maximum loan to value limits for construction loans follow FDIC supervisory limits, up to a maximum of 80%. The Bank commits to provide the permanent mortgage financing on most of our construction loans on income-producing property. Advances on construction loans are made in accordance with a schedule reflecting the cost of the improvements. Construction loans include land acquisition loans up to a maximum 65% loan to value on raw land. Construction loans may have greater credit risk than permanent loans. In many cases, the loan s repayment is dependent on the completion of construction and other real estate improvements, which entails risk that construction permits may be delayed or may not be received, or that there may be delays or cost overruns during construction. Repayment is also often dependent on the sale or rental of the improved property, which depends on market conditions and the availability of permanent financing. Developers and contractors may also encounter liquidity risks or other risks related to other projects which are not being financed.

Commercial Business Loans. The Bank offers secured commercial term loans with repayment terms which are normally limited to the expected useful life of the asset being financed, generally not exceeding seven years. The Bank also offers revolving loans, lines of credit, letters of credit, time notes and Small Business Administration guaranteed loans. Business lines of credit have adjustable rates of interest and are payable on demand, subject to annual review and renewal. Commercial business loans are generally secured by a variety of collateral such as accounts receivable, inventory and equipment, and are generally supported by personal guarantees. Loan to value ratios depend on the collateral type and generally do not exceed 95% of the liquidation value of the collateral. Some commercial loans may also be secured by liens on real estate. The Bank generally does not make unsecured commercial loans.

The Asset Based Lending Group serves the commercial middle market in New England, as well as the Bank s market in northeastern New York. This group expands the Bank s business lending offerings to include revolving lines of credit and term loans secured by accounts receivable, inventory, and other assets to manufacturers, distributors and select service companies experiencing seasonal working capital needs, rapid sales growth, a turnaround, buyout or recapitalization with credit needs ranging from $2 to $25 million. Asset based lending involves monitoring loan collateral so that outstanding balances are always properly secured by business assets.

In the fourth quarter of 2011, the Bank recruited an experienced commercial lending team to serve the commercial middle market in Central/Eastern Massachusetts. This team also has expertise in health care and education financing. Additionally, the Bank has reorganized its small business lending function to expand this important business financing capability and includes the retail division in the origination of conforming small business loans in order to provide the best service to community based small businesses.

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Commercial loans are of higher risk and are made primarily on the basis of the borrower s ability to make repayment from the cash flows of its business. Further, any collateral securing such loans may depreciate over time, may be difficult to monitor and appraise and may fluctuate in value. The Bank gives additional consideration to the borrower s credit history and the guarantor s capacity to help mitigate these risks.

Consumer Loans. The Bank s consumer loans consist principally of home equity lines of credit, together with second mortgage loans and automobile loans. The Bank s home equity lines of credit are typically secured by first or second mortgages on borrowers residences. Home equity lines have an initial revolving period up to fifteen years, followed by an amortizing term up to twenty years. These loans are normally indexed to the prime rate. Home equity loans also include amortizing fixed-rate second mortgages with terms up to fifteen years. Lending policies for combined debt service and collateral coverage are similar to those used for residential first mortgages, although underwriting verifications are more streamlined. The maximum combined loan-to-value is 80%. Home equity line credit risks are similar to those of adjustable-rate first mortgages, although these loans may be more sensitive to losses when interest rates are rising due to increased sensitivity to rate changes. Additionally, there may be possible compression of collateral coverage on second lien home equity lines. The Bank also includes all other consumer loans in this portfolio total, including personal secured and unsecured loans and overdraft protection facilities. The acquired Beacon operations include direct and indirect automobile loan portfolios. Beacon originated indirect automobile loans through established relationships with a number of automobile dealers in Central New York. For new automobiles, the amount financed could be up to 100% of the value of the vehicle, plus applicable taxes and dealer charges (i.e., warranty and insurance charges). For used automobiles, the amount of the loan was limited to the loan value of the vehicle, as established by industry guides.

Maturity and Sensitivity of Loan Portfolio. The following table shows contractual final maturities of selected loan categories at year-end 2012. The contractual maturities do not reflect premiums, discounts, deferred costs, and prepayments.

Item 1 - Table 2 - Loan Contractual Maturity -Scheduled Loan Amortizations are not included in the maturities presented.

Contractual Maturity (In thousands)	**One Year or Less**	**More than One to Five Years**	**More Than Five Years**	**Total**
Construction mortgage loans:				
Residential	$ 6,870	$ 19,849	$	$ 26,719
Commercial	64,752	103,073		167,825
Commercial business loans	171,817	326,681	101,628	600,126
Total	$ 243,439	$ 449,603	$ 101,628	$ 794,670

For the $551 million of loans above which mature in more than one year, $162 million of these loans are fixed-rate and $388 million are variable rate.

Loan Administration. Lending activities are governed by a loan policy approved by the Board s Risk Management Committee. Internal staff perform and monitor post-closing loan documentation review, quality control, and commercial loan administration. The lending staff assigns a risk rating to all commercial loans. Management primarily relies on internal risk management staff to review the risk ratings of the majority of commercial loan balances.

The Bank s lending activities follow written, non-discriminatory underwriting standards and loan origination procedures established by the Risk Management Committee and Management. The Bank s loan underwriting is based on a review of certain factors including risk ratings, recourse, loan-to-value ratios and material policy exceptions. The

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Risk Management Committee has established individual and combined loan limits and lending approval authorities. Management s Executive Loan Committee is responsible for commercial and residential loan approvals in accordance with these standards and procedures. Generally, commercial lending management has the authority to approve pass rated secured loans up to $2 million and in conjunction with the Senior Credit Officer up to $7.5 million (or $5 million in the case of material policy exceptions). The Executive Loan Committee approves secured loans over these amounts (and over $1 million unsecured).

The Bank s lending activities are conducted by its salaried and commissioned loan personnel. Designated salaried branch staff originate conforming residential mortgages and receive bonuses based on overall performance. Additionally, the Bank employs commissioned residential mortgage originators. Commercial lenders receive salaries and are eligible for bonuses based on overall performance. From time to time, the Bank will purchase whole loans or participations in loans. These loans are underwritten according to the Bank s underwriting criteria and procedures and are generally serviced by the originating lender under terms of the applicable participation agreement. The Bank routinely sells newly originated fixed rate residential mortgages in the secondary market. Customer rate locks are offered without charge and rate locked applications are generally committed for forward sale or hedged with derivative financial instruments to minimize interest rate risk pending delivery of the loans to the investors. The Bank sells a limited number of commercial loan participations on a non-recourse basis. The Bank issues loan commitments to its prospective borrowers conditioned on the occurrence of certain events. Loan origination commitments are made in writing on specified terms and conditions and are generally honored for up to sixty days from approval; some commercial commitments are made for longer terms.

The loan policy sets certain limits on concentrations of credit and requires periodic reporting of concentrations to the Risk Management Committee. Loans outstanding to the ten largest relationships averaged $23 million each, or 5.1% of total risk based capital. Total year-end commercial construction loans outstanding were 37% of the Bank s risk based capital at year-end, and total commercial mortgage outstandings (including certain owner-occupied loans) were estimated at 272% of risk based capital. The Bank s portfolio management objective has been to reduce these concentrations. The FDIC has established monitoring guidelines of 100% and 300% for these ratios, respectively. Above these guidelines, additional monitoring and risk management controls are required.

Problem Assets. The Bank prefers to work with borrowers to resolve problems rather than proceeding to foreclosure. For commercial loans, this may result in a period of forbearance or restructuring of the loan, which is normally done at current market terms and does not result in a troubled loan designation. For residential mortgage loans, the Bank generally follows FDIC guidelines to attempt a restructuring that will enable owner-occupants to remain in their home. However, if these processes fail to result in a performing loan, then the Bank generally will initiate foreclosure or other proceedings no later than the 90th day of a delinquency, as necessary, to minimize any potential loss. Management reports delinquent loans and non-performing assets to the Board quarterly. Loans are generally removed from accruing status when they reach 90 days delinquent, except for certain loans which are well secured and in the process of collection. Delinquent automobile loans are maintained on accrual until they reach 120 days delinquent, and then they are generally charged-off.

Real estate acquired by the Bank as a result of loan collections is classified as real estate owned until sold. When property is acquired it is recorded at fair market value less estimated selling costs at the date of foreclosure, establishing a new cost basis. Holding costs and decreases in fair value after acquisition are expensed. Interest income that would have been recorded for 2012 if nonaccruing loans been current according to their original terms, amounted to $1.5 million. Included in the amount is $19 thousand related to troubled debt restructurings. The amount of interest income on those loans that was recognized in net income in 2012 was $0.3 million. Included in this amount is $43 thousand

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related to troubled debt restructurings. Interest income on accruing troubled debt restructurings totaled $0.1 million for 2012. The total carrying value of troubled debt restructurings was $4.6 million at year-end.

The following table sets forth additional information on year-end problem assets and accruing troubled debt restructurings (TDR). Due to accounting standards for business combinations, non-accrual loans of acquired banks are recorded as accruing on the acquisition date. Therefore, measures related to accruing and non-accruing loans reflect these standards and may not be comparable compared to prior periods.

Item 1 - Table 3 - Problem Assets and Accruing TDR

(In thousands)	**2012**	**2011**	**2010**	**2009**	**2008**
Non-accruing loans:					
Residential mortgages	$ 7,466	$ 7,010	$ 2,173	$ 3,304	$ 1,646
Commercial mortgages	12,617	14,280	9,488	31,917	7,738
Commercial business	3,681	990	1,305	3,115	1,921
Consumer	1,748	1,954	746	364	866
Total non-performing loans	25,512	24,234	13,712	38,700	12,171
Real estate owned	1,929	1,900	3,386	30	498
Total non-performing assets	$ 27,441	$ 26,134	$ 17,098	$ 38,730	$ 12,669
Troubled debt restructurings (accruing)	$ 3,641	$ 1,263	$ 7,829	$ 17,818	$ 7,456
Accruing loans 90+ days past due	$ 18,977	$ 10,184	$ 1,054	$ 91	$ 923
Total non-performing loans/total loans	0.64%	0.82%	0.64%	1.97%	0.61%
Total non-performing assets/total assets	0.52%	0.65%	0.59%	1.43%	0.48%

Asset Classification and Delinquencies. The Bank performs an internal analysis of its commercial loan portfolio and assets to classify such loans and assets in a manner similar to that employed by the federal banking regulators. There are four classifications for loans with higher than normal risk: Loss, Doubtful, Substandard and Special Mention. Normally an asset classified as Loss is fully charged-off. Substandard assets have one or more defined weaknesses and are characterized by the distinct possibility that the insured institution will sustain some loss if the deficiencies are not corrected. Doubtful assets have the weaknesses of substandard assets with the additional characteristic that the weaknesses make collection or liquidation in full on the basis of currently existing facts, conditions and values questionable, and there is a high possibility of loss. Assets that do not currently expose the insured institution to sufficient risk to warrant classification in one of the aforementioned categories but possess weaknesses are designated Special Mention. Please see the additional discussion of non-accruing and potential problem loans in Item 7 and additional information about loans by risk rating in the Loans Note to the consolidated financial statements.

Allowance for Loan Losses. The Bank s loan portfolio is regularly reviewed by management to evaluate the adequacy of the allowance for loan losses. The allowance represents management s estimate of inherent losses that are probable and estimable as of the date of the financial statements. The allowance includes a specific component for impaired loans (a specific loan loss reserve) and a general component for portfolios of all outstanding loans (a general loan loss reserve). There is no allowance for loan losses assigned at the time of acquisition to loans acquired in business combinations which are carried at fair value, including the impact of expected losses, as of the acquisition date. An allowance on such loans is established subsequent to the acquisition date through the provision for loan losses based on an analysis of factors including environmental factors. The loan loss allowance is discussed further in the Note about Significant Accounting Policies in the consolidated financial statements.

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For loans covered by the loan loss allowance, management assesses specific loan loss reserves when it deems that it is probable that the Bank will be unable to collect all amounts due according to the contractual terms stipulated in the loan agreement. Management weighs various factors in its assessment, including but not limited to, its review of the borrower s payment history and the borrower s future ability to service the debt, the current value of any pledged collateral, and the strength of any guarantor support. Generally non-accruing commercial loans are deemed impaired and evaluated for specific valuation allowances. Confirmed loan losses are charged-off directly to the allowance. Losses are deemed confirmed when upon review of all the available evidence, any portion of the loan balance is deemed uncollectible. Subsequent recoveries, if any, are credited to the allowance.

For loans from business activities covered by the loan loss allowance, management estimates general loan loss reserves when it is probable that there would be credit losses in portfolios of loans with similar characteristics. Management has identified four primary loan portfolios: residential mortgages, commercial mortgages, commercial business, and consumer loans. Sub-portfolios within these primary loan portfolios are also evaluated in order to arrive at a more precise general loan loss allowance. The methodology includes a historical loss component and an environmental factors component. The historical loss component is based on the Bank s risk rating system in combination with the attribution of loss factors based on corporate default and recovery rates in the industry. The environmental factors component assesses loss potential as it may be affected by economic business conditions, lending policies and procedures, portfolio characteristics, management and staff changes, problem loan trends, and credit concentration trends. While the general loss reserve is analyzed according to the various subportfolios, the general loss reserve in aggregate is available to cover all losses in all components of the loan portfolio.

Management believes that it uses the best information available to establish the allowance for loan losses. However, future adjustments to the allowance for loan losses may be necessary, and results of operations could be adversely affected if circumstances differ substantially from the assumptions used in making its determinations. Because the estimation of inherent losses cannot be made with certainty, there can be no assurance that the existing allowance for loan losses is adequate or that increases will not be necessary should the quality of any loan or loan portfolio category deteriorate as a result of the factors discussed above. Additionally, the regulatory agencies, as an integral part of their examination process, also periodically review the Bank s allowance for loan losses. Such agencies may require the Bank to make additional provisions for estimated losses based upon judgments different from those of management. Any material increase in the allowance for loan losses may adversely affect the Bank s financial condition and results of operations.

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The following table presents an analysis of the allowance for loan losses for the years indicated.

Item 1 - Table 4 - Allowance for Loan Loss

(In thousands)	2012	2011	2010	2009	2008
Balance at beginning of year	$ 32,444	$ 31,898	$ 31,816	$ 22,908	$ 22,116
Charged-off loans:					
Residential mortgages	2,647	1,322	409	2,016	143
Commercial mortgages	4,229	4,046	6,403	27,596	1,384
Commercial business	697	1,443	2,685	5,945	884
Consumer	1,877	885	1,188	3,586	2,031
Total charged-off loans	9,450	7,696	10,685	39,143	4,442
Recoveries on charged-off loans:					
Residential mortgages	103	231	213		
Commercial mortgages	52	189	794	22	100
Commercial business	96	109	1,094	64	290
Consumer	373	150	140	235	264
Total recoveries	624	679	2,241	321	654
Net loans charged-off	8,826	7,017	8,444	38,822	3,788
Allowance attributed to loans acquired by merger					
Provision for loan losses	9,590	7,563	8,526	47,730	4,580
Transfer of commitment reserve					
Balance at end of year	$ 33,208	$ 32,444	$ 31,898	$ 31,816	$ 22,908
Ratios:					
Net charge-offs/average loans	0.26%	0.27%	0.42%	1.96%	0.19%
Recoveries/charged-off loans	6.60	8.82	20.97	0.82	14.72
Net loans charged-off/allowance for loan losses	26.58	21.63	26.47	109.81	14.77
Allowance for loan losses/total loans	0.83	1.10	1.49	1.62	1.14
Allowance for loan losses/non-accruing loans	130.17	133.88	232.63	82.21	188.22

The following tables present year-end data for the approximate allocation of the allowance for loan losses by loan categories at the dates indicated (including an apportionment of any unallocated amount). The first table shows for each category the amount of the allowance allocated to that category as a percentage of the outstanding loans in that category. The second table shows the allocated allowance together with the percentage of loans in each category to total loans. Management believes that the allowance can be allocated by category only on an approximate basis. The allocation of the allowance to each category is not indicative of future losses and does not restrict the use of any of the allowance to absorb losses in any category. Due to the impact of accounting standards for acquired loans, data in the accompanying tables may not be comparable between accounting periods.

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Item 1 - Table 5A - Allocation of Allowance for Loan Loss by Category

	2012		2011		2010		2009		2008	
(Dollars in thousands)	Amount Allocated	Percent of Amount Allocated to Total Loans in Each Category	Amount Allocated	Percent of Amount Allocated to Total Loans in Each Category	Amount Allocated	Percent of Amount Allocated to Total Loans in Each Category	Amount Allocated	Percent of Amount Allocated to Total Loans in Each Category	Amount Allocated	Percent Amount All to Tota Loans in I Catego
Residential mortgages	$ 6,444	0.49%	$ 3,420	0.34%	$ 3,200	0.50%	$ 3,169	0.52%	$ 2,006	
Commercial mortgages	19,275	1.36	22,176	1.92	19,923	2.15	19,659	2.31	13,539	
Commercial business	5,707	0.95	4,566	1.11	6,498	2.27	6,099	3.28	4,184	
Consumer	1,782	0.27	2,282	0.62	2,277	0.80	2,889	0.92	3,179	
Total	$ 33,208	0.83%	$ 32,444	1.10%	$ 31,898	1.49%	$ 31,816	1.62%	$ 22,908	

Item 1 - Table 5B - Allocation of Allowance for Loan Loss

	2012		2011		2010		2009		2008	
(Dollars in thousands)	Amount Allocated	Percent of Loans in Each Category to Total Loans	Amount Allocated	Percent of Loans in Each Category to Total Loans	Amount Allocated	Percent of Loans in Each Category to Total Loans	Amount Allocated	Percent of Loans in Each Category to Total Loans	Amount Allocated	Percent of Loans in Each Category to Total Loans
Residential mortgages	$ 6,444	33.20%	$ 3,420	34.51%	$ 3,200	30.11%	$ 3,169	31.05%	$ 2,006	33.74%
Commercial mortgages	19,275	35.44	22,176	39.11	19,923	43.21	19,659	43.42	13,539	40.13
Commercial business	5,707	15.05	4,566	13.88	6,498	13.35	6,099	9.48	4,184	8.92
Consumer	1,782	16.31	2,282	12.50	2,277	13.33	2,889	16.05	3,179	17.21
Total	$ 33,208	100.00%	$ 32,444	100.00%	$ 31,898	100.00%	$ 31,816	100.00%	$ 22,908	100.00%

INVESTMENT SECURITIES ACTIVITIES

The securities portfolio provides cash flow to protect the safety of customer deposits and as a potential source of liquidity for funding loan commitments. The portfolio is also used to manage interest rate risk and to earn a reasonable return on investment. Decisions are made in accordance with the Company s investment policy and include consideration of risk, return, duration, and portfolio concentrations. Day-to-day oversight of the portfolio rests with the Chief Financial Officer and the Treasurer. The Asset/Liability Committee meets monthly and reviews investment strategies. The Risk Management Committee reviews all securities transactions and provides general oversight of the investment function.

The Company has historically maintained a high-quality portfolio of limited duration mortgage-backed securities, together with a portfolio of municipal bonds including national and local issuers and local economic development bonds issued to non-profit organizations. Nearly all of the mortgage-backed securities are issued by Ginnie Mae, Fannie Mae or Freddie Mac, and they generally have an average duration of two to four years. They principally consist of collateralized mortgage obligations (generally consisting of planned amortization class bonds). Other than securities issued by the above agencies, no other issuer concentrations exceeding 10% of stockholders equity existed at year-end 2012. The municipal portfolio provides tax-advantaged yield, and the local economic development bonds were originated by the Company to area borrowers. Nearly all of the Company s available for sale municipal securities are investment grade rated and most of the portfolio carries credit enhancement protection. The Company also invests in equity securities of local financial institutions for a variety of reasons, particularly if it concludes the financial institution is undervalued or if the Company might consider partnering with the financial institution in the future. The Company owns restricted equity in the Federal Home Loan Bank of Boston (FHLBB) based on its operating relationship with the FHLBB. The Company owns an interest rate swap against a tax advantaged economic development bond issued to a local not-for-profit organization, and as a result this security is carried as a trading

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account security. The Bank did not record any material losses or write-downs of investment securities during the year and none of the Company s investment securities were other-than-temporarily impaired at year-end.

The following tables present the amortized cost and fair value of the Company s securities, by type of security, for the years indicated.

Item 1 - Table 6A - Amortized Cost and Fair Value of Securities

	2012		2011		2010	
(In thousands)	**Amortized Cost**	**Fair Value**	**Amortized Cost**	**Fair Value**	**Amortized Cost**	**Fair Value**
Securities available for sale						
Municipal bonds and obligations	$ 79,498	$ 84,757	$ 73,436	$ 77,854	$ 79,292	$ 79,906
Mortgage-backed securities	318,245	321,685	289,084	292,707	170,294	172,883
Other bonds and obligations	35,241	34,436	30,702	28,186	40,931	38,548
Marketable equity securities	22,467	25,291	20,236	21,009	15,756	18,905
Total securities available for sale	$ 455,451	$ 466,169	$ 413,458	$ 419,756	$ 306,273	$ 310,242
Securities held to maturity						
Municipal bonds and obligations	$ 8,295	$ 8,295	$ 10,349	$ 10,349	$ 7,069	$ 7,069
Mortgage-backed securities	76	83	79	83	83	86
Tax advantaged economic development bonds	41,678	43,137	47,869	49,348	48,861	50,016
Other bonds and obligations	975	975	615	615	423	423
Total securities held to maturity	$ 51,024	$ 52,490	$ 58,912	$ 60,395	$ 56,436	$ 57,594
Trading account security	$ 13,610	$ 16,893	$ 14,096	$ 17,395	$ 14,560	$ 16,155
Restricted equity securities	$ 39,785	$ 39,785	$ 37,118	$ 37,118	$ 23,120	$ 23,120

Item 1 - Table 6B - Amortized Cost and Fair Value of Securities

	2012		2011		2010	
(In thousands)	**Amortized Cost**	**Fair Value**	**Amortized Cost**	**Fair Value**	**Amortized Cost**	**Fair Value**
U.S. Treasuries,other Government agencies and corporations	$ 340,789	$ 347,058	$ 309,399	$ 313,799	$ 186,133	$ 191,874
Municipal bonds and obligations	143,080	153,082	145,750	154,946	149,782	153,146
Other bonds and obligations	76,001	75,197	68,435	65,919	64,474	62,091
Total Securites	$ 559,870	$ 575,337	$ 523,584	$ 534,664	$ 400,389	$ 407,111

The schedule includes available-for-sale and held-to-maturity securities as well as the trading security and restricted equity securities.

The following table summarizes year-end 2012 amortized cost, weighted average yields and contractual maturities of debt securities. A significant portion of the mortgage-based securities are planned amortization class bonds. Their expected durations are 2-4 years at current interest rates, but the contractual maturities shown reflect the underlying maturities of the collateral mortgages. Additionally, the mortgage-based securities maturities shown below are based on final maturities and do not include scheduled amortization.

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Item 1 - Table 7 - Weighted Average Yield

(In millions)	One Year or Less Amortized Cost	One Year or Less Weighted Average Yield	More than One Year to Five Years Amortized Cost	More than One Year to Five Years Weighted Average Yield	More than Five Years to Ten Years Amortized Cost	More than Five Years to Ten Years Weighted Average Yield	More than Ten Years Amortized Cost	More than Ten Years Weighted Average Yield	Total Amortized Cost	Total Weighted Average Yield
Municipal bonds and obligations	$ 4.6	1.26%	$ 4.5	4.97%	$ 17.1	6.38%	$ 61.7	6.38%	$ 87.8	6.04%
Mortgage-backed securities	0.0	5.34	7.8	2.88	22.9	2.01	287.7	1.43	318.3	1.51
Other bonds and obligations	0.6	1.96	9.0	4.46	29.6	5.63	38.7	5.33	77.9	5.32
Total	$ 5.2	1.34%	$ 21.3	3.99%	$ 69.6	4.62%	$ 388.1	2.60%	$ 484.0	2.94%

DEPOSIT ACTIVITIES AND OTHER SOURCES OF FUNDS

Deposits are the major source of funds for the Bank s lending and investment activities. Deposit accounts are the primary product and service interaction with the Bank s customers. The Bank serves personal, commercial, non-profit, and municipal deposit customers. Most of the Bank s deposits are generated from the areas surrounding its branch offices. The Bank offers a wide variety of deposit accounts with a range of interest rates and terms. The Bank also periodically offers promotional interest rates and terms for limited periods of time. The Bank s deposit accounts consist of interest-bearing checking, noninterest-bearing checking, regular savings, money market savings and time certificates of deposit. The Bank emphasizes its transaction deposits checking and NOW accounts for personal accounts and checking accounts promoted to businesses. These accounts have the lowest marginal cost to the Bank and are also often a core account for a customer relationship. The Bank offers a courtesy overdraft program to improve customer service, and also provides debit cards and other electronic fee producing payment services to transaction account customers. The Bank is promoting remote deposit capture devices so that commercial accounts can make deposits from their place of business. Money market accounts have increased in popularity due to their interest rate structure. Savings accounts include traditional passbook and statement accounts. The Bank s time accounts provide maturities from three months to ten years. Additionally, the Bank offers a variety of retirement deposit accounts to personal and business customers. Deposit service fee income also includes other miscellaneous transaction and convenience services sold to customers through the branch system as part of an overall service relationship.

The Bank offers 100% insurance on all deposits as a result of a combination of insurance from the FDIC and the Massachusetts Depositors Insurance Fund, a mutual insurance fund sponsored by Massachusetts-chartered savings banks.

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The following table presents information concerning average balances and weighted average interest rates on the Bank s interest-bearing deposit accounts for the years indicated. Deposit amounts in the following tables include balances associated with discontinued operations.

Item 1 - Table 8 - Average Balance and Weighted Average Rates for Deposits

	2012			2011			2010		
(In millions)	**Average Balance**	**Percent of Total Average Deposits**	**Weighted Average Rate**	**Average Balance**	**Percent of Total Average Deposits**	**Weighted Average Rate**	**Average Balance**	**Percent of Total Average Deposits**	**Weighted Average Rate**
Demand	$ 870.1	21%	%	$ 377.9	14%	%	$ 279.2	14%	%
NOW	368.4	9	0.2	244.2	9	0.4	199.3	10	0.4
Money market	1,396.2	33	0.4	833.3	31	0.7	597.3	29	0.9
Savings	480.1	11	0.1	369.6	13	0.2	224.3	11	0.3
Time	1,077.5	26	1.6	902.6	33	1.8	749.2	36	2.6
Total	$ 4,192.3	100%	0.6%	$ 2,727.6	100%	0.9%	$ 2,049.3	100%	1.3%

At year-end 2012, the Bank had time deposit accounts in amounts of $100 thousand or more maturing as follows:

Item 1 - Table 9 - Maturity of Deposits > $100,000

Maturity Period (In thousands)	**Amount**	**Weighted Average Rate**
Three months or less	$ 91,591	1.13%
Over 3 months through 6 months	76,007	0.89
Over 6 months through 12 months	143,394	1.38
Over 12 months	310,702	1.74
Total	$ 621,694	1.46%

The Company also uses borrowings from the FHLBB as an additional source of funding, particularly for daily cash management and for funding longer duration assets. FHLBB advances also provide more pricing and option alternatives for particular asset/liability needs. The FHLBB functions as a central reserve bank providing credit for member institutions. As an FHLBB member, the Company is required to own capital stock of the FHLBB. FHLBB borrowings are secured by a blanket lien on most of the Bank s mortgage loans and mortgage-related securities, as well as certain other assets. Advances are made under several different credit programs with different lending standards, interest rates, and range of maturities. The Company has a $15 million trust preferred obligation outstanding and in September 2012 issued $75 million in senior subordinated notes. Subject to certain limitations, the Company can also choose to issue common stock in public stock offerings and can also potentially obtain privately placed common and preferred stock, and subordinated, and senior debt from institutional and private investors.

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DERIVATIVE FINANCIAL INSTRUMENTS

The Company uses interest rate swap instruments for its own account and also offers them for sale to commercial customers for their own accounts, normally in conjunction with commercial loans offered by the Bank to these customers. At year-end 2012, the Company held derivative financial instruments with a total notional amount of $1.31 billion, including $488 million in interest rate contracts with its retail and commercial customers. The Company has a policy for managing its derivative financial instruments, and the policy and program activity are overseen by the Risk Management Committee. Derivative financial instruments with counterparties which are not customers are limited to a select number of national financial institutions. Collateral may be required based on financial condition tests. The Company works with a third-party firm which assists in marketing swap transactions, documenting transactions, and providing information for bookkeeping and accounting purposes.

WEALTH MANAGEMENT SERVICES

The Company s Wealth Management Group provides consultative investment management and trust relationships to individuals, businesses, and institutions, with an emphasis on personal investment management. The Wealth Management Group has built a track record over more than a decade with its dedicated in-house investment management team. In 2011, the Wealth Management business line expanded with the integration of the Renaissance Investment Group in the Legacy merger. At year-end 2012, assets under management (including investment accounts) totaled $1.05 billion. Wealth Management services include investment management, trust administration, estate planning, and private banking. The Bank also provides a full line of investment products, financial planning, and brokerage services utilizing Commonwealth Financial Network as the broker/dealer. The Group s principal operations are in Western New England and it is expanding its services in the Company s other regions.

INSURANCE

As an independent insurance agent, the Berkshire Insurance Group represents a carefully selected group of financially sound, reputable insurance companies offering attractive coverage at competitive prices. The Insurance Group offers a full line of personal and commercial property and casualty insurance. It also offers employee benefits insurance and a full line of personal life, health, and financial services insurance products. Berkshire Insurance Group operates a focused cross-sell program of insurance and banking products through all offices and branches of the Bank with some of the Group s offices located within the Bank s branches. The Group s principal operations are in Western New England, and it is expanding its services in the Company s other regions.

PERSONNEL

At year-end 2012, the Company had 1,012 full time equivalent employees. Total employees increased from 760 at the start of the year (excluding employees assigned to discontinued operations which were divested in January, 2012). The increase was primarily due to business combinations during the year. Berkshire continues to develop its staffing, including staff for new branches and hires related to team development. The Company has also developed staff with targeted skills to deepen the Company s infrastructure. The Company s employees are not represented by a collective bargaining unit.

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SUBSIDIARY ACTIVITIES

The Company wholly-owns two active consolidated subsidiaries: the Bank and Berkshire Insurance Group. The Bank is a Massachusetts-chartered savings bank. One of the Bank s subsidiaries is Berkshire Bank Municipal Bank, which is chartered in the state of New York. Berkshire Insurance Group is incorporated in Massachusetts.

The Company also owns all of the common stock of a Delaware statutory business trust, Berkshire Hills Capital Trust I. The capital trust was organized under Delaware law to facilitate the issuance of trust preferred securities and is not consolidated into the Company s financial results. Its only activity has been the issuance of the $15 million trust preferred security related to the junior subordinated debentures reported in the Company s consolidated financial statements.

Additional information about the subsidiaries is contained in Exhibit 21 to this report.

SEGMENT REPORTING

The Company has two reportable operating segments, banking and insurance. Banking includes the activities of the Bank and its subsidiaries, which provide commercial and retail banking services. Insurance includes the activities of Berkshire Insurance Group, which provides commercial and consumer insurance services. The only other consolidated financial activity of the Company is that of the Company s role as parent of the Bank and Berkshire Insurance Group. For more information about the Company s reportable operating segments, see the related note in the consolidated financial statements.

REGULATION AND SUPERVISION

General

Berkshire Hills Bancorp is a Delaware corporation and savings and loan holding company registered with the Federal Reserve Board. The Bank s deposits are insured up to applicable limits by the FDIC and by the Depositors Insurance Fund of Massachusetts for amounts in excess of the FDIC insurance limits. The Bank is subject to extensive regulation by the Massachusetts Commissioner of Banks (the Commissioner) as its chartering agency, and by the FDIC, as its deposit insurer. The Bank is required to file reports with the Commissioner and the FDIC concerning its activities and financial condition in addition to obtaining regulatory approvals prior to entering into certain transactions such as mergers with, or acquisitions of, other savings institutions. The Commissioner and the FDIC conduct periodic examinations to test the Bank s safety and soundness and compliance with various regulatory requirements. As a savings and loan holding company, Berkshire Hills Bancorp is required by federal law to file reports with, and otherwise comply with the rules and regulations of, the Federal Reserve Board. The regulatory structure gives the regulatory authorities extensive discretion in connection with their supervisory and enforcement activities and examination policies, including policies with respect to the classification of assets and the establishment of adequate loan loss reserves for regulatory purposes. Any change in such regulatory requirements and policies, whether by the Commissioner, the Massachusetts legislature, the FDIC, the Federal Reserve Board or Congress, could have a material adverse impact on Berkshire Hills Bancorp, the Bank and their operations.

The 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) made extensive changes in the regulation of insured depository institutions. Under the Dodd-Frank Act, the Office of Thrift Supervision (OTS), the previous federal regulator of Berkshire Hills Bancorp, was eliminated. At the same time, responsibility for the regulation and supervision of savings and loan holding companies, such as Berkshire Hills Bancorp, was transferred

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to the Federal Reserve Board, which also supervises bank holding companies. The transfer took place as of July 21, 2011.

Additionally, the Dodd-Frank Act created a new Consumer Financial Protection Bureau as an independent bureau of the Federal Reserve Board. The Consumer Financial Protection Bureau assumed responsibility for the implementation of the federal financial consumer protection and fair lending laws and regulations, a function previously assigned to prudential regulators, and has authority to impose new requirements. However, institutions of less than $10 billion in assets, such as the Bank, will continue to be examined for compliance with consumer protection and fair lending laws and regulations by, and be subject to the primary enforcement authority of their prudential regulator rather than the Consumer Financial Protection Bureau.

In addition, the Dodd-Frank Act directed changes in the way that institutions are assessed for deposit insurance, mandated the imposition of consolidated capital requirements on savings and loan holding companies such as Berkshire Hills Bancorp, required originators of certain securitized loans to retain a percentage of the risk for the transferred loans, stipulated regulatory rate-setting for certain debit card interchange fees, repealed restrictions on the payment of interest on commercial demand deposits and contained a number of reforms related to mortgage originations. Many of the provisions of the Dodd-Frank Act are subject to delayed effective dates and/or require the issuance of implementing regulations. Their impact on operations cannot yet be fully assessed. However, there is a significant possibility that the Dodd-Frank Act will, at a minimum, result in increased regulatory burden, compliance costs and interest expense for the Company and the Bank.

Certain regulatory requirements applicable to the Company, including certain changes made by the Dodd-Frank Act, are referred to below or elsewhere herein. The description of statutory provisions and regulations applicable to savings institutions and their holding companies set forth in this Form 10-K does not purport to be a complete description of such statutes and regulations and their effects on the Company and is qualified in its entirety by reference to the actual laws and regulations.

Massachusetts Banking Laws and Supervision

General. As a Massachusetts-chartered savings bank, the Bank is subject to supervision, regulation and examination by the Commissioner and to various Massachusetts statutes and regulations which govern, among other things, investment powers, lending and deposit-taking activities, borrowings, maintenance of surplus and reserve accounts, distribution of earnings and payment of dividends. In addition, the Bank is subject to Massachusetts consumer protection and civil rights laws and regulations. The approval of the Commissioner is required for a Massachusetts-chartered bank to establish or close branches, merge with other financial institutions, organize a holding company, issue stock and undertake certain other activities.

Massachusetts regulations generally allow Massachusetts banks to engage in activities permissible for federally chartered banks or banks chartered by another state. The Commissioner has adopted procedures reducing regulatory burdens and expense and expediting branching by well-capitalized and well-managed banks.

Dividends. A Massachusetts stock bank may declare cash dividends from net profits not more frequently than quarterly and non-cash dividends at any time. No dividends may be declared, credited or paid if the bank s capital stock is impaired. The approval of the Commissioner is required if the total of all dividends declared in any calendar year exceeds the total of its net profits for that year combined with its retained net profits of the preceding two years. Net profits for this purpose means the remainder of all earnings from current operations plus actual recoveries on loans and

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investments and other assets after deducting from the total thereof all current operating expenses, actual losses, accrued dividends on preferred stock, if any, and all federal and state taxes.

Loans to One Borrower Limitations. Massachusetts banking law grants broad lending authority. However, with certain limited exceptions, total obligations of one borrower to a bank may not exceed 20.0% of the total of the bank s capital, which is defined under Massachusetts law as the sum of the bank s capital stock, surplus account and undivided profits.

Loans to a Bank s Insiders. Massachusetts banking laws prohibit any executive officer, director or trustee from borrowing, otherwise becoming indebted, or becoming liable for a loan or other extension of credit by such bank to any other person, except for any of the following loans or extensions of credit: (i) loans or extensions of credit, secured or unsecured, to an officer of the bank in an amount not exceeding $100,000; (ii) loans or extensions of credit intended or secured for educational purposes to an officer of the bank in an amount not exceeding $200,000; (iii) loans or extensions of credit secured by a mortgage on residential real estate to be occupied in whole or in part by the officer to whom the loan or extension of credit is made, in an amount not exceeding $750,000; and (iv) loans or extensions of credit to a director or trustee of the bank who is not also an officer of the bank in an amount permissible under the bank s loan to one borrower limit.

The loans listed above require approval of the majority of the members of the Bank s Board of Directors, excluding any member involved in the loan or extension of credit. No such loan or extension of credit may be granted with an interest rate or other terms that are preferential in comparison to loans granted to persons not affiliated with the savings bank.

Investment Activities. In general, Massachusetts-chartered savings banks may invest in preferred and common stock of any corporation organized under the laws of the United States or any state provided such investments do not involve control of any corporation and do not, in the aggregate, exceed 4.0% of the bank s deposits. Massachusetts-chartered savings banks may in addition invest an amount equal to 1.0% of their deposits in stocks of Massachusetts corporations or companies with substantial employment in Massachusetts which have pledged to the Commissioner that such monies will be used for further development within the Commonwealth. However, these powers are constrained by federal law.

Regulatory Enforcement Authority. Any Massachusetts-chartered bank that does not operate in accordance with the regulations, policies and directives of the Commissioner may be sanctioned for non-compliance, including seizure of the property and business of the bank and suspension or revocation of its charter. The Commissioner may, under certain circumstances, suspend or remove officers or directors who have violated the law, conducted the bank s business in a manner which is unsafe, unsound or contrary to the depositors interests or been negligent in the performance of their duties. In addition, upon finding that a bank has engaged in an unfair or deceptive act or practice, the Commissioner may issue an order to cease and desist and impose a fine on the bank concerned. Finally, Massachusetts consumer protection and civil rights statutes applicable to the Bank permit private individual and class action lawsuits and provide for the rescission of consumer transactions, including loans, and the recovery of statutory and punitive damage and attorney s fees in the case of certain violations of those statutes.

Depositors Insurance Fund. All Massachusetts-chartered savings banks are required to be members of the Depositors Insurance Fund (DIF), a corporation that insures savings bank deposits in excess of federal deposit insurance coverage. The DIF is a private, industry-sponsored insurance company and is not backed by the federal government or the Commonwealth of Massachusetts. The DIF is authorized to charge savings banks an annual assessment for its coverage. Such assessments may vary based on the risk classification assigned to the institution.

The combination of FDIC and DIF insurance provides customers of Massachusetts-chartered savings banks with full deposit insurance on all their deposit accounts. DIF insurance coverage requires no applications or special forms.

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Depositors automatically receive this added insurance benefit at no cost whenever they make a deposit to a new or existing account at a DIF member bank. The DIF is examined annually by the Massachusetts Division of Banks and audited by an independent auditor.

Massachusetts has other statutes or regulations that are similar to the federal provisions discussed below.

Federal Regulations

Capital Requirements. Under FDIC regulations, federally insured state-chartered banks that are not members of the Federal Reserve System (state non-member banks), such as the Bank, are required to comply with minimum leverage capital requirements. For an institution determined by the FDIC to not be anticipating or experiencing significant growth and to be in general a strong banking organization, rated composite 1 under the Uniform Financial Institutions Rating System established by the Federal Financial Institutions Examination Council, the minimum capital leverage requirement is a ratio of Tier 1 capital to total average assets (as defined) of 3%. For all other institutions, the minimum leverage capital ratio is not less than 4%. Tier 1 capital is the sum of common stockholders equity, noncumulative perpetual preferred stock (including any related surplus) and minority investments in certain subsidiaries, less intangible assets (except for certain servicing rights and credit card relationships) and certain other items.

The Bank must also comply with the FDIC risk-based capital guidelines. The FDIC guidelines require state non-member banks to maintain certain levels of regulatory capital in relation to regulatory risk-weighted assets. Risk-based capital ratios are determined by allocating assets and specified off-balance sheet items to four risk-weighted categories ranging from 0% to 100%, with higher levels of capital being required for the categories perceived as representing greater risk.

State non-member banks must maintain a minimum ratio of total capital to risk-weighted assets of at least 8%, of which at least one-half must be Tier 1 capital. Total capital consists of Tier 1 capital plus Tier 2 or supplementary capital items, which include allowances for loan losses in an amount of up to 1.25% of risk-weighted assets, cumulative preferred stock, a portion of the net unrealized gain on equity securities and other capital instruments. The includable amount of Tier 2 capital cannot exceed the amount of the institution s Tier 1 capital.

As a savings and loan holding company, the Company is not currently subject to any separate regulatory capital requirements, although this is expected to change in the future. The Bank s regulatory capital is included in the Stockholders Equity note of the Company s financial statements in Item 8 of this report. At year-end 2012, the Bank met each of its capital requirements.

On June 6, 2012, the FDIC and the other federal bank regulatory agencies issued a series of proposed rules that would revise their leverage and risk-based capital requirements and the method for calculating risk-weighted assets to make them consistent with agreements that were reached by the Basel Committee on Banking Supervision and certain provisions of the Dodd-Frank Act. The proposed rules would apply to all depository institutions, top-tier bank holding companies with total consolidated assets of $500 million or more and top-tier savings and loan holding companies. Among other things, the proposed rules establish a new common equity Tier 1 minimum capital requirement (4.5% of risk-weighted assets) and a higher minimum Tier 1 capital to risk-based assets requirement (6% of risk-weighted assets) and assign higher risk weight (150%) to exposures that are more than 90 days past due or are on nonaccrual status and certain commercial real estate facilities that finance the acquisition, development or construction of real property. The proposed rules also require unrealized gains and losses on certain securities holdings to be included for purposes of calculating regulatory capital requirements. The proposed rules limit a banking organization s capital distributions and certain discretionary bonus payments if the banking organization does not hold a capital conservation buffer

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consisting of a specified amount of common equity Tier 1 capital in addition to the amount necessary to meet its minimum risk-based capital requirements. The proposed rules indicated that the final rules would become effective on January 1, 2013, and the changes set forth in the final rules will be phased in from January 1, 2013 through January 1, 2019. However, the agencies have recently indicated that, due to the volume of public comments received, the final rule has been delayed past January 1, 2013.

Interstate Banking and Branching. Federal law permits a bank, such as the Bank, to acquire an institution by merger in a state other than Massachusetts unless the other state has opted out. Federal law, as amended by the Dodd-Frank Act, authorizes de novo branching into another state to the extent that the target state allows its state chartered banks to establish branches within its borders. The Bank operates branches in New York, Vermont, and Connecticut, as well as Massachusetts. At its interstate branches, the Bank may conduct any activity that is authorized under Massachusetts law that is permissible either for a savings bank chartered in that state (subject to applicable federal restrictions) or a branch in that state of an out-of-state national bank. The New York State Superintendent of Banks, the Vermont Commissioner of Banking and Insurance, and the Connecticut Commissioner of Banking may exercise certain regulatory authority over the Bank s New York, Vermont, and Connecticut branches.

Prompt Corrective Regulatory Action. Federal law requires, among other things, that federal bank regulatory authorities take prompt corrective action with respect to banks that do not meet minimum capital requirements. For these purposes, the law establishes three categories of capital deficient institutions: undercapitalized, significantly undercapitalized and critically undercapitalized.

An institution is deemed to be well capitalized if it has a total risk-based capital ratio of 10% or greater, a Tier 1 risk-based capital ratio of 6% or greater, and a leverage ratio of 5% or greater. An institution is adequately capitalized if it has a total risk-based capital ratio of 8% or greater, a Tier 1 risk-based capital ratio of 4% or greater and generally a leverage ratio of 4% or greater. An institution is undercapitalized if it has a total risk-based capital ratio of less than 8%, a Tier 1 risk-based capital ratio of less than 4%, or generally a leverage ratio of less than 4% (3% or less for institutions with the highest examination rating). An institution is deemed to be significantly undercapitalized if it has a total risk-based capital ratio of less than 6%, a Tier 1 risk-based capital ratio of less than 3%, or a leverage ratio of less than 3%. An institution is considered to be critically undercapitalized if it has a ratio of tangible equity (as defined in the regulations) to total assets that is equal to or less than 2%. At year-end 2012, the Bank met the conditions to be classified as a well capitalized institution.

Undercapitalized banks must adhere to growth, capital distribution (including dividend) and other limitations and are required to submit a capital restoration plan. No institution may make a capital distribution, including payment as a dividend, if it would be undercapitalized after the payment. A bank s compliance with such plans is required to be guaranteed by its parent holding company in an amount equal to the lesser of 5% of the institution s total assets when deemed undercapitalized or the amount needed to comply with regulatory capital requirements. If an undercapitalized bank fails to submit an acceptable plan, it is treated as if it is significantly undercapitalized. Significantly undercapitalized banks must comply with one or more of a number of additional restrictions, including but not limited to an order by the FDIC to sell sufficient voting stock to become adequately capitalized , requirements to reduce assets and cease receipt of deposits from correspondent banks or dismiss directors or officers, and restrictions on interest rates paid on deposits, compensation of executive officers and capital distributions by the parent holding company. Critically undercapitalized institutions must comply with additional sanctions including, subject to a narrow exception, the appointment of a receiver or conservator within 270 days after it obtains such status.

The recently proposed rules that would increase regulatory capital requirements would adjust the prompt corrective action categories accordingly.

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Transactions with Affiliates. Transactions between depository institutions and their affiliates are governed by Sections 23A and 23B of the Federal Reserve Act. In a holding company context, at a minimum, the parent holding company of a savings bank and any companies which are controlled by such parent holding company are affiliates of the savings bank. Generally, Section 23A limits the extent to which the savings bank or its subsidiaries may engage in covered transactions, such as loans, with any one affiliate to 10% of such savings bank s capital stock and surplus, and contains an aggregate limit on all such transactions with all affiliates to 20% of capital stock and surplus. Loans to affiliates and certain other specified transactions must comply with specified collateralization requirements. Section 23B requires that transactions with affiliates be on terms that are no less favorable to the savings bank or its subsidiary as similar transactions with non-affiliates.

Further, federal law restricts an institution with respect to loans to directors, executive officers, and principal stockholders (insiders). Loans to insiders and their related interests may not exceed, together with all other outstanding loans to such persons and affiliated entities, the institution s total capital and surplus. Loans to insiders above specified amounts must receive the prior approval of the Board of Directors. Further, loans to insiders must be made on terms substantially the same as offered in comparable transactions to other persons, except that such insiders may receive preferential loans made under a benefit or compensation program that is widely available to the Bank s employees and does not give preference to the insider over the employees. Federal law places additional limitations on loans to executive officers.

Enforcement. The FDIC has extensive enforcement authority over insured savings banks, including the Bank. This enforcement authority includes, among other things, the ability to assess civil money penalties, issue cease and desist orders and to remove directors and officers. In general, these enforcement actions may be initiated in response to violations of laws and regulations and unsafe or unsound practices. The FDIC has authority under federal law to appoint a conservator or receiver for an insured bank under certain circumstances.

Insurance of Deposit Accounts**.** The Bank s deposit accounts are insured by the Deposit Insurance Fund of the FDIC up to applicable legal limits, and, as discussed above under Massachusetts Banking Laws and Supervision Depositors Insurance Fund, by the Massachusetts Depositors Insurance Fund for amounts in excess of federal deposit insurance coverage.

The FDIC insures deposits up to the standard maximum deposit insurance amount (SMDIA) of $250 thousand. The deposit insurance limit was increased in response to the Dodd-Frank Act, which, among other provisions, made permanent the increase in the SMDIA from $100 thousand to $250 thousand. Additionally, in November 2010, pursuant to the Dodd-Frank Act, the FDIC issued a final rule to provide separate temporary coverage for noninterest-bearing transaction accounts. The final rule indicates that all funds held in noninterest-bearing transaction accounts were fully insured, without limit, and that this unlimited coverage was separate from, and in addition to, the coverage provided to depositors with respect to other accounts held at an insured depository institution, such as the Bank. This provision for non-interest bearing transaction accounts became effective December 31, 2010 and terminated on December 31, 2012.

The FDIC has adopted a risk-based insurance assessment system. The FDIC assigns an institution to one of four risk categories based on the institution s financial condition and supervisory ratings. An institution s assessment rate depends on the capital category and supervisory category to which it is assigned, based on a final rule which became effective in April 2011. Under the final rule, banks in Risk Category 1 have a base assessment rate of 5-9 basis points and those in Risk Category 2 have a rate of 14 basis points, subject to adjustment based on certain risk additional risk factors specified by the FDIC. The overall range, including prospective adjustments, is 2.5 to 45 basis points.

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Assessment rates are scheduled to decline as the FDIC Reserve Ratio improves. As required by the Dodd-Frank Act, FDIC assessments are now based on each institution s total assets less Tier 1 capital, rather than deposits, as was previously the case. The FDIC has stated that nearly all of the 7,600-plus institutions with assets less than $10 billion will pay smaller assessments as a result of this final rule.

In the fourth quarter of 2009, due to stress on the insurance fund, the FDIC voted to require insured institutions to prepay thirteen quarters of estimated insurance assessments. The estimated quarterly risk-based assessments for the fourth quarter of 2009 and for all of 2010, 2011, and 2012 were paid by the Bank on December 30, 2009.

In addition, FDIC insured institutions are required to pay assessments to the Federal Deposit Insurance Corporation to fund interest payments on bonds issued by the Financing Corporation, an agency of the federal government established to recapitalize a predecessor to deposit insurance fund. These assessments will continue until the Financing Corporation bonds mature in 2017 through 2019. The assessment rate is adjusted quarterly to reflect changes in the assessment bases of the fund based on quarterly Call Report and Thrift Financial Report submissions and for the quarter ended December 31, 2012 amounted to .66 basis points of total assets less Tier 1 capital.

Insurance of deposits may be terminated by the FDIC upon a finding that the institution has engaged in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, regulation, rule, order or condition imposed by a regulator. Management does not know of any practice, condition or violation that might lead to termination of deposit insurance.

The Dodd-Frank Act increased the minimum target DIF ratio from 1.15% of estimated insured deposits to 1.35% of estimated insured deposits. The FDIC must seek to achieve the 1.35% ratio by September 30, 2020. Insured institutions with assets of $10 billion or more are supposed to fund the increase. The Dodd-Frank Act eliminated the 1.50% maximum fund ratio, instead leaving it to the discretion of the FDIC. The FDIC has recently exercised that discretion by establishing a long range fund ratio of 2.00%.

The FDIC has authority to increase insurance assessments. A significant increase in insurance premiums would likely have an adverse effect on the operating expenses and results of operations of the Bank. Management cannot predict what insurance assessment rates will be in the future.

Federal Home Loan Bank System. The Bank is a member of the Federal Home Loan Bank system, which consists of 12 regional Federal Home Loan Banks that provide a central credit facility primarily for member institutions. The Bank, as a member, is required to acquire and hold shares of capital stock in the FHLBB.

The Federal Home Loan Banks are required to provide funds for certain purposes including contributing funds for affordable housing programs. These requirements, and general financial results, could reduce the amount of dividends that the Federal Home Loan Banks pay to their members and result in the Federal Home Loan Banks imposing a higher rate of interest on advances to their members. Historically, the FHLBB paid dividends to member banks based on money market interest rates. Due to losses initially reported in the fourth quarter of 2008, the FHLBB suspended its dividend to members in the first quarter of 2009. The dividend remained suspended through year-end 2010, but was restored to a nominal amount in the first quarter of 2011 and has improved in subsequent quarters, though is still much lower than 2008 levels.

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Holding Company Regulation

General. Federal law allows a state savings bank that qualifies as a Qualified Thrift Lender, discussed below, to elect to be treated as a savings association for purposes of the savings and loan holding company provisions of federal law. Such election allows its holding company to be regulated as a savings and loan holding company by the Federal Reserve Board rather than as a bank holding company by the Federal Reserve Board under the federal Bank Holding Company Act. As such, the Parent is registered with the Federal Reserve Board and must adhere to the Federal Reserve Board s regulations and reporting requirements. In addition, the Federal Reserve Board may examine, supervise and take enforcement action against the Parent and its non-savings institution subsidiaries. Among other things, this authority permits the Federal Reserve Board to restrict or prohibit activities that are determined to be a serious risk to the subsidiary savings institution. By regulation, the Federal Reserve Board may restrict or prohibit the Bank from paying dividends.

The Dodd-Frank Act provided for the elimination of the OTS and transferred its authority over and responsibilities for savings and loan holding companies to the Federal Reserve Board. That transfer was effective July 21, 2011. The Gramm-Leach-Bliley Act of 1999 provided that unitary savings and loan holding companies may engage in activities permitted to a financial holding company under that legislation and those permitted for multiple savings and loan holding companies. A financial holding company may engage in activities that are financial in nature, including underwriting equity securities and insurance, activities that are incidental or complementary to financial activities. The Dodd-Frank Act added that any savings and loan holding company that engages in activities permissible for a financial holding company must meet the qualitative requirements for a bank holding company to be a financial holding company and conduct the activities in accordance with the requirements that would apply to a financial holding company s conduct of the activity. A multiple savings and loan holding company is generally limited to activities permissible for bank holding companies under Section 4(c)-(8) of the Bank Holding Company Act and certain additional activities authorized by Federal Reserve Board regulations, subject to the prior approval of the Federal Reserve Board. Certain activities require prior Federal Reserve Board approval.

Federal law prohibits a savings and loan holding company from, directly or indirectly, acquiring more than 5% of the voting stock of another savings association or savings and loan holding company or from acquiring such an institution or company by merger, consolidation or purchase of its assets, without prior written approval of the Federal Reserve Board. In evaluating applications by holding companies to acquire savings associations, the Federal Reserve Board considers factors such as the financial and managerial resources and future prospects of the Company and the institution involved, the effect of the acquisition on the risk to the insurance fund, the convenience and needs of the community and competitive factors.

To be regulated as a savings and loan holding company (rather than as a bank holding company), the bank must qualify as a Qualified Thrift Lender. To qualify as a Qualified Thrift Lender, the bank must maintain compliance with the test for a domestic building and loan association, as defined in the Internal Revenue Code, or with a Qualified Thrift Lender Test. Under the Qualified Thrift Lender Test (the QLT Test), a savings institution is required to maintain at least 65% of its portfolio assets (total assets less: (1) specified liquid assets up to 20% of total assets; (2) intangibles, including goodwill; and (3) the value of property used to conduct business) in certain qualified thrift investments (primarily residential mortgages and related investments, including certain mortgage-backed securities) in at least 9 months out of each 12-month period. At year-end 2012, the Bank maintained at least 65% of its portfolio assets in qualified thrift investments and met the QTL Test for the year.

Savings and loan holding companies have not historically been subjected to consolidated regulatory capital requirements. However, the Dodd-Frank Act requires the Federal Reserve Board to set, for all depository institution

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holding companies, minimum consolidated capital levels that are as stringent as those required for the insured depository institution subsidiaries. The components of Tier 1 capital must be restricted to capital instruments that are currently considered to be Tier 1 capital for insured depository institutions. That would exclude from Tier 1 capital such instruments as trust preferred securities and cumulative preferred stock that are currently permitted for bank holding companies. The Dodd-Frank Act provides that instruments issued before May 19, 2010 will be grandfathered for companies with consolidated assets of $15 billion or less. The Dodd-Frank Act further provides that holding companies that were not regulated by the Federal Reserve Board as of May 19, 2010 (which would include most savings and loan holding companies) are subject to a five-year transition period from the July 21, 2010 date of enactment of the Dodd-Frank Act before such capital requirements apply. The proposed capital rules discussed earlier would implement the consolidated capital requirements for savings and loan holding companies. However, the proposed rules did not incorporate the referenced grandfather for instruments issued before May 19, 2010 or the transition period, notwithstanding the Dodd-Frank statutory language, so it is uncertain whether any final rule will do so.

The Dodd-Frank Act also extended the source of strength doctrine to savings and loan holding companies. The regulatory agencies must promulgate regulations implementing the source of strength policy, which requires holding companies to act as a source of strength to their subsidiary depository institutions by providing capital, liquidity and other support in times of financial distress. Further, the Federal Reserve Board has issued a policy statement regarding the payment of dividends by bank holding companies that it has suggested is applicable to savings and loan holding companies as well. In general, the policy provides that dividends should be paid only out of current earnings and if the prospective rate of earnings retention by the holding company appears consistent with the organization s capital needs, asset quality and overall financial condition. Regulatory guidance provides for regulatory consultation as to capital distributions in certain circumstances such as where the company s net income for the past four quarters, net of dividends previously paid over that period, is insufficient to fully fund the dividend or the company s overall rate of earnings retention is inconsistent with the company s capital needs and overall financial condition. The ability of a savings and loan holding company to pay dividends may be restricted if a subsidiary bank becomes undercapitalized. In addition, a subsidiary savings association of a saving and loan holding company must file prior notice with, and receive the nonobjection of, the Federal Reserve Board, before paying dividends to their parent savings and loan holding company. These regulatory policies could affect the ability of Berkshire Hills Bancorp to pay dividends or otherwise engage in capital distributions.

Acquisition of the Company. Under the Federal Change in Bank Control Act, a notice must be submitted to the Federal Reserve Board if any person (including a company), or group acting in concert, seeks to acquire control of a savings and loan holding company. A change in control may occur, and prior notice is required, upon the acquisition of 10% or more of the Company s outstanding voting stock, unless the Federal Reserve Board has found that the acquisition will not result in a change of control of the Company.

Massachusetts Holding Company Regulation. In addition to the federal holding company regulations, a bank holding company organized or doing business in Massachusetts must comply with regulations under Massachusetts law. Approval of the Massachusetts regulatory authorities would be required for the Company to acquire 25% or more of the voting stock of another depository institution. Similarly, prior regulatory approval would be necessary for any person or company to acquire 25% or more of the voting stock of the Company. The term bank holding company, for the purpose of Massachusetts law, is defined generally to include any company which, directly or indirectly, owns, controls or holds with power to vote more than 25% of the voting stock of each of two or more banking institutions, including commercial banks and state co-operative banks, savings banks and savings and loan association and national banks, federal savings banks and federal savings and loan associations. In general, a holding company controlling, directly or indirectly, only one banking institution will not be deemed to be a bank holding company for the purposes of

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Massachusetts law. Under Massachusetts law, the prior approval of the Board of Bank Incorporation is required before any of the following: any company becoming a bank holding company; any bank holding company acquiring direct or indirect ownership or control of more than 5% of the voting stock of, or all or substantially all of the assets of, a banking institution; or any bank holding company merging with another bank holding company. Although Berkshire Hills Bancorp is not a bank holding company for purposes of Massachusetts law, any future acquisition of ownership, control, or the power to vote 25% or more of the voting stock of another banking institution or bank holding company would cause it to become such.

Legislation. The U.S. Congress, state lawmaking bodies and federal and state regulatory agencies continue to consider a number of wide-ranging and comprehensive proposals for altering the structure, regulation and competitive relationships of the nation s financial institutions. The Federal Reserve Board in coordination with the Department of the Treasury, the Office of the Comptroller of the Currency, and the FDIC, have proposed implementation of new risk-based capital guidelines incorporating policies outlined by the Basel Committee. The Company is in the process of assessing the impact of the changes proposed by this rulemaking and cannot predict the extent to which the Company may be affected thereby.

Berkshire Bank Municipal Bank

Berkshire Bank Municipal Bank is a state-chartered limited purpose commercial bank in New York, established to accept deposits of municipalities and other governmental entities in the State of New York. Berkshire Bank Municipal Bank is subject to extensive regulation, examination and supervision by the New York State Superintendent of Banks, as its primary regulator, and the FDIC, as the deposit insurer. It is also subject to regulation as to certain matters by the Federal Reserve Board. As of year-end 2012, Berkshire Bank Municipal Bank met all of its capital requirements and met the capital conditions to be classified as a well capitalized institution.

Other Regulations

Consumer Protection Laws. The Bank is subject to federal and state consumer protection statues and regulations including, but not limited to, the following:

- Truth-In-Lending Act, governing disclosures of credit terms to consumer borrowers;

- Home Mortgage Disclosure Act, requiring financial institutions to provide certain information about home mortgage and refinance loans;

- Equal Credit Opportunity Act, prohibiting discrimination on the basis of race, creed or other prohibited factors in extending credit;

- Fair Credit Reporting Act, governing the provision of consumer information to credit reporting agencies and the use of consumer information;

- Fair Debt Collection Act, governing the manner in which consumer debts may be collected by collection agencies; and

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- Electronic Funds Transfer Act, governing automatic deposits to and withdrawals from deposit accounts and customers rights and liabilities arising from the use of automated teller machines and other electronic banking services.

The Bank also is subject to federal laws protecting the confidentiality of consumer financial records, and limiting the ability of the institution to share non-public personal information with third parties.

The Community Reinvestment Act (CRA) establishes a requirement for federal banking agencies that, in connection with examinations of financial institutions within their jurisdiction, the agencies evaluate the record of the financial institutions in meeting the credit needs of their local communities, including low- and moderate-income neighborhoods, consistent with the safe and sound operation of those institutions. These factors are also considered in evaluating mergers, acquisitions and applications to open a branch or new facility. Under the CRA, institutions are assigned a rating of outstanding, satisfactory, needs to improve, or substantial non-compliance. A less than satisfactory rating would result in suspension of any growth of the Bank through acquisitions or opening de novo branches until the rating is improved. As of the most recent CRA examination by the FDIC, the Bank s CRA rating was satisfactory.

Anti-Money Laundering Laws. The Bank is subject to extensive anti-money laundering provisions and requirements, which require the institution to have in place a comprehensive customer identification program and an anti-money laundering program and procedures. These laws and regulations also prohibit financial institutions from engaging in business with foreign shell banks; require financial institutions to have due diligence procedures and, in some cases, enhanced due diligence procedures for foreign correspondent and private banking accounts; and improve information sharing between financial institutions and the U.S. government. The Bank has established policies and procedures intended to comply with these provisions.

TAXATION

The Company reports its income on a calendar year basis using the accrual method of accounting. This discussion of tax matters is only a summary and is not a comprehensive description of the tax rules applicable to the Company and its subsidiaries. Further discussion of income taxation is contained in the income taxes note to the consolidated financial statements.

Federal

The federal income tax laws apply to the Company in the same manner as to other corporations with some exceptions. Corporations may exclude from income 100% of dividends received from the Bank and from Berkshire Insurance Group as members of the same affiliated group of corporations. For federal income tax purposes, corporations may carry back net operating losses to the preceding two taxable years and forward to the succeeding twenty taxable years, subject to certain limitations.

State

The Company reports income on a calendar year basis to the Commonwealth of Massachusetts. The Massachusetts income tax rate for financial institutions was 9.5% in 2011 and declined to 9.0% in 2012 and thereafter. The Company s taxable income under Massachusetts tax law includes gross income as defined under the Internal Revenue Code, plus interest from non-Massachusetts municipal obligations, less deductions, but not the credits, allowable under the provisions of the Internal Revenue Code. Carry forwards and carry backs of net operating losses are not allowed under Massachusetts tax law. Also no deduction is allowed for bonus depreciation or state income taxes paid.

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Massachusetts tax law generally permits special tax treatment for a qualifying limited purpose securities corporation. The Bank s three securities corporations all qualify for this treatment, and are taxed at a 1.3% rate on their gross income.

The Company also pays certain franchise taxes annually in the states of Vermont, New York, and Connecticut. These taxes were immaterial to the Company s results.

ITEM 1A. RISK FACTORS

Overall Business Risks

The Company s Business May Be Adversely Affected by Conditions in the Financial Markets and Economic Conditions Generally and Locally

National and local conditions reflect low growth conditions and heightened uncertainty related to public policy. Stubbornly high unemployment has led to sustained monetary stimulus by the Federal Reserve Bank. Repetitive federal fiscal and treasury deadlines contribute to uncertainty and the potential for market disruption. Private sector growth has been substantially offset by public sector austerity. Private sector liquidity has grown and investment has been modest, while public sector leverage has increased due to long term imbalances in taxing and spending. Regulation of the financial system continues to evolve and add to uncertainty and operating burdens. Real estate markets have improved from the lows reached after the 2008 decline, and recovery is uneven across U.S. regional markets. A deterioration of business and economic conditions, particularly in our local markets, could adversely affect the credit quality of the Company s loans, results of operations and financial condition.

Lending

Continued and Prolonged Deterioration in the Housing Sector, Commercial Real Estate, and Related Markets May Adversely Affect Our Business and Financial Results.

Commercial and residential real estate markets have been impacted by the broader economic conditions previously discussed. Real estate lending is a major business activity for the Company. Real estate market conditions affect the value and marketability of this real estate collateral, and they also affect the cash flows, liquidity, and net worth of many borrowers whose operations and finances depend on real estate market conditions. Adverse conditions in our market areas could reduce our growth rate, affect the ability of our customers to repay their loans and generally affect our financial condition and results of operations.

Our Emphasis on Commercial Lending May Expose Us to Increased Lending Risks, Which Could Hurt Our Profits.

We plan to continue to emphasize the origination of commercial loans, which generally exposes us to a greater risk of nonpayment and loss because repayment of such loans often depends on the successful operations and income stream of the borrowers. Commercial loans are historically more sensitive to economic downturns. Such sensitivity includes potentially higher default rates and possible reduction of collateral values. Commercial lending involves larger loan sizes and larger relationship exposures, which can have a greater impact on profits in the event of adverse loan performance. The majority of the Company s commercial loans is secured by real estate and subject to the previously discussed real

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estate risk factors. Commercial lending sometimes involves construction or other development financing, which is dependent on the future success of new operations. The Company s commercial lending activities have extended across wider parts of its New England and New York markets into areas where the Company has less business experience. The Company s commercial lending includes asset based lending, which depends on the Company s processes for monitoring and being able to liquidate collateral on which these loans rely. Commercial loans may increase as a percentage of total loans, and commercial lending may continue to expose the company to increased risks.

Our Allowance for Loan Losses May Prove to be Insufficient to Absorb Losses in Our Loan Portfolio.

Like all financial institutions, we maintain an allowance for loan losses which is our estimate of the probable losses that are inherent in the loan portfolio as of the financial statement date. However, our allowance for loan losses may not be sufficient to cover actual loan losses, and future provisions for loan losses could materially and adversely affect our operating results. The accounting measurements related to impairment and the loan loss allowance require significant estimates which are subject to uncertainty and changes relating to new information and changing circumstances. Additionally, the allowance can only reflect those losses which are reasonably estimable, and there are constraints in our ability to estimate losses in this period of unusual economic and financial stress. This is particularly relevant for our estimates of losses for pools of loans. Accordingly, at any time, there may be probable losses inherent in the portfolio but which we are not reasonably able to estimate until additional information emerges which can form the basis for a reasonable estimate.

State and federal regulators, as an integral part of their examination process, periodically review our allowance for loan losses and may require us to increase our allowance for loan losses by recognizing additional provisions for loan losses charged to expense, or to decrease our allowance for loan losses by recognizing loan charge-offs, net of recoveries. Any such additional provisions for loan losses or charge-offs, as required by these regulatory agencies, could have a material adverse effect on our financial condition and results of operations.

Our Estimates of Discounts on Acquired Loans With Deteriorated Credit Quality May Be Inadequate.

Under generally accepted principles for business combinations, there is no loan loss allowance recorded for acquired loans, which are recorded at net fair value on the acquisition date. This net fair value generally includes embedded loss estimates for acquired loans with deteriorated credit quality. These estimates are based on projections of expected cash flows for these problem loans, which in many cases rely on estimates deriving from the liquidation of collateral. If the projections are inadequate, the fair value estimates may exceed the actual collectability of the balances, and this may result in the related loans being considered impaired, which would result in a reduction in interest income. If fair value estimates differ from actual collectability, then tangible book value of the Company will have been recorded incorrectly at the time of the acquisition, and subsequent earnings will differ from original estimates. Measures of tangible book value and earnings impacts of business combinations are frequently used in evaluating the merits and value of business combinations.

Operating

Our Expansion, Growth, and Acquisitions Could Negatively Impact Earnings If Not Successful.

We plan to achieve significant growth organically, by geographic expansion, through business line expansion, and through acquisitions. We have recently expanded into new geographic markets and anticipate that we will continue to expand into additional geographic markets as we grow as a regional bank. The success of this expansion depends on our ability to continue to maintain and develop an infrastructure appropriate to support and integrate such growth. Also, our success

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depends on the acceptance by customers of us and our services in these new markets and, in the case of expansion through acquisitions, our success depends on many factors, including the long-term recruitment and retention of key personnel and acquired customer relationships. The profitability of our expansion strategy also depends on whether the income we generate in the new markets will offset the increased expenses of operating a larger entity with increased personnel, more branch locations and additional product offerings.

We continue to identify and evaluate opportunities to expand through acquisition of banks, insurance agencies, and wealth management firms. Some of these opportunities could result in further geographic expansion. Merger and acquisition activities are subject to a number of risks, including lending, operating, and integration risks. Growth through acquisition requires careful due diligence, evaluation of risks, and projections of future operations and financial conditions. Actual results may differ from our expectations and could have a material adverse effect on our financial condition and results of operations. Growth through acquisition also often involves the negotiation and execution of extensive merger agreements. Such agreements may give rise to litigation, constrain us in certain ways, or expose us to other risks beyond our normal operating risks.

The Company s recruitment of new executive and commercial lending management has in several cases brought in new management who previously worked at larger institutions. These individuals have often served larger customers than the Company has historically serviced, and they have had the benefit of larger capital and administrative resources than are present in the Company s current structure. The success of this recruitment may depend on the successful integration of these individuals into the Company and may expose the Company to lending and operating losses related to large new customers in newer markets. The Company s commercial banking strategy has particularly focused on taking market share from larger national institutions and in many cases these new accounts are larger than the Company s historic accounts. Additionally, the Company s ability to service these accounts may in some cases involve arranging loan participations and syndications. These activities can expose the Company to additional lending, administrative, and liquidity risks. The Company also actively recruits in other business lines, including private banking and wealth management. This activity can give the Company additional access to large customers in its markets in order to expand our business. Such recruitment can affect the retention of new and old business, and can also be affected by competitive reactions and other relationship risks in retaining accounts.

Operations acquired in business combinations have frequently been subject to bank regulations prior to the merger date. Related regulatory examinations may result in the identification of certain operating matters requiring remediation, undisclosed deficiencies related to regulatory compliance, deficiencies that arise as a result of integration of acquired operations and operating activities conducted by those operations subsequent to the merger date, or impacts on existing business operations which are being integrated with the acquired operations. Any identified deficiencies related to regulatory compliance may result in changes that affect operating revenues and costs, including the scope or scale of business activities.

Competition From Financial Institutions and Other Financial Service Providers May Adversely Affect Our Growth and Profitability.

Competition in the banking and financial services industry is intense. We compete with commercial banks, savings institutions, mortgage brokerage firms, credit unions, finance companies, mutual funds, insurance companies, and brokerage and investment banking firms operating locally and elsewhere. Larger banking institutions have substantially greater resources and lending limits and may offer certain services that we do not. Local competitors with excess capital may accept lower returns on new business. There is increased competition by out-of-market competitors through the internet. Federal regulations and financial support programs may in some cases favor competitors or place

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us at an economic disadvantage. Our profitability depends on our continued ability to successfully compete and grow profitably in our market areas.

We are Subject to Security and Operational Risks Relating to Our Use of Technology that Could Damage Our Reputation and Our Business.

Security breaches of confidential information in our internet banking activities could expose us to possible liability and damage our reputation. Any compromise of our data security could also deter customers from using our internet banking services. We rely on industry standard internet security systems to provide the security and authentication necessary to effect secure transmission of data. These precautions may not protect our security systems from compromises or breaches and could result in damage to our reputation and our business. We utilize third party core banking software and for some systems we have outsourced our data processing to a third party. If our third party providers encounter difficulties or if we have difficulty in communicating with such third parties, it could significantly affect our ability to adequately process and account for customer transactions, which could significantly affect our business operations. We utilize file encryption in designated internal systems and networks and are subject to certain state and federal regulations regarding how we manage data security. Natural disasters and disaster recovery risks could affect our operating systems, which could affect our reputation.

Financial and Operating Counterparties Expose Us to Risks.

We have increased our use of derivative financial instruments, primarily interest rate swaps, which exposes us to financial and contractual risks with counterparty banks. We maintain correspondent bank relationships, manage certain loan participations, engage in securities transactions, and engage in other activities with financial counterparties that are customary to our industry. We also utilize services from major vendors of technology, telecommunications, and other essential operating services.   There is financial and operating risk in these relationships, which we seek to manage through internal controls and procedures, but there are no assurances that we will not experience loss or interruption of our business as a result of unforeseen events with these providers.

We May Not Be Able to Attract and Retain Skilled People.

Our success depends, in large part, on our ability to attract new employees, retain and motivate our existing employees, and continue to compensate employees competitively. Competition for the best people in our industry can be intense and we may not be able to hire or retain appropriately qualified individuals.

Our Controls and Procedures May Fail or Be Circumvented.

Management regularly reviews and updates the Company s 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. Any failure or circumvention of the controls and procedures or failure to comply with regulations related to controls and procedures could have a material adverse effect on the Company s business, results of operations and financial condition.

New Mortgage Lending Operations In Eastern Massachusetts Expose Us to New Operating Risks.

In 2012, the Bank acquired the business assets of an established residential mortgage origination company in Eastern Massachusetts. Under the agreement the Bank has employed the former employees of this company and is utilizing its business name and operating procedures to originate residential mortgages in Eastern Massachusetts as well as in other areas of Massachusetts and surrounding markets. The volume of mortgage originations has exceeded the Bank s existing mortgage originations volume, and involves lending in a new market area with new staff and new processes. The Bank has assimilated these operations into the Bank s risk management program. There has been turnover in the position of the senior manager of consumer lending, who oversees these operations and the Bank has utilized a third party financial accounting resource to assist in the accounting of these operations. The conduct of these new activities exposes the Bank to the risk of loan losses, losses related to interest rate risk management, litigation, and other risks common in mortgage banking operations.

Derivatives and Counterparty Risks Have Increased Due to the Expanded Mortgage Operations.

The total notional amount of derivative financial instruments more than doubled in 2012, largely due to the expanded mortgage operations. The increase includes customer interest rate lock commitments on applications for mortgages that Berkshire intends to sell, and forward sales of securities intended to hedge the interest rate risk of these rate lock commitments until the loans are closed and sold. These activities involve new derivative instruments and new broker/dealer counterparties, as well as the utilization of a new vendor responsible for managing the hedging position. Additionally, Berkshire sells closed loans on a servicing released basis under mandatory and best efforts contracts to institutional secondary market purchasers which are new counterparties for Berkshire. Berkshire could experience losses if there are failures in the controls or accounting for these activities or if there are performance failures by any of these new counterparties. The risk of loss is increased if interest rates change suddenly and the intended hedging objectives are not achieved as a result of market or counterparty behaviors.

The Planned Core Bank Processing System Conversion Exposes Us to Operating and Financial Risks.

In 2012, the Bank converted its core bank processing system to a new system and a new vendor. This system was changed from primarily an in-house system run on the Bank s own computers to one that is primarily a service bureau solution running on the provider s computers and relying on long distance telecommunications. Core systems conversions involve extensive planning and operational changes that affect bank account records, customer service delivery, internal procedures, technology risk management, and other significant operating activities. The changes expose the Bank to new risks with new systems and new vendors. The Bank has worked closely with third parties to manage the related operating and financial risks.

Liquidity

Our Wholesale Funding Sources May Prove Insufficient to Replace Deposits at Maturity and Support Our Operations and Future Growth.

We must maintain sufficient funds to respond to the needs of depositors and borrowers. As a part of our liquidity management, we use a number of funding sources in addition to core deposit growth and repayments and maturities of loans and investments. These sources include Federal Home Loan Bank advances, proceeds from the sale of loans, and liquidity resources at the holding company. Our financial flexibility will be severely constrained if we are unable to maintain our access to funding or if adequate financing is not available to accommodate future growth at acceptable costs. Finally, if we are required to rely more heavily on more expensive funding sources to support future growth, our revenues may not increase proportionately to cover our costs. In this case, our operating margins and profitability would be adversely affected. Turbulence in the capital and credit markets may adversely affect our liquidity and financial condition and the willingness of certain counterparties and customers to do business with us.

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Changes in Deposit Insurance May Affect Demand for Deposits.

At the end of 2012, the FDIC terminated unlimited deposit insurance for transaction accounts. Due to its growth, the Bank is also evaluating alternative structures of deposit protection which might be utilized differently from its historic offering of DIF insurance. Changes to deposit protection may affect demand for deposits.

Our Ability to Service Our Debt, Pay Dividends and Otherwise Pay Our Obligations as They Come Due Is Substantially Dependent on Capital Distributions from the Bank, and These Distributions Are Subject to Regulatory Limits and Other Restrictions.

A substantial source of our holding company income is the receipt of dividends from the Bank, from which we service our debt, pay our obligations, and pay shareholder dividends.   The availability of dividends from the Bank is limited by various statutes and regulations. It is possible, depending upon the financial condition of the Bank and other factors, that the applicable regulatory authorities could assert that payment of dividends or other types of payments are an unsafe or unsound practice. If the Bank is unable to pay dividends to us, we may not be able to service our debt, pay our obligations or pay dividends on our common stock. The inability to receive dividends from the Bank would adversely affect our business, financial condition, results of operations and prospects.

New Subordinated Debt May Affect the Company s Future Profitability and Ability to Service Its Obligations and Provide Dividends to Shareholders.

The Company issued $75 million in subordinated debt at the parent level in the most recent quarter. Proceeds from this debt were primarily used as partial consideration for the Beacon merger on October 19, 2012. The merger of Beacon into Berkshire Bank is expected to produce earnings accretion, which will provide additional cash flow to service the new subordinated debt. The Company relies primarily on payments from Berkshire Bank, which could be interrupted in the future due to economic or regulatory changes. The additional leverage at the parent could affect its access to other sources of funds and the general adequacy of its liquidity.

Interest Rates

Changes in Interest Rates Could Adversely Affect Our Results of Operations and Financial Condition.

Net interest income is our largest source of income. Changes in interest rates can affect the level of net interest income. The Company s interest rate sensitivity is discussed in more detail in Item 7A of this report. We principally manage interest rate risk by managing our volume and mix of our earning assets and funding liabilities. In a changing interest rate environment, we may not be able to manage this risk effectively. If we are unable to manage interest rate risk effectively, our business, financial condition and results of operations could be materially harmed. Changes in interest rates can also affect the demand for our products and services, and the supply conditions in the U.S. financial and capital markets. Changes in the level of interest rates may negatively affect our ability to originate real estate loans, the value of our assets and our ability to realize gains from the sale of our assets, all of which ultimately affect our earnings.

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Securities Market Values

Declines in the Value of Certain Investment Securities Could Require Write-Downs, Which Would Reduce Our Earnings.

Unrealized losses on investment securities result from changes in credit spreads and liquidity issues in the marketplace, along with changes in the credit profile of individual securities issuers. We have concluded that, as of year-end 2012, any unrealized losses are temporary in nature, and we have the intent and ability to hold these investments for a time necessary to recover our cost or stated maturity (at which time, full payment is expected). However, a continued decline in the value of these securities or other factors could result in an other-than-temporary impairment write-down which would reduce our earnings. Some of the Company s securities are locally originated economic development bonds. These securities could become impaired due to economic and real estate market conditions which also affect loan risk. We have an investment in the stock of the Federal Home Loan Bank of Boston, which recently reinstituted a modest dividend after a period when the dividend was suspended. If the capitalization of a Federal Home Loan Bank, including the FHLBB, became substantially diminished it could result in a write-down which would reduce our earnings.

Regulatory

Legislative and Regulatory Initiatives May Affect our Business Activities and Increase Operating Costs.

The potential exists for additional federal or state laws and regulations regarding lending, funding practices, capital, and liquidity standards. Bank regulatory agencies are expected to be more active in responding to concerns and trends identified in examinations, including the expected issuance of many formal enforcement orders. In addition, new laws, regulations, and other regulatory changes may also increase our compliance costs and affect our business and operations. Moreover, the FDIC sets the cost of our FDIC insurance premiums, which can affect our profitability.

We are required by federal and state regulatory authorities to maintain adequate levels of capital to support our operations. Regulatory capital requirements and their impact on the Company may change. We may need to raise additional capital in the future to support our operations and continued growth. Our ability to raise capital, if needed, will depend on conditions in the capital markets at that time, which are outside of our control, and on our financial performance. If we cannot raise additional capital when needed, it could affect our operations and our ability to execute our strategic plan, which includes further expanding our operations through internal growth and acquisitions.

The Dodd-Frank Act made extensive changes in the regulation of insured depository institution. In addition to eliminating the OTS and creating the Consumer Financial Protection Bureau, the Dodd-Frank Act, among other things, directs changes in the way that institutions are assessed for deposit insurance, mandates the imposition of consolidated capital requirements on savings and loan holding companies, requires originators of certain securitized loans to retain a percentage of the risk for the transferred loans, stipulates regulatory rate-setting for certain debit card interchange fees, repeals restrictions on the payment of interest on commercial demand deposits and contains a number of reforms related to mortgage originations. The impact of many of the provisions of the Dodd-Frank Act cannot yet be fully assessed. However, there is a significant possibility that the Dodd-Frank Act will, at a minimum, result in increased regulatory burden, compliance costs and interest expense for the Company.

New laws, regulations, and other regulatory changes, along with negative developments in the financial industry and the domestic and international credit markets, may significantly affect the markets in which we do business, the markets for

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and value of our loans and investments, and our ongoing operations, costs and profitability. For more information, see Regulation and Supervision in Item 1 of this report.

Proposed New Federal Bank Capital Rules May Affect the Company s Future Condition and Performance.

On June 12, 2012, the Office of the Comptroller of the Currency (OCC), Board of Governors of the Federal Reserve System (FRB), and the Federal Deposit Insurance Corporation (FDIC) announced that they are seeking comment on three notices of proposed rulemaking that would revise and replace the agencies current capital rules as these federal agencies move forward with implementing capital requirements consistent with agreements reached by the Basel Committee on Banking Supervision (Basel III). The proposed rules are currently preliminary and the Company will be assessing the potential impact of the proposed and final rules. Please see the further discussion of bank regulation and capital rules in Item I in this Form 10-K.

Provisions of Our Certificate of Incorporation, Bylaws and Delaware Law, as Well as State and Federal Banking Regulations, Could Delay or Prevent a Takeover of Us by a Third Party.

Provisions in our certificate of incorporation and bylaws, the corporate law of the State of Delaware, and state and federal regulations could delay, defer or prevent a third party from acquiring us, despite the possible benefit to our stockholders, or otherwise adversely affect the price of our common stock. These provisions include: limitations on voting rights of beneficial owners of more than 10% of our common stock; supermajority voting requirements for certain business combinations; the election of directors to staggered terms of three years; and advance notice requirements for nominations for election to our Board of Directors and for proposing matters that stockholders may act on at stockholder meetings. In addition, we are subject to Delaware laws, including one that prohibits us from engaging in a business combination with any interested stockholder for a period of three years from the date the person became an interested stockholder unless certain conditions are met. These provisions may discourage potential takeover attempts, discourage bids for our 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, our common stock. These provisions could also discourage proxy contests and make it more difficult for you and other stockholders to elect directors other than the candidates nominated by our Board.

Goodwill and Other Intangible Assets

Our Acquisitions Have Resulted in Significant Goodwill, Which if it Becomes Impaired Would be Required to be Written Down, Resulting in a Negative Impact on Earnings.

The initial recording and subsequent impairment testing of goodwill and other intangible assets requires subjective judgments about the estimates of the fair value of assets acquired. Factors that may significantly affect the estimates include specific industry or market sector conditions, changes in revenue growth trends, customer behavior, competitive forces, cost structures and changes in discount rates. It is possible that future impairment testing could result in an impairment of the value of goodwill or intangible assets, or both. If we determine impairment exists at a given point in time, our earnings and the book value of the related intangible asset(s) will be reduced by the amount of the impairment. Notwithstanding the foregoing, the results of impairment testing on goodwill and core deposit intangible assets have no impact on our tangible book value or regulatory capital levels. These are non-GAAP financial measures. They are not a substitute for GAAP measures and should only be considered in conjunction with the Company s GAAP financial information.

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Trading of our Common Stock

The Trading History of Our Common Stock Is Characterized By Low Trading Volume. The Value of Your Investment May be Subject To Sudden Decreases Due To the Volatility of the Price of Our Common Stock.

Our common stock trades on the New York Stock Exchange and was transferred from the NASDAQ Global Select Market in 2012. The level of interest and trading in our stock depends on many factors beyond our control. The market price of our common stock may be highly volatile and subject to wide fluctuations in response to numerous factors, including, but not limited to, the factors discussed in other risk factors and the following: actual or anticipated fluctuations in our operating results; changes in interest rates; changes in the legal or regulatory environment in which we operate; press releases, announcements or publicity relating to us or our competitors or relating to trends in our industry; changes in expectations as to our future financial performance, including financial estimates or recommendations by securities analysts and investors; future sales of our common stock; changes in economic conditions in our marketplace, general conditions in the U.S. economy, financial markets or the banking industry; and other developments affecting our competitors or us. These factors may adversely affect the trading price of our common stock, regardless of our actual operating performance, and could prevent our stockholders from selling their common stock at a desirable price.

In the past, stockholders have brought securities class action litigation against a company following periods of volatility in the market price of their securities. We could be the target of similar litigation in the future, which could result in substantial costs and divert management s attention and resources.

Recent Mergers

Recent Mergers May Create Unforeseen Risks For the Bank and the Company.

The Company reported risk factors in the stock registration and proxy/prospectus forms filed with the SEC related to the CBT and Beacon acquisitions. While the CBT, Greenpark, and Beacon business combinations have been completed, the Company continues to recognize the risks related to integration, regulation, and management of the acquired operations which were previously identified in the subject SEC filings. Similarly, the Company completed the conversion of its core processing system in the third quarter of 2012. In the near term, the Company recognizes the risks related to the utilization, integration, and internal control of its new systems related to the integration of the CBT systems in the final quarter of 2012, and related to the integration of the Beacon systems with the new core banking system, which is planned for the first quarter of 2013. Unforeseen difficulties in managing these conversions and subsequent business operations could negatively impact customer service, account retention, revenues, costs, and earnings.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

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ITEM 2. PROPERTIES

The Company s headquarters are located in owned and leased facilities located in Pittsfield, Massachusetts. The Company also owns or leases other facilities within its primary market areas: Berkshire County, Massachusetts; Pioneer Valley (Springfield area), Massachusetts; Southern Vermont; the Capital Region; Northeastern New York and now, Northern Connecticut and Central New York. The Company has 77 full-service banking offices. The Company s Asset Based Lending Group operates from a leased facility in Woburn, Massachusetts and its Central/Eastern Massachusetts Commercial Banking Team operates from a leased facility in Westborough, Massachusetts.

During 2012, the Company acquired The Connecticut Bank and Trust Company and Beacon Federal Bancorp, Inc, which significantly expanded its owned and leased facilities. Berkshire utilizes the former headquarters facilities at acquired banks and may identify and reduce excess facilities capacity over time. CBT added eight Hartford area branches in the second quarter of 2012, while Beacon added an additional four branches in New York, one branch in Eastern Massachusetts, and two branches in Tennessee to the Company s total in the fourth quarter. The Company divested several Legacy Berkshire County branches in accordance with its merger agreement, in January, 2012. In selected other locations, the Company may combine or relocate other branches over time based on market conditions. During 2012, Berkshire consolidated and relocated most of its headquarters operations in buildings currently owned and/or leased in Pittsfield.

The addition of Beacon also brought an additional Insurance Agency, Beacon Comprehensive. With this addition, Berkshire Insurance Group operates from 12 locations in both Western Massachusetts in both standalone premises as well as in rented space located in the Bank s premises and now in Syracuse, NY.

For several years, all new Berkshire branch locations have been based around its new retail branch design which eliminates traditional teller counters and provides an interactive customer service environment through pod stations which include automated cash handling technology. In many cases, this branch design also includes a multimedia community room which is offered for use by nonprofit community groups. Berkshire is also remodeling certain existing branches with this design over time. Berkshire currently has 12 offices configured based on this new branch design, including all of the de novo branch offices opened in recent years. Berkshire s presence in Albany has mostly resulted from de novo branch expansion. In 2012, the Company opened four branch offices in this market, bringing the total branch count to 17 as it progresses towards its goal of 20 or more branch offices in this area.

In 2012, Berkshire expanded significantly in Eastern Massachusetts, including the acquisition of the operations of Greenpark Mortgage Corporation, including its eight mostly rented lending offices. This brings Berkshire s total lending office count to ten in Eastern Massachusetts. The Company has acquired property to construct a branch and regional headquarters in Westborough in 2013. With the Beacon acquisition, the Company has also acquired its first Eastern Massachusetts bank branch in Chelmsford.

ITEM 3. LEGAL PROCEEDINGS

At December 31, 2012, neither the Company nor the Bank was involved in any pending legal proceedings believed by management to be material to the Company s financial condition or results of operations. Periodically, there have been various claims and lawsuits involving the Bank, such as claims to enforce liens, condemnation proceedings on properties in which the Bank holds security interests, claims involving the making and servicing of real property loans and other issues incident to the Bank s business. However, neither the Company nor the Bank is a party to any pending

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legal proceedings that it believes, in the aggregate, would have a material adverse effect on the financial condition or operations of the Company.

ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable.

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PART II

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

Market Information

The common shares of the Company trade on the New York Stock Exchange under the symbol BHLB . The following table sets forth the quarterly high and low closing sales price information and dividends declared per share of common stock in 2012 and 2011.

	High	Low	Dividends Declared
2012			
First quarter	$ 24.49	$ 21.03	$ 0.17
Second quarter	23.49	20.15	0.17
Third quarter	23.66	21.19	0.17
Fourth quarter	24.26	20.89	0.18
2011			
First quarter	$ 22.92	$ 20.68	$ 0.16
Second quarter	22.85	20.45	0.16
Third quarter	24.14	17.11	0.16
Fourth quarter	22.50	17.56	0.17

Holders

The Company had approximately 3,508 holders of record of common stock at March 14, 2013.

Dividends

The Company intends to pay regular cash dividends to common stockholders; however, there can be no assurance as to future dividends because they are dependent on the Company s future earnings, capital requirements, financial condition, and regulatory environment. Dividends from the Bank have been a source of cash used by the Company to pay its dividends, and these dividends from the Bank are dependent on the Bank s future earnings, capital requirements, and financial condition. Further information about dividend restrictions is provided in the Stockholders Equity note in the consolidated financial statements.

Recent Sales of Unregistered Securities; Use of Proceeds From Registered Securities

On September 28, 2012, the Company issued $75.0 million principal amount of fixed to floating rate unregistered subordinated notes through a private placement to institutional investors in accordance with Rule 506 of Regulation D. The notes are due in 2027 and are redeemable at par by the Company during the final five years. The notes bear interest at a fixed rate of 6.875% for the first ten years and convert to a variable rate of interest in the final five years. The proceeds were used for Beacon merger consideration and other corporate purposes. There have been no other sales of registered or unregistered securities within the last three years.

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Purchases of Equity Securities by the Issuer and Affiliated Purchases

There were no purchases of equity securities during the fourth quarter of 2012 made by or on behalf of the Company or any affiliated purchaser , as defined by Section 240.10b-18(a)(3) of the Securities and Exchange Act of 1934, of shares of the Company s common stock. On December 14, 2007, the Company authorized the purchase of up to 300 thousand shares, from time to time, subject to market conditions. The repurchase plan will continue until it is completed or terminated by the Board of Directors. The Company has no intentions to terminate this plan or to cease any potential future purchases. As of year-end 2012, there were 98 thousand shares that remain unpurchased under this plan.

The following table sets forth information regarding the activity during the fourth quarter of 2012:

Period	Total number of shares purchased (1)		Average price paid per share	Total number of shares purchased as part of publicly announced plans or programs	Maximum number of shares that may yet be purchased under the plans or programs
October 1-31, 2012	9,661	$	24.12		97,993
November 1-30, 2012					97,993
December 1-31, 2012					97,993
Total	9,661	$	24.12		97,993

(1) Shares represent common stock withheld by the Company to satisfy tax withholding requirements on the vesting of shares under the Company s benefit plans.

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Common Stock Performance Graph

The performance graph compares the Company s cumulative stockholder return on its common stock over the last five years to the cumulative return of the NYSE Composite Index, the KBW Regional Bank Index, the NASDAQ Composite Index, and the SNL Bank and Thrift Index. Total stockholder return is measured by dividing total dividends (assuming dividend reinvestment) for the measurement period plus share price change for a period by the share price at the beginning of the measurement period. The Company s cumulative stockholder return over a five-year period is based on an initial investment of $100 on December 31, 2007.

We have chosen to change the comparison indexes this year. The NYSE Composite was chosen to replace the Nasdaq composite because the Company moved its stock listing to the NYSE in 2012 and feels the diversity and breadth of the index makes it a more accurate broad market indicator. The KBW Regional Bank Index (KRX) was chosen to replace the SNL Bank and Thrift Index because the Company has grown and feels the KRX more accurately reflects its peers. The index is also more widely available to the public. All four indices are represented in the chart below.

Information used on the graph and table was obtained from a third party provider, a source believed to be reliable, but the Company is not responsible for any errors or omissions in such information.

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	Period Ending					
Index	**12/31/07**	**12/31/08**	**12/31/09**	**12/31/10**	**12/31/11**	**12/31/12**
Berkshire Hills Bancorp, Inc.	100.00	121.62	83.92	92.70	95.95	106.37
NASDAQ Composite	100.00	60.02	87.24	103.08	102.26	120.42
SNL Bank and Thrift	100.00	57.51	56.74	63.34	49.25	66.14
NYSE Composite Index	100.00	59.11	73.77	81.76	76.76	86.69
PHLX KBW Regional Banking Index	100.00	78.34	59.36	70.18	65.17	71.99

In accordance with the rules of the SEC, this section captioned Common Stock Performance Graph, shall not be incorporated by reference into any of our future filings made under the Securities Exchange Act of 1934 or the Securities Act of 1933. The Common Stock Performance Graph, including its accompanying table and footnotes, is not deemed to be soliciting material or to be filed under the Exchange Act or the Securities Act.

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ITEM 6. SELECTED FINANCIAL DATA

The following summary data is based in part on the consolidated financial statements and accompanying notes, and other schedules appearing elsewhere in this Form 10-K. Historical data is also based in part on, and should be read in conjunction with, prior filings with the SEC.

(In thousands, except per share data)	At or For the Years Ended December 31, 2012	2011	2010	2009	2008
Selected Financial Data:					
Total assets	$ 5,296,809	$ 3,992,257	$ 2,882,298	$ 2,700,991	$ 2,666,729
Securities	573,871	533,181	405,953	420,966	341,516
Loans	3,988,654	2,956,570	2,142,162	1,961,658	2,007,152
Allowance for loan losses	(33,208)	(32,444)	(31,898)	(31,816)	(22,908)
Goodwill and intangibles	274,258	223,364	173,079	176,100	178,830
Deposits	4,100,409	3,101,175	2,204,441	1,986,762	1,829,580
Borrowings and subordinated debentures	448,088	237,402	260,301	306,668	374,621
Total stockholders equity	667,265	551,808	387,323	385,148	408,425
Selected Operating Data:					
Total interest and dividend income	$ 175,939	$ 138,260	$ 112,277	$ 115,476	$ 133,211
Total interest expense	32,551	31,740	35,330	45,880	57,471
Net interest income	143,388	106,520	76,947	69,596	75,740
Service charges and fee income	51,265	33,727	29,859	28,181	30,334
All other non-interest income (loss)	2,791	2,076	(108)	(3,004)	1,261
Total net revenue	197,444	142,323	106,698	94,773	107,335
Provision for loan losses	9,590	7,563	8,526	47,730	4,580
Total non-interest expense	140,806	116,442	82,137	78,571	71,699
Income tax expense (benefit) - continuing operations	13,223	1,884	2,420	(15,597)	8,812
Net income from discontinued operations	(637)	914			
Net income (loss)	$ 33,188	$ 17,348	$ 13,615	$ (15,931)	$ 22,244
Less: Cumulative preferred stock dividend and accretion				1,030	
Less: Deemed dividend from preferred stock repayment				2,954	
Net income (loss) available to common stockholders	$ 33,188	$ 17,348	$ 13,615	$ (19,915)	$ 22,244
Dividends per common share	$ 0.69	$ 0.65	$ 0.64	$ 0.64	$ 0.63
Basic earnings per common share	1.49	0.97	0.98	(1.51)	2.08
Diluted earnings per common share	1.49	0.97	0.98	(1.51)	2.06
Weighted average common shares outstanding - basic	22,201	17,885	13,862	13,189	10,700
Weighted average common shares outstanding - diluted	22,329	17,952	13,896	13,189	10,791

(1) For the years 2011 and 2010, the above schedule has been adjusted for prior year lease adjustments discussed in Note 2 in the Consolidated Financial Statements.

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	At or For the Years Ended December 31,				
	2012	2011	2010	2009	2008
Selected Operating Ratios and Other Data:					
Performance Ratios:					
Return on average assets	0.73%	0.50%	0.50%	(0.74)%	0.87%
Return on average equity	5.66	3.64	3.55	(4.83)	6.47
Interest rate spread	3.47	3.38	3.01	2.61	3.06
Net interest margin	3.62	3.57	3.28	3.00	3.44
Non-interest income/total net revenue	27.38	25.16	27.88	26.57	29.44
Non-interest expense/average assets	3.11	3.34	2.99	2.93	2.81
Dividend payout ratio	43.62	67.01	65.16	N/M	30.58
Growth Ratios:					
Total loans	34.91	38.02	9.20	(2.27)	3.24
Total deposits	32.22	40.68	10.96	8.59	0.39
Total net revenues	38.73	33.39	12.58	(8.15)	21.19
Capital Ratios:					
Tier 1 capital to average assets - bank	7.46	8.41	8.04	7.86	9.34
Total capital to risk-weighted assets - bank	11.79	11.29	10.61	10.71	12.28
Stockholders equity/total assets	12.60	18.82	13.44	14.26	15.32
Tangible common stockholders equity to tangible assets (3)	7.82	8.71	7.91	8.29	7.75
Asset Quality Ratios:					
Net loans charged-off/average total loans	0.26	0.27	0.42	1.96	0.19
Allowance for loan losses/total loans	0.83	1.10	1.49	1.62	1.14
Net loans charged-off - Business activities/average total loans- Business activities	0.34	0.32	0.42	1.96	0.19
Allowance for loan losses - Business activities/total loans - Business activities	1.21	1.41	1.49	1.62	1.14
Share Data:					
Book value per share	$ 26.53	$ 26.09	$ 27.52	$ 27.68	$ 30.33
Market price at year end	$ 23.86	$ 22.19	$ 22.11	$ 20.68	$ 30.86

(1) All performance ratios are based on average balance sheet amounts where applicable.
(2) N/M = Not Meaningful
(3) Tangible common stockholders equity to tangible assets exclude goodwill and other intangibles. This is a non-GAAP financial measure that the Company believes provide investors with information that is useful in understanding our financial performance and condition.
(4) Generally accepted accounting principles require that loans acquired in a business combination be recorded at fair value, whereas loans from business activities are recorded at cost. The fair value of loans acquired in a business combination includes expected loan losses, and there is no loan loss allowance recorded for these loans at the time of acquisition. Accordingly, the ratio of the loan loss allowance to total loans is reduced as a result of the existence of such loans, and this measure is not directly comparable to prior periods. Similarly, net loan charge-offs are normally reduced for loans acquired in a business combination since these loans are recorded net of expected loan losses. Therefore, the ratio of net loan charge-offs to average loans is reduced as a result of the existence of such loans, and this measure is not directly comparable to prior periods. Other institutions may have loans acquired in a business combination, and therefore there may be no direct comparability of these ratios between and among other institutions.
(5) For the years 2011 and 2010, the above schedule has been adjusted for prior year lease adjustments.

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Average Balances, Interest and Average Yields/Cost

The following table presents an analysis of average rates and yields on a fully taxable equivalent basis for the years presented. Tax exempt interest revenue is shown on a tax-equivalent basis for proper comparison using a statutory federal income tax rate of 35%.

Item 6 - Table 3 - Average Balance, Interest and Average Yields / Costs

	2012			2011			2010		
(Dollars in millions)	Average Balance	Interest	Average Yield/ Rate	Average Balance	Interest	Average Yield/ Rate	Average Balance	Interest	Average Yield/ Rate
Interest-earning assets:									
Loans:									
Residential Loans	$ 1,193.9	$ 52.7	4.42%	$ 876.1	$ 42.5	4.85%	$ 633.6	$ 32.9	5.19%
Commercial Mortgages	1,271.6	69.1	5.44	1,058.0	52.9	5.00	881.9	43.3	4.91
Commercial Business Loans	507.9	20.4	4.01	344.3	16.5	4.79	204.0	10.5	5.15
Consumer Loans	427.5	17.8	4.17	336.7	13.4	3.98	299.9	11.7	3.90
Total Loans	3,400.9	160.0	4.71	2,615.1	125.3	4.79	2,019.4	98.4	4.87
Investment securities (2)	550.8	17.6	3.19	444.9	16.5	3.71	403.5	16.7	4.14
Federal funds sold and short-term investments	76.4	0.9	0.13	14.7		0.11	11.4		0.14
Total interest-earning assets	4,028.1	178.5	4.43	3,074.7	141.8	4.61	2,434.3	115.1	4.73
Intangible assets	241.7			207.5			174.5		
Other non-interest earning assets	262.4			201.8			134.2		
Total assets	$ 4,532.2			$ 3,484.0			$ 2,743.0		
Interest-bearing liabilities:									
Deposits:									
NOW accounts	$ 304.1	$ 0.9	0.30%	$ 244.2	$ 0.9	0.4%	$ 199.3	$ 0.7	0.35%
Money market accounts	1,189.1	5.8	0.48	833.3	5.6	0.67	597.3	5.6	0.94
Savings accounts	390.8	0.7	0.19	369.6	0.8	0.22	224.3	0.6	0.27
Certificates of deposit	1,056.0	15.1	1.43	902.6	16.3	1.81	749.2	19.4	2.59
Total interest-bearing deposits	2,940.0	22.5	0.77	2,349.7	23.6	1.00	1,770.1	26.3	1.49
Borrowings and notes	432.1	10.1	2.33	250.4	8.4	3.35	282.0	9.0	3.19
Total interest-bearing liabilities	3,372.1	32.6	0.97	2,600.1	32.0	1.23	2,052.1	35.3	1.72
Non-interest-bearing demand deposits	529.0			377.9			279.1		
Other non-interest-bearing liabilities	44.8			29.8			28.7		
Total liabilities	3,945.9			3,007.8			2,359.9		
Equity	586.3			476.2			383.1		
Total liabilities and equity	$ 4,532.2			$ 3,484.0			$ 2,743.0		
Net interest-earning assets	$ 656.0			$ 474.6			$ 382.2		
Net interest income		$ 145.9			$ 109.8			$ 79.8	
Supplementary data									
Total non-maturity deposits	$ 2,413.0			$ 1,825.0			$ 1,300.0		
Total deposits	3,469.0			2,727.6			2,049.2		
Fully taxable equivalent adjustment	2.6			2.7			2.8		
Interest rate spread			3.47%			3.38%			3.01%

Net interest margin	3.62	3.57	3.28
Cost of funds	0.84	1.08	1.52
Cost of deposits	0.65	0.87	1.28
Interest-earning assets/interest-bearing liabilities	119.45	118.25	118.62

Notes:

(1) The average balances of loans includes nonaccrual loans, and deferred fees and costs.
(2) The average balance of investment securities is based on amortized cost.
(3) The above schedule includes balances associated with discontinued operations.
(4) The above schedule is not adjusted for prior year lease adjustments.
(5) The average balances of borrowings and notes includes the capital lease obligation presented under other liabilities on the consolidated balance sheet.

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RATE/VOLUME ANALYSIS

The following table presents the effects of rate and volume changes on the fully taxable equivalent net interest income. Tax exempt interest revenue is shown on a tax-equivalent basis for proper comparison using a statutory, federal income tax rate of 35%. For each category of interest-earning assets and interest-bearing liabilities, information is provided with respect to changes attributable to (1) changes in rate (change in rate multiplied by prior year volume), (2) changes in volume (change in volume multiplied by prior year rate) and (3) changes in volume/rate (change in rate multiplied by change in volume) have been allocated proportionately based on the absolute value of the change due to the rate and the change due to volume.

Item 6 - Table 4 - Rate Volume Analysis

	2012 Compared with 2011 Increase (Decrease) Due to			2011 Compared with 2010 Increase (Decrease) Due to		
(In thousands)	**Rate**	**Volume**	**Net**	**Rate**	**Volume**	**Net**
Interest income:						
Residential Loans	$ (4,064)	$ 14,305	$ 10,241	$ (2,262)	$ 11,879	$ 9,617
Commercial Loans	4,850	11,332	16,182	861	8,796	9,657
Commercial Business Loans	(2,986)	6,885	3,899	(817)	6,764	5,947
Consumer Loans	695	3,761	4,456	232	1,457	1,689
Total Loans	(1,505)	36,283	34,778	(1,986)	28,896	26,910
Investment securities	(2,505)	3,581	1,076	(1,826)	1,626	(200)
Short-term investments	35	872	907	(4)	4	
Total interest income	(3,975)	40,736	36,761	(3,816)	30,526	26,710
Interest expense:						
NOW accounts	(229)	204	(25)	62	169	231
Money market accounts	(1,873)	1,994	121	(1,774)	1,842	68
Savings accounts	(136)	45	(91)	(98)	333	235
Certificates of deposit	(3,685)	2,509	(1,176)	(6,660)	3,492	(3,168)
Total deposits	(5,923)	4,752	(1,171)	(8,470)	5,836	(2,634)
Borrowings	(3,078)	4,777	1,699	400	(1,045)	(645)
Total interest expense	(9,001)	9,529	528	(8,070)	4,791	(3,279)
Change in net interest income	$ 5,026	$ 31,207	$ 36,233	$ 4,254	$ 25,735	$ 29,989

(1) The above schedule includes balances associated with discontinued operations.

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

GENERAL

This discussion is intended to assist in understanding the financial condition and results of operations of the Company. This discussion should be read in conjunction with the consolidated financial statements and accompanying notes contained in this report.

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APPLICATION OF CRITICAL ACCOUNTING POLICIES AND ACCOUNTING ESTIMATES

The Company s significant accounting policies are described in Note 1 to the consolidated financial statements in this Form 10-K. Please see those policies in conjunction with this discussion. The accounting and reporting policies followed by the Company conform, in all material respects, to accounting principles generally accepted in the United States and to general practices within the financial services industry. The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. While the Company bases estimates on historical experience, current information and other factors deemed to be relevant, actual results could differ from those estimates.

The SEC defines critical accounting policies as those that require application of management s most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain and may change in future periods. Please see those policies in conjunction with this discussion. Management believes that the following policies would be considered critical under the SEC s definition:

Allowance for Loan Losses. The allowance for loan losses represents probable credit losses that are inherent in the loan portfolio at the financial statement date and which may be estimated. Management uses historical information, as well as current economic data, to assess the adequacy of the allowance for loan losses as it is affected by changing economic conditions and various external factors, which may impact the portfolio in ways currently unforeseen. Although management believes that it uses appropriate available information to establish the allowance for loan losses, future additions to the allowance may be necessary if certain future events occur that cause actual results to differ from the assumptions used in making the evaluation. Conditions in the local economy and real estate values could require the Company to increase provisions for loan losses, which would negatively impact earnings.

Acquired Loans. Loans that the Company acquired in business combinations are initially recorded at fair value with no carryover of the related allowance for credit losses. Determining the fair value of the loans involves estimating the amount and timing of principal and interest cash flows initially expected to be collected on the loans and discounting those cash flows at an appropriate market rate of interest. Going forward, the Company continues to evaluate reasonableness of expectations for the timing and the amount of cash to be collected. Subsequent decreases in expected cash flows may result in changes in the amortization or accretion of fair market value adjustments, and in some cases may result in the loan being considered impaired. For collateral dependent loans with deteriorated credit quality, the Company estimates the fair value of the underlying collateral of the loans. These values are discounted using market derived rates of return, with consideration given to the period of time and costs associated with the foreclosure and disposition of the collateral.

Income Taxes. Significant management judgment is required in determining income tax expense and deferred tax assets and liabilities. The Company uses the asset and liability method of accounting for income taxes in which deferred tax assets and liabilities are established for the temporary differences between the financial reporting basis and the tax basis of the Company s assets and liabilities. The realization of the net deferred tax asset generally depends upon future levels of taxable income and the existence of prior years taxable income, to which carry back refund claims could be made. A valuation allowance is maintained for deferred tax assets that management estimates are more likely than not to be unrealizable based on available evidence at the time the estimate is made. In determining the valuation allowance, the Company uses historical and forecasted future operating results, based upon approved business plans, including a review of the eligible carry-forward periods, tax planning opportunities and other relevant considerations. These underlying assumptions can change from period to period. For example, tax law changes or variances in future projected operating performance could result in a change in the valuation allowance. Should actual factors and

conditions differ materially from those considered by management, the actual realization of the net deferred tax asset could differ materially from the amounts recorded in the financial statements. If the Company is not able to realize all or part of its net deferred tax asset in the future, an adjustment to the deferred tax asset valuation allowance would be charged to income tax expense in the period such determination is made.

Goodwill and Identifiable Intangible Assets. Goodwill and identifiable intangible assets are recorded as a result of business acquisitions and combinations. These assets are evaluated for impairment annually or whenever events or changes in circumstances indicate the carrying value of these assets may not be recoverable. When these assets are evaluated for impairment, if the carrying amount exceeds fair value, an impairment charge is recorded to income. The fair value is based on observable market prices, when practicable. Other valuation techniques may be used when market prices are unavailable, including estimated discounted cash flows and market multiples analyses. These types of analyses contain uncertainties because they require management to make assumptions and to apply judgment to estimate industry economic factors and the profitability of future business strategies. In the event of future changes in fair value, the Company may be exposed to an impairment charge that could be material.

Determination of Other-Than-Temporary Impairment of Securities. The Company evaluates debt and equity securities within the Company s available for sale and held to maturity portfolios for other-than-temporary impairment (OTTI), at least quarterly. If the fair value of a debt security is below the amortized cost basis of the security, OTTI is required to be recognized if any of the following are met: (1) the Company intends to sell the security; (2) it is more likely than not that the Company will be required to sell the security before recovery of its amortized cost basis; or (3) for debt securities, the present value of expected cash flows is not sufficient to recover the entire amortized cost basis. For all impaired debt securities that the Company intends to sell, or more likely than not will be required to sell, the full amount of the depreciation is recognized as OTTI through earnings. Credit-related OTTI for all other impaired debt securities is recognized through earnings. Noncredit related OTTI for such debt securities is recognized in other comprehensive income, net of applicable taxes. In evaluating its marketable equity securities portfolios for OTTI, the Company considers its intent and ability to hold an equity security to recovery of its cost basis in addition to various other factors, including the length of time and the extent to which the fair value has been less than cost and the financial condition and near term prospects of the issuer. Any OTTI on marketable equity securities is recognized immediately through earnings. Should actual factors and conditions differ materially from those expected by management, the actual realization of gains or losses on investment securities could differ materially from the amounts recorded in the financial statements.

Fair Value of Financial Instruments. The Company uses fair value measurements to record fair value adjustments to certain financial instruments and to determine fair value disclosures. Trading assets, securities available for sale, and derivative instruments are recorded at fair value on a recurring basis. Additionally, from time to time, the Company may be required to record at fair value other assets on a nonrecurring basis, or to establish a loss allowance or write-down based on the fair value of impaired assets. Further, the notes to financial statements include information about the extent to which fair value is used to measure assets and liabilities, the valuation methodologies used and its impact to earnings. For financial instruments not recorded at fair value, the notes to financial statements disclose the estimate of their fair value. Due to the judgments and uncertainties involved in the estimation process, the estimates could result in materially different results under different assumptions and conditions.

SUMMARY

Berkshire produced record net income totaling $33.2 million in 2012, which was a 91% increase over 2011 net income of $17.3 million. There was general improvement of profitability, and measures of capital, asset quality, and liquidity

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remained favorable. Berkshire continued to generate positive operating leverage in 2012; revenues grew by 39% which was almost twice the 21% growth in expenses.

Berkshire s earnings per share increased by 54% to $1.49 in 2012, and measured $1.98 before the $0.49 after-tax impact of merger, conversion, and nonrecurring items. In November 2012, Berkshire raised its quarterly cash dividend by 6% to $0.18 per share, mirroring a similar increase in the prior year. The total return on Berkshire stock was 10.9% in 2012, including price appreciation and dividend yield.

Berkshire believes that it significantly added to the value of its franchise in 2012, as highlighted below:

- Market share improved in targeted areas, based on the advantages of Berkshire s positioning among the major regional banks in its markets with the focus, flexibility, and capacity to gain share from national banks and smaller community banks
- Berkshire expanded its footprint in Eastern Massachusetts, Northern Connecticut, and Central New York all of which are large and healthy markets which offer significant long term opportunities for business development
- Revenues were diversified, with significant growth in new fee income sources and diversification of the loan portfolio both by loan type and loan geography
- A new core banking system was installed which improves distribution channels, enhances product capabilities, deepens customer relationship management, enhances scalability, improves efficiency, and provides more capabilities for data analytics to drive future profitable targeted growth

Major accomplishments included:

- Ongoing loan and deposit growth from business development in Berkshire s footprint
- The acquisition of CBT The Connecticut Bank and Trust Company (Hartford, CT) and Beacon Federal Bancorp (Syracuse, NY)
- Loan production from lending team recruitment including the new commercial team in Westborough, MA and the new mortgage banking team in Eastern Massachusetts. Recruitment also resulted in the addition of another new seasoned commercial lending team after year-end, which is based in Eastern Massachusetts
- Four de novo branches were opened in the Albany market, bringing the total branch count to 17 as Berkshire progressed towards its goal of 20 or more offices in this market
- The insurance and wealth management business lines were enhanced, with a conversion to new insurance carriers and the consolidation of wealth management in new offices.

Income growth in 2012 also included the full year benefit of two bank acquisitions in 2011: Rome Bancorp (Rome, NY) and Legacy Bancorp (Pittsfield, MA). Berkshire s initiatives over the past two years have resulted in an 84% increase in total assets to $5.3 billion, placing it among the 100 largest exchange traded banks in the U.S. Total branch offices increased by 83% to 77 offices. Annualized fourth quarter net revenue increased by 117% to $238 million. Berkshire s office footprint extends from Boston to Syracuse, and from Hartford into Vermont. Berkshire believes that its new size and reach open up new opportunities to further develop revenue and improve efficiency based on the strong leadership that it has recruited, its investment in scalable infrastructure and operating models, and its use of Six Sigma and data analytics to sharpen its product and customer management. Through its regional headquarters, it offers responsive local

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market leadership across its business lines. The Company is flexibly pursuing the best opportunities for profitable growth across its geography and diversified product and service offerings.

Berkshire has managed its capital and funding sources to support its growth and the needs of its markets as the regional economy improves. Total common shares outstanding increased by 79% to $25.1 million over the last two years primarily due to shares issued as merger consideration, which contributed $247 million in new equity. In November 2012, Berkshire transferred its stock listing to the New York Stock Exchange, maintaining the BHLB ticker symbol. Berkshire also privately placed $75 million in subordinated debt in 2012 with institutional investors to fund the cash portion of merger consideration. This placement took advantage of favorable market conditions to improve the weighted average cost of capital. Berkshire significantly expanded its relationships with national investment grade financial institutions as secondary market outlets and providers of financial derivatives to support expanded mortgage originations.

Berkshire continues to add to its senior and middle management ranks, recruiting high caliber professionals to offer products and services competitive with national banks, driving market share gains in the retail and commercial middle markets. Financial disciplines guide pricing based on targeted profit margins and return on equity. Credit disciplines govern portfolio concentrations, credit selection, and loan structures targeted to maintain favorable momentum in credit metrics. Risk disciplines target income protection in the event of anticipated future interest rate increases, along with maintaining appropriate capital and liquidity buffers. Berkshire balances current period earnings targets with ongoing investments in strengthening its scalable infrastructure to support future growth and profitability improvement.

An important investment in 2012 was the core systems conversion in September. The Company expects this system to expand its distribution channels, enhance customer service, and improve its overall efficiency. Importantly, Berkshire expects to use this system analytically to better track customer relationships, cross sales, and product utilization, and to therefore strengthen and deepen profitability management. Management plans to use this technology together with its Six Sigma process engineering disciplines to improve data analytics and further drive smart growth. This focus will also contribute to risk management, where the Company s focus is on continuing to maintain strong asset quality, modest credit charges, and careful interest rate management in the current challenging environment.

Berkshire recently introduced new messaging themes for its America s Most Exciting Bank® brand, and in 2012 named Olympic gold medal and National Hall of Fame basketball coach Geno Auriemma as company spokesperson. Berkshire annually convenes AMEBU America s Most Exciting Bank University to support brand and culture development companywide. The Company has an ongoing program to rebrand targeted branch offices across its region based on its redesigned branch footprint which enhances customer engagement, revenue potential, and cost management. Berkshire s charitable foundations continue their leadership in philanthropy and community involvement in its regions. Reflecting Berkshire s evolving governance, 2012 was the first full year for the new Capital Committee of the Board, which evaluates strategic impacts of the changing regulatory and economic factors affecting capital adequacy, capital supply, and returns on capital. At the end of the year, the Board promoted Mr. Daly to Chairman, in addition to his existing roles as President and CEO. The Board appointed Mr. Bossidy to the new role of Lead Independent Director, where he will continue to provide leadership and oversight to the Company s governance.

COMPARISON OF FINANCIAL CONDITION AT DECEMBER 31, 2012 AND 2011

Balance Sheet Summary. Berkshire has increased its balance sheet significantly over the last two years as it has taken advantage of opportunities to enlarge and strengthen its footprint in its New England and upstate New York markets. The Company believes that its geographic and size positioning give it sustainable competitive advantage for gaining customer preference and increasing market and wallet share in these markets. Balance sheet growth has been integral to

generating positive operating leverage and improved operating profitability and return on equity. This growth has also improved the flexibility and diversification of revenue sources. The Company manages according to disciplines to maintain balance sheet strength including asset quality, interest rate risk, liquidity, and capital strength. Berkshire significantly increased its common shares outstanding over the last two years through merger consideration to provide appropriate capital support for this growth. Berkshire s goal is to produce competitive long term shareholder returns and to maintain strong access to capital markets to support its deposit and loan activities in meeting the needs of the communities that it serves.

Total assets increased during 2012 by $1.3 billion (33%) to $5.3 billion. Over the last two years, total assets have increased by $2.4 billion (84%). Growth included the 2012 acquisitions of CBT, Beacon, and Greenpark Mortgage operations ($1.2 billion in total assets) and the 2011 acquisitions of Rome and Legacy ($1.2 billion in total assets). Most categories of assets and liabilities increased as a result of these acquisitions. Assets and liabilities from discontinued operations at year-end 2011 were related to four former Legacy New York branches which were divested in January 2012.

Berkshire produced a 5% increase in loans and deposits from business development in 2012, separate and distinct from the impact of the bank acquisitions. This was the product of Berkshire s ongoing expansion in its regional markets with particular emphasis on commercial relationship growth. Commercial business development produced a 25% increase in commercial business loans and total

demand deposits increased by 27% from business development. At year-end, commercial deposits funded 64% of outstanding commercial loans, reflecting the benefit of the Company s relationship approach to developing commercial business.

Overall measures of asset quality, capital, and liquidity remained strong through the year. Total shareholders equity increased by $115 million (21%) primarily due to equity issued as merger consideration. Total intangible assets increased by $51 million (23%) due primarily to merger related goodwill. Berkshire utilized additional borrowings, particularly to fund growth in residential mortgages held for sale, as well as the cash consideration used for mergers. Due to this additional leverage, the ratio of total equity to assets decreased to 12.6% from 13.8% during the year. Reflecting the higher proportion of residential mortgage related assets, the Bank s risk based capital ratio improved to 11.8% from 11.3% during the year. The ratio of loans/deposits increased slightly to 97% from 95%. At year-end, 34% of total loans were loans acquired in business combinations which were recorded at fair value in the last two years. Total outstanding common shares increased by 19% to $25.1 million in 2012 due primarily to shares issued as merger consideration. Book value per share improved to $26.53 from $26.09 primarily due to the benefit of retained earnings.

Investment Securities. Berkshire s goal is to maintain a high quality portfolio consisting primarily of liquid investment securities with managed durations to limit the potential for market value declines in rising rate markets. Berkshire focuses on loan growth as the primary use of funds from deposit growth and the primary source of interest income. The investment portfolio provides additional liquidity and interest rate risk management flexibility, in addition to the capacity to generate higher earnings. The Company evaluates the portfolio within its overall objectives of producing growth in earnings per share and return on equity.

The portfolio increased in 2012 primarily due to securities acquired in bank acquisitions. There were no major changes in the structure of the portfolio during the year and the portfolio yield decreased due to the ongoing low rate environment. The Company evaluates options for managing the portfolio s size, risk, and duration to mitigate the income impact of potential further yield compression within the stated overall portfolio objective.

Total investment securities increased by $41 million (8%) during the year due to $121 million in investment securities acquired in bank acquisitions. Berkshire restructures the investments and borrowings of acquired banks at the time of acquisition when these instruments are recorded at fair value. Depending on circumstances, some of this restructuring is done immediately prior to acquisition and some is done shortly after acquisition. This restructuring allows Berkshire to conform these instruments to its own policy objectives. Berkshire had liquidated portions of the recently acquired Beacon portfolio in the fourth quarter. Berkshire also liquidated selected existing securities positions which became uneconomical during the year as asset yields continued to decline. At year-end, the Company was in the process of evaluating alternatives for replacing some of those securities depending in part on anticipated changes in securities market yields and prices.

The increase in total securities in 2012 consisted mainly of structured U.S. agency collateralized mortgage obligations with targeted average lives in the 2 5 year range. Berkshire also continues to invest in dividend yielding equity securities of local financial institutions. Investment securities as a percentage of earning assets decreased modestly to 12% at year-end 2012, compared to 15% at the start of the year.

At year-end 2012, Berkshire s $574 million securities portfolio was primarily comprised of $322 million in mortgage-backed securities guaranteed or sponsored by the U.S. government. These securities constituted 56% of the portfolio at year-end, increasing slightly from 55% at the start of the year. Municipal securities and development bonds were little changed, totaling $135 million (23% of the portfolio) at year-end 2012. Other significant components of the portfolio at year-end included $31 million of corporate bonds and trust preferred securities, $25 million of marketable equity securities (consisting primarily of exchange traded common stock issued by community banks in the region), and $40 million of restricted securities which mostly consisted of Federal Home Loan bank stock. Approximately 81% of the total portfolio was designated as available for sale, with the primary exceptions being the restricted stock and locally issued development bonds (classified as held to maturity municipal securities except for one security classified as a trading obligation as a result of a related interest rate swap). The net unrealized gain on securities available for sale totaled $10.7 million, or 2.4% of book value at year-end 2012, compared to 1.5% a year earlier.

The Company did not record any write-downs of investment securities in 2012 and none of the Company s investment securities were classified as other-than-temporarily impaired during the year or at year-end. Gross unrealized losses on securities with unrealized losses declined to $3 million from $4 million. Detail on these securities, including one security with a $1.7 million unrealized loss, is included in the Securities note in the consolidated financial statements. There were several downgrades of corporate bonds and single issuer trust preferred securities during 2012, due primarily to changes in the ratings environment for large financial institutions. At year-end 2012, all available for sale debt securities carried at least one investment grade rating by a major rating agency except for the above security, one security called at par after year-end, and one $1.5 million security downgraded to a Ba1 rating which had a 0.3% premium valuation at year-end. The Company s held to maturity securities are generally unrated local securities, all of which are performing and none of which is deemed criticized according to the Company s internal ratings systems.

The tax equivalent yield on investment securities declined to 3.2% in 2012 from 3.7% in 2011, reflecting the impact of portfolio turnover and growth in the ongoing low interest rate environment. The effective duration of the debt securities portfolio at year-end 2012 was estimated at approximately 3.0 years, with a year-end tax equivalent yield of approximately 2.7%. These data reflect the shorter duration planned amortization class bonds which comprise the majority of the mortgage backed securities portfolio, combined with the generally medium term duration of other debt securities.

Loans. Berkshire s focus has been on expanding and diversifying its loan portfolio to serve the credit needs of its markets and develop profitable financial service relationships with customers in and around its footprint. In 2012, the loan portfolio grew as a result of business combinations in Eastern Massachusetts, Northern Connecticut, and Central

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New York. Berkshire has also focused on lending team and talent recruitment which contributed to growth from business development in its markets. Berkshire s loan growth was net of certain non-relationship balances which were not retained during the year, along with certain balances which were sold. Results reflect the Company s overall strategic focus on balancing growth, earnings, and risk objectives. Production of residential mortgages and commercial business loans also reflected improved market conditions. Ongoing low interest rates have pressured gross loan yields and margins, particularly in commercial lending. The Company continues to target a business mix that satisfies its long term return on equity and interest rate sensitivity targets, and it uses financial derivatives with national institutional partners as an integral component of this strategy. The Company believes that its risk disciplines and high quality underwriting standards are improving the long run risk profile of its credit portfolio.

Total loans increased by $1.03 billion (35%) to $3.99 billion in 2012. This included $875 million in acquired loans from the CBT and Beacon acquisitions. Excluding loans acquired in business combinations, net loan growth was $157 million (5%) in 2012, including $125 million in residential mortgages and $101 million in commercial business loans. Real estate related loans were affected by accelerated runoff in the second half of the year. This included higher prepayments resulting from record low interest rates, along with targeted reductions of non-relationship commercial accounts. Loans acquired as a result of bank mergers were generally in-market conforming loans except for approximately $83 million in loans associated with Beacon s two Tennessee branches. CBT s loan portfolio reflected its emphasis on small business banking. Beacon s loans were more consumer oriented, together with a more recently developed commercial portfolio concentrated in Central New York. For the year, residential mortgage loans decreased to 33% of total loans from 35%, and commercial mortgages decreased to 36% from 39%. Commercial business loans increased to 15% from 14% and consumer loans increased to 16% from 12%.

Berkshire conducts thorough pre-merger due diligence on loans acquired in business combinations, together with post-merger fair value analysis with the assistance of a third party. The Company recorded the acquired loans at estimated net fair value, including estimated discounts for impaired loans. The Company recorded a net discount of $38.2 million in 2012 on loans acquired in business combinations (4.2% of the acquired book balance). Acquired impaired loans totaled $102.1million (11.2% of total acquired loans). Discount on these loans totaled $43.2 million (42.4% of book value), including $31.4 million of nonaccretable discount representing estimated uncollectable amounts. This net discount included premiums and discounts for loans with various prepayment speeds and prepayment volatility, which has contributed to volatility in quarterly net interest income. Additionally, net interest income is charged or credited based on collections of nonaccretable discount as impaired loans are liquidated. The balance of accretable discount on impaired loans acquired from business combinations totaled $8.2 million at year-end 2012, compared to $1.3 million at year-end 2011. The increase included $11.8 million added for new loans acquired in 2012 less $4.8 million in accretion recorded to income in 2012.

Berkshire continues to take commercial market share from national competitors as a result of the capabilities and responsiveness of the commercial banking teams that it has recruited in recent years. Total commercial loans increased by $447 million (29%) to $2.01 billion in 2012, including $390 million acquired in the bank mergers. In addition to these acquired loans, this increase was primarily due to growth in commercial business loans, which increased by $101 million to $600 million and grew at a 25% rate excluding the $88 million benefit of loans acquired in bank mergers. Growth from business development included the contribution from Berkshire s new Central Massachusetts commercial banking team, which was recruited in December 2011 and is located in Westborough. Berkshire s asset based lending team operates from Eastern Massachusetts and serves Berkshire s entire footprint. Asset based loans outstanding

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increased in 2012 by $105 million to $258 million. Shortly after year-end, a new Eastern Massachusetts commercial team was recruited to further expand middle market commercial banking in Central/Eastern Massachusetts.   Loan growth has included ongoing contributions from Berkshire s New York region, including loan participations originated with Beacon prior to its acquisition. Shortly after year-end, new commercial leadership was recruited for the Syracuse area to build on the foundation provided with the Beacon merger. Similarly, new commercial leadership was recruited for the Hartford/Springfield market in the second half of 2012 to build on the foundation provided with the CBT merger. Berkshire has also enhanced its small business lending program, with expanded services provided through its branch network.

The $304 million (30%) increase in the residential mortgage portfolio to $1.32 billion included $179 million in balances acquired in the bank mergers. The $125 million increase excluding these bank mergers primarily represented business development from the eight new Eastern Massachusetts mortgage lending offices added as a result of the recruitment of the Greenpark mortgage team. Berkshire s loan production consisted primarily of conforming fixed rate mortgages to borrowers in and around its markets. The majority of mortgage production is sold to national institutional secondary market partners and government agencies. Growth in Berkshire s mortgage portfolio included mortgages which were purchased from Greenpark Mortgage prior to its acquisition, together with increased originations by the expanded mortgage banking operation in the strong refinancing market that developed in the second half of the year due to record low interest rates. Growth of the mortgage portfolio was net of $20 million of seasoned mortgages sold during the year as part of the Company s overall asset/liability management. Additional information about mortgage production is included in the later discussion of non-interest income in the results of operations section. The balance of residential mortgages includes net deferred costs and premiums which increased to $11 million from $5 million in 2012 due primarily to premiums paid on purchased Greenpark mortgages. These amounts are amortized into mortgage income and have also contributed to increased quarterly volatility in net interest income due to higher volatility in prepayment speeds.

Total consumer loans increased by $281 million (76%) to $651 million in 2012 including $307 million in balances acquired in bank mergers. This included $266 million in balances of acquired other consumer loans consisting primarily of indirect auto loans in the Beacon portfolio. Berkshire s total auto loan portfolio increased to $165 million at year-end 2012, compared to $21 million at the prior year-end. Beacon had an established auto lending function that Berkshire expects to maintain and may expand in targeted areas. Berkshire s consumer loan outstandings from business development decreased in 2012 due to the impact of loan refinancings and the Company s concentration on residential mortgage production. Home equity loans increased by $27 million to $325 million in 2012, including $41 million in balances acquired in bank mergers.

The yield on loans was little changed at 4.73% in the fourth quarter of 2012, compared to 4.74% in the fourth quarter of the prior year. The benefit of purchase accounting accretion for loans acquired in bank mergers generally offset the yield compression experienced in the industry due to continuing low interest rates. The purchase accounting accretion relates to the higher rates assigned to higher risk and impaired acquired loans when they are fair valued at acquisition. The overall yield on acquired loans was established at 6.0% for CBT and 5.8% for Beacon based on the initial yields assigned as of the merger dates. The net accretion in 2012 included the new accretion from acquired loans and a decline in the rate of accretion as loans acquired in 2011 are reduced. There is further information about the impact of accretion in the later discussion of net interest income in the results of operations section.

Berkshire continues to favor an asset sensitive interest rate risk profile, and seeks to manage the retention of long term fixed rate loans and securities. The majority of fixed rate residential mortgage production is sold servicing released in the secondary market.   The Bank offers back-to-back interest rate swaps to certain commercial loan customers, which allows the Bank to book a variable rate loan while providing the customer with a contract to fix its interest rate. This

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allows the Company to be more competitive with national financing sources without booking long-term, fixed rate assets at current low interest rates, as well as providing a source of fee income. The Bank s loans and securities with contractual repricings over three years increased to 44% of assets from 39% at the start of the year, due primarily to growth in the residential mortgage portfolio. The impact on portfolio durations is believed to be lower due to the higher rate of prepayments in the current environment. Berkshire utilizes forward starting interest rate swaps to help maintain an overall asset sensitive interest rate risk profile as measured by the sensitivity of net interest income.

Asset Quality. Berkshire has a Chief Risk Officer and a Risk Committee of the Board which keep a close focus on maintaining strong asset quality, with most focus on the loan portfolio due to the low risk characteristics of the investment portfolio. This includes setting loan portfolio objectives, maintaining sound underwriting, close portfolio oversight, and careful management of problem assets and potential problem assets. Additionally, merger due diligence is an integral component of maintaining asset quality. Under accounting standards for business combinations, acquired loans are recorded at fair value and are deemed performing regardless of their payment status. Therefore, some overall portfolio measures of asset quality are not comparable between years or among institutions as a result of recent business combinations. The recorded values of impaired loans acquired in business combinations were generally within estimates made by Berkshire during due diligence prior to negotiating the final terms of the merger agreements, and the quality and performance of acquired criticized assets has been within the range of Berkshire s expectations. A general goal is to achieve significant resolutions of impaired loans acquired in bank mergers in the first year following the acquisition date.

Year-end non-performing assets were little changed at $27 million in 2012 compared to $26 million in 2011. They declined to 0.52% of total assets at year-end 2012 due primarily to the asset growth from acquisitions. Loans which became non-performing during the year totaled $21 million in 2012, compared to $29 million in the prior year. The impact of new non-performing assets was mostly offset by resolutions including upgrades, collections, and charge-offs. Increased non-performing commercial business loans were mostly offset by lower non-performing commercial real estate loans. The ten largest non-performing loans totaled $12.8 million and were generally well secured, with $3.3 million in impairment reserves as of year-end. The largest non-performing asset at year-end was approximately $2.4 million. For loans from business activities, the ratio of non-performing loans to total loans was 0.88% at year-end, compared to 1.03% at the start of the year.

Loans classified as performing troubled debt restructurings increased to $4.6 million from $1.3 million during 2012 due to a limited number of commercial credits. There were no loans which were restructured in 2012 that subsequently defaulted during the year. Foreclosed real estate remained negligible at year-end 2012, totaling $1.9 million. Accruing loans over 90 days past due measured 0.48% of total loans at year-end 2012, compared to 0.34% at the start of the year. These loans totaled $19.0 million at year-end 2012, including $15.5 million in loans acquired in business combinations which are recorded as accruing under accounting standards for business combinations. Loans delinquent 30-89 days increased to 0.63% of total loans from 0.55% due to delinquent loans acquired in 2012 bank mergers.

Net loan charge-offs were 0.26% of average loans in 2012. Total net charge-offs were $8.8 million in 2012, compared to $7.0 million in 2011. Loans acquired in business combinations are recorded at fair value, including the impact of estimated credit losses. Therefore, net charge-offs from acquired loans contributed only $0.2 million to total net charge-offs in 2012. Based on an average of period-end balances, net charge-offs in 2012 measured approximately 0.35% of average loans excluding loans acquired in business combinations.

The credit risk profile of the Company s loan portfolio is described in the Loans note in the consolidated financial statements. The Company s risk management process focuses primary attention on loans with higher than normal risk, which includes loans rated special mention and classified (substandard and lower). These loans are referred to as

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criticized loans, and criticized assets are the total of criticized loans and foreclosed real estate. Criticized assets increased as a result of the business combinations in 2012. Criticized assets totaled $187 million (3.5% of total assets) at year-end 2012, compared to $161 million (4.0% of total assets) at the start of the year. The Company views its potential problem loans as those loans from business activities which are rated as classified and continue to accrue interest. These loans have a possibility of loss if weaknesses are not corrected. Classified loans acquired in business combinations are recorded at fair value and are classified as performing at the time of acquisition and therefore are not generally viewed as potential problem loans. Potential problem loans totaled $62 million at year-end 2012 compared to $80 million at the prior year-end. The ten largest potential problem loans totaled $48 million at year-end 2012, with the largest such loan totaling $10 million. All of these ten loans were viewed by the Company as stable or improving. The Company s evaluation of its credit risk profile also compares the amount of classified assets to the total of the Bank s Tier 1 Capital plus the loan loss allowance. This ratio was 35% at year-end 2012, and was unchanged from the prior year-end.

Loan Loss Allowance. The determination of the allowance for loan losses is a critical accounting estimate. The Company s methodologies for determining the loan loss allowance are discussed in Item 1 of this report and Item 8 includes further information about the accounting policy for the loan loss allowance and the Company s accounting for the allowance in the consolidated financial statements.

The Company considers the allowance for loan losses appropriate to cover probable losses which can be reasonably estimated and which are inherent in the loan portfolio as of the balance sheet date. Under accounting standards for business combinations, acquired loans are recorded at fair value with no loan loss allowance on the date of acquisition. The fair value of acquired loans includes the impact of estimated loan losses for the life of the portfolio, including factors which are not probable or inherent as of the acquisition date, and including subjective assessments of risk. A loan loss allowance is recorded by the Company for the emergence of new probable and estimable losses relating to acquired loans which were not impaired as of the acquisition date. Because of the accounting for acquired loans, some measures of the loan loss allowance are not comparable to periods prior to the acquisition date or to other financial institutions.

The total amount of the loan loss allowance was $33.2 million at year-end 2012, compared to $32.4 million at the start of the year. The increase was due to growth in general reserves on acquired loans to $1.3 million from $0.5 million. This reflected a general increase in environmental risk for loans acquired in 2011 based on inherent losses which have become probable and estimable in addition to those which were projected at acquisition. For loans from business activities, the related year-end allowance was unchanged from year-to-year, with a $0.5 million increase in impaired loan reserves offset by an identical decrease in general pool reserves. Loans from business activities increased in 2012, and as a result the related year-end allowance decreased to 1.21% of these loans from 1.41% at the beginning of the year. The reduction in coverage of these balances is consistent with the increased proportion of lower risk residential mortgages, the gradual shift of commercial balances from real estate loans to lower risk loans secured by business operating assets, and the decline in potential problem loans. The decrease in this ratio is consistent with the Company s ongoing plan to strengthen the portfolio s risk metrics and gradually reduce the percentage of the portfolio with inherent losses that are probable and estimable. The year-end allowance provided 3.8X coverage of 2012 net charge-offs and 1.3X coverage of year-end non-accrual loans. The specific reserve for loans from business activities individually evaluated for impairment measured 8% of the related loan balances, demonstrating the general strength of collateral support for impaired commercial loans.

Other Assets.

Most categories of assets increased due to the Company s expanded operations including business combinations. Loans held for sale increased as a result of Berkshire s expanded mortgage production. This increase was due to the expansion of the mortgage banking operations and the record mortgage production due to heightened refinancing

demand resulting from record low interest rates. Designated mortgage originations are held for sale to longstanding secondary market relationships and are hedged in order to minimize interest rate risk from the time that interest rates are initially locked during the application process. For loans held for sale, Berkshire enters into mandatory delivery or best efforts sale contracts with institutional secondary market purchasers.

Goodwill increased due to the business combinations. Goodwill is the difference between the fair value of consideration paid for these acquisitions and the fair value of net assets and liabilities acquired. The balance of goodwill includes goodwill related to prior acquisitions. Goodwill is analyzed annually for impairment in accordance with accounting standards, and there was no impairment charge recognized based on the most recent analysis in 2012. In the current market environment, there was no significant intangible asset recorded for the fair value of core deposits acquired. Total intangible assets were $274 million at year-end 2012, compared to $223 million at year-end 2011.

The total net deferred tax asset increased to $58 million from $41 million during 2012 primarily due to deferred taxes related to the loan purchase accounting discounts recorded for bank acquisitions. The purchase accounting portion of the asset increased to $28 million from $12 million during the year. Deferred tax assets, net of valuation allowances, are expected to be realized in the future through the reversal of existing taxable temporary differences and future taxable income. At year end 2012, the balance included a net $6.1 million asset related to approximately $20 million in net operating loss carry forwards from acquired institutions.

Deposits. In its overall New England/New York footprint, Berkshire increased its deposit market share from business activities based on most recent FDIC data. Berkshire continues to promote lower cost relationship oriented accounts in all of its markets, along with commercial deposits associated with its increased originations of commercial business loans and small business loans. Berkshire has also benefited from ongoing de novo branch expansion in its Albany, New York region and has increased its commercial deposit acquisition in Eastern Massachusetts. Berkshire seeks to flexibly balance its objectives for market share and wallet share growth with its goals for controlling funds costs and its need for funds based on the totality of its asset/liability management goals.

Total deposits increased by $1.00 billion (32%) in 2012 to $4.10 billion. This included $834 million in acquired deposits from the CBT and Beacon acquisitions. Excluding acquired deposits, net deposit growth was $165 million (5%) in 2012. This was concentrated in a $120 million increase in demand deposit balances which are targeted by Berkshire s strategies to promote low cost relationship oriented accounts. Demand deposits increased to 16% of total deposits from 14% as a result of this strong growth. Time deposits decreased to 29% of total deposits from 31% during the year and time account runoff was offset by growth in money market accounts which also reflected customer liquidity preferences in the ongoing low rate environment. Berkshire produced growth exceeding 5% from business activities for all major categories of deposits in 2012 except for this decrease in time deposits. The year 2012 was the fourth consecutive year in which the deposit growth rate from business activities exceeded the loan growth rate from business activities, which has contributed to improved liquidity from operations. The ratio of loans/deposits was 97% at year-end 2012. Berkshire increased its total branch offices to 77 from 60 during the year 2012 and continued with its ongoing program of gradually introducing its AMEB branch design in new locations. During 2012, Berkshire also introduced its My Banker personalized concierge banking service targeted towards meeting the financial services needs of professionals and others with similar qualifying banking needs.

Deposit growth included the benefit of four Albany area de novo branch offices that were opened in that market during the year. Much of the rest of the growth from business development was in commercial accounts in Central/Eastern Massachusetts as a result of Berkshire s expanded operations in that market. Year-end commercial

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demand deposits increased to $413 million in 2012 from $262 million at the start of the year, including the benefit of commercial business development and bank mergers. Berkshire offers deposit insurance on 100% of its deposit balances due to a combination of insurance from the FDIC and the Massachusetts Depositors Insurance Fund. As the Company continues to pursue deposit growth across its expanding franchise, it expects to evaluate deposit protection alternatives.

By emphasizing lower cost non-maturity deposits and lowering time deposit costs, the Company has reduced the cost of its deposits in order to offset the impact of lower asset yields in the current low interest rate environment. The average annualized cost of deposits decreased to 0.59% in the fourth quarter of 2012, compared to 0.73% in the fourth quarter of 2011. The cost of deposits also benefited from acquired accounts, which had an average cost of 0.50% for Beacon at the time of acquisition. A total of $655 million in time deposits is scheduled to mature in 2013, and the weighted average cost of time deposits is expected to continue to decline based on continuing low interest rates. In its pricing process, Berkshire seeks to maintain a flexible balance between supporting business volume growth in its regional markets while also supporting its net interest margin in light of ongoing yield compression for earning assets. The Company believes it has further capacity to adjust funding costs in future quarters if appropriate based on market and interest rate conditions.

Borrowings. Berkshire utilizes borrowings to manage short term liquidity, to provide overnight funding for targeted asset classes, as medium term funding for portions of the loan portfolio, and for qualifying regulatory capital to support overall balance sheet soundness. Most outstanding borrowings are from the Federal Home Loan Bank of Boston, but the Bank and the holding company also utilize other established short term funding sources.   In 2012, Berkshire expanded its funding and capital sources with the institutional placement of subordinated debt described below.

Total borrowings increased by $211 million in 2012, including the $117 million fair value of borrowings acquired in bank mergers. As previously discussed, Berkshire routinely restructures the investments and borrowings of acquired banks to conform with its policies. In some cases this restructuring is accomplished shortly before the merger is consummated and in other cases it is completed promptly after the effective time of the merger.   In addition to acquired borrowings, Berkshire increased its use of overnight borrowings to fund growth in mortgage loans held for sale subsequent to the recruitment of its Eastern Massachusetts mortgage banking team. These loans held for sale are generally liquidated within several weeks and it is common to fund these assets with overnight borrowings, thereby generating a positive spread based on the long term fixed rate coupons of the mortgages held for sale.

On September 28, 2012, the Company received an investment by institutional investors of $75 million in fifteen year senior subordinated notes issued by the Company. The coupon on these notes is 6 7/8% fixed for the first ten years. Cash proceeds were primarily used to fund the cash consideration required for the acquisition of Beacon Federal Bancorp on October 19. The notes qualify for Tier 2 regulatory capital treatment for bank holding companies. As a savings and loan holding company, Berkshire Hills Bancorp is not presently subject to bank holding company regulatory capital requirements, but it is expected to become subject to these requirements in the future based on anticipated regulatory changes. One of the Company   s objectives with this capital placement was to reduce the long term cost of regulatory capital by obtaining fixed rate regulatory capital with tax deductible interest at this time of record low interest rates.

The cost of borrowings decreased steadily in 2012 from 3.35% in the fourth quarter of 2011 to 1.70% in the third quarter of 2012 due to the low interest rate environment and the increased use of overnight borrowings. The cost of borrowings increased to 2.80% in the fourth quarter of 2012 due to the impact of the higher coupon on the subordinated debt discussed above. The cost of borrowings includes the cost of interest rate swaps discussed in the following

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section. Berkshire often uses variable rate borrowings from the Federal Home Loan Bank which are matched with interest rate swaps with investment grade national banks in order to achieve the lowest cost and most flexible medium term funding. Additionally, Berkshire increased its use of forward starting swaps in 2012 in order to provide future interest rate protection of variable rate borrowings without increasing current period funding costs.

Derivative Financial Instruments and Hedging Activities. At year-end 2012, the Company held derivative financial instruments with a notional amount totaling $1.312 billion, compared to $578 million at the start of the year. The increase primarily resulted from an increase in derivatives related to mortgage banking, which totaled $618 million in notional amount at year-end 2012, compared to $43 million at the start of the year. Most derivative instruments relate to routine lending activity with customers offset with interest contracts with national institutional counterparties in order to provide customers with the benefit of low rate long term borrowings.

The Company records a non-hedging derivative for interest rate lock commitments related to residential mortgage originations intended for sale. Most mortgage customers elect to lock a fixed interest rate at or around the time of making a mortgage application. The notional amount of these rate lock commitments totaled $283 million at year-end 2012.

The Company enters into forward commitments which are recorded as economic hedges in order to hedge the interest rate risk for rate locked mortgage applications in process and closed mortgage loans held for sale. These commitments are primarily forward sales of to-be-announced mortgage backed securities. Generally, when mortgage loans are closed, the forward commitment is liquidated and replaced with a mandatory delivery forward sale of the mortgage to a secondary market investor. In some cases, a best-efforts forward sale agreement is utilized as the forward commitment. At year-end 2012, forward commitments totaled $336 million and were hedging the $283 million in interest rate lock commitments and the $85 million balance of mortgages held for sale. This resulted in a 91% coverage ratio of pipeline interest rate risk and allowed for potential application fallout. The Company endeavors to lock-in its gain on sale at the time of the rate lock agreement and to manage pipeline interest rate risk within established guidelines.

As previously discussed, the Company uses interest rate swaps in conjunction with commercial loan originations. The Company enters into a swap contract with the commercial customer and into an offsetting reverse swap contract with a national investment grade financial institution. Each of these contracts is recorded as an economic hedge, and the Company had a $205 million notional amount of customer swaps and an identical amount of reverse swaps at year-end 2012, which was increased from $160 million at the start of the year.

The Company also uses interest rate swaps recorded as cash flow hedges to fix the interest rate on certain of its variable rate borrowings. These swaps totaled $270 million at year-end 2012, compared to $200 million at the start of the year. The year-end balance included $140 million in forward starting swaps.

The net fair value of derivative financial instruments was estimated at a net loss of $10 million at year-end 2012, compared to a net loss of $13 million at the start of the year. The gross gain on derivative assets recorded in other assets totaled $20 million at year-end 2012, compared to $14 million at the start of the year. The gross loss on derivative instruments recorded in other liabilities totaled $30 million at year-end 2012, compared to $27 million at the start of the year. This loss is generally secured with investment securities pledged as collateral to counterparties.

Stockholders Equity. Berkshire pursues a balance of capital to maintain financial soundness while using common equity efficiently to produce a strong return on equity and book value growth as a basis for shareholder value creation.

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A sound capital structure reduces risk and enhances shareholder return and access to capital markets to support the Company s banking activities and the markets that it serves. In its payment of dividends, management of treasury shares, issuance of equity compensation, and balancing of capital sources, the Company strives to achieve a capital structure that is attractive to the investment community and which satisfies the policy and supervision purposes of the Company s regulators. When Berkshire negotiates business combinations, it generally expects to use its common shares as a significant component of merger consideration and to balance the mix of cash and stock to arrive at a targeted capital ratio based on the characteristics of the combined banks.

In 2012, total equity increased by $115 million (21%) to $667 million, including $84 million in common stock issued for bank merger consideration. Berkshire issued 3.665 million shares for this consideration, at an average value of $22.99 based on the Berkshire stock closing price at the time of the acquisitions. Berkshire converted Beacon s outstanding stock options to equivalent Berkshire stock options and recorded a $6 million credit to be paid in capital for the value of these options. Other sources of equity in 2012 included $3 million received from stock option exercises and $2 million in stock issued for equity compensation. For the year 2012, net income of $33 million funded cash stock dividends to shareholders of $16 million and contributed to a $14 million increase in retained earnings. In the fourth quarter of the year, Berkshire increased its quarterly cash dividend by 6% to $0.18 per share. This was the second consecutive year with a 6% increase in the quarterly dividend.

The ratio of tangible equity/tangible assets decreased to 7.8% from 8.7% during 2012 due to the additional leverage related to the year s business combinations. Tangible equity is a non-GAAP financial measure commonly used by investors and it excludes goodwill and other intangible assets, which increased by $51 million to $274 million due to the business combinations during the year. The ratio of equity to assets decreased to 12.6% from 13.8%, also due to the merger related leverage. Tangible book value per share increased to $15.63 from $15.53 due to the benefit of internal capital generation which offset the dilutive impact of business combinations which were all targeted to produce accretion to future earnings per share. Total book value per share increased to $26.53 from $26.09, also due to the retained earnings benefit, which offset the lower share value recorded on new shares issued as merger consideration.

At year-end 2012, Berkshire Bank s regulatory capital ratios exceeded the requirements to be considered well capitalized , with the total risk-based capital ratio increasing to 11.8% from 11.3% at the start of the year. Berkshire Bank s federal regulator is the FDIC. The increase reflected the higher proportion of lower risk residential mortgage related assets.

The Company is a savings and loan holding company and is not subject to specific regulatory capital requirements. In the third quarter of 2011, the regulation of Berkshire Hills Bancorp (the holding company) became the responsibility of the Federal Reserve Bank of Boston. The holding company s prior federal regulator, was the Office of Thrift Supervision, which was eliminated by federal legislation. Under a transition rule, the Federal Reserve Bank is expected to specify specific regulatory capital requirements for savings and loan holding companies which will become effective in 2015. The Company does not expect that there will be any material impact on its business as a result of this holding company regulatory change.

COMPARISON OF OPERATING RESULTS FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011

Berkshire s results in 2012 and 2011 include operations acquired in both years. As a result, most categories of revenue and expense increased due to these acquisitions in addition to ongoing operations. Earnings growth in 2012 included the partial year benefit of operations acquired in 2012 in addition to the full year benefit of operations acquired in 2011. Earnings per share were affected by shares issued as merger consideration. Eight bank branches acquired in the Legacy acquisition in the third quarter of 2011 were designated as discontinued operations and were divested in the

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following two quarters. All references to revenue and expense in this discussion exclude these discontinued operations. Operating results were also affected by merger and conversion expenses, and gains recorded on investments in acquired banks.

Net income increased by $15.8 million (91%) to a record $33.2 million in 2012, compared to $17.3 million in 2011. Earnings per share increased by $0.52 (54%) to $1.49 from $0.97. Net merger and nonrecurring items, including securities gains and results of discontinued operations, totaled $11.1 million and $10.4 million after-tax in 2012 and 2011 respectively. These amounts equated to $0.49 per share and $0.57 per share in 2012 and 2011 respectively. Excluding these items, adjusted earnings were $1.98 per share in 2012 and $1.54 in 2011.

The fourth quarter of 2012 was the first quarter in which results included all acquired operations. Net income totaled $9.3 million ($0.38 per share) in that quarter. Net merger and nonrecurring items as described above were $3.9 million ($0.16 per share). Before these net items, results of operations totaled $13.2 million ($0.54 per share).

The fourth quarter return on equity was 5.8%, and measured 8.2% before the net merger and nonrecurring items. The return on equity was 3.6% in 2010 before the Company undertook most of its recent growth initiatives. The Company views its return on equity before net merger and nonrecurring items as indicative of its underlying profitability from operations. The run rate of quarterly operating profitability has more than doubled over the past two years as a result of Berkshire s growth initiatives including business development, team recruitment, and accretive acquisitions. Over that time, the Company has increased the tangible book value of its shares while also paying a steady and increasing stock dividend.

Berkshire has benefited from positive operating leverage, with revenue growth outpacing growth in operating expenses. Based on its financial and pricing disciplines, it has invested in earning assets and acquisitions according to its targets for double digit returns on its invested capital. Growth has resulted in a larger franchise, with improved market share and wallet share. These initiatives have also further diversified revenue sources and earnings streams, both geographically and among our business lines. Berkshire continues to focus on opportunistic investment and multiple earnings levers to support earnings growth and profitability improvement. It also continues to invest in its franchise, including targeted strengthening of staff, opening new offices, and rebranding selected existing offices.

Berkshire views its net merger related costs as part of the economic investment for its acquisitions. Conversion expenses were primarily related to the core systems conversion which is a long term investment in the Company s operating infrastructure. These investments are intended to be accretive to return on equity and to contribute to long term earnings growth and franchise value. References to earnings before merger, conversion, and nonrecurring items (including results of discontinued operations) are not GAAP measures and are not intended to substitute for GAAP income and expense measures. Such items recorded in both years were within the range of the Company s expectations.

Total Net Revenue. Berkshire evaluates its top line with the measure of net revenue, which is the sum of net interest income and non-interest income. The Company also evaluates net revenue before security gains/losses and nonrecurring items in order to evaluate the success of its operations. A critical focus of Berkshire s strategy is to produce positive operating leverage by growing operating revenue at a higher pace than operating expenses. Berkshire also measures revenue per share to assess the accretion to shareholder value potential based on the Company s growth initiatives.

Total net revenue increased by $55 million (39%) to a record level of $197 million in 2012. Net revenue ended the year at a fourth quarter annualized run rate of approximately $238 million, which was a 49% increase over the $160 million annualized run rate in the fourth quarter of 2011 due to the benefit of mergers and organic growth. Net

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revenue per share increased by 12% to $8.84 in 2012 compared to $7.93 in 2011, primarily reflecting the accretive revenue benefit of business combinations. Due to higher mortgage banking revenues, fee income was 26% of net revenue in 2012 compared to 24% in 2011. Berkshire targets fee income at 30% or more of revenues over the long run. This ratio declined from 28% in 2010 primarily because acquired banks had a higher reliance on net interest income as a revenue source.

Net Interest Income. Berkshire targets growth in net interest income based on increased business volumes related to market share gains in its markets. The Company also regularly evaluates the use of leveraged securities investments within risk management parameters to improve income and returns on capital. During 2012 and 2011, the Company s focus was also significantly devoted to integrating assets and liabilities acquired in business combinations to maintain profitable relationships and optimize the benefit of acquired accounts in accordance with the financial targets established for these bank acquisitions. Net interest income increased by $37 million (35%) to $143 million in 2012, compared to 2011, including the benefit of the bank acquisitions net of discontinued operations. This included a full year s benefit from 2011 acquisitions together with a partial year benefit from 2012 acquisitions.

The net interest margin increased to 3.62% in 2012 from 3.57% in 2011. The margin benefited from the addition of acquired bank balances. Based on fair value analyses performed as of the acquisition date, the net interest margin of acquired Beacon accounts was estimated at approximately 4.9%. This primarily reflected the higher yield assigned to acquired higher risk and impaired loans, including recording all impaired loans as accruing in accordance with accounting principles. Additionally, the yields assigned to acquired time deposits and borrowings reflected current low interest rates and remaining maturities. Berkshire believes that its net interest margin from business activities was declining during 2012. This reflects the impact of asset repricings in the ongoing low interest rate environment, while deposit liability cost reductions were limited by competitive market conditions and the near zero level of many short term market interest rates.

The significant loan growth in the last two years has resulted in a balance of accretable yield on acquired loans totaling $18.1 million, including $8.2 million related to acquired impaired loans. Growth in residential mortgages has contributed to an increase in deferred loan costs and premiums totaling $10.6 million. The accretable yield is accreted into income while deferred costs are amortized against income. The net amount of purchase accounting loan accretion credited to net interest income was $6.3 million in 2012, compared to $3.2 million in 2011. The net amount of loan premium and cost amortization charged against net interest income was $2.3 million in 2012, compared to $1.1 million in the prior year. The growth in accretable yield and deferred costs have led to greater volatility in the quarterly net interest margin due to the uneven impacts of loan prepayments from quarter to quarter. Additionally, recoveries/charge-offs related to nonaccretable discount are recorded when acquired impaired loans are liquidated, and this activity is also variable and unpredictable.

Changes in asset yields and funds cost in 2012 included both the full year impact of acquisitions in 2011 as well as the partial year impact of acquisitions in 2012. Changes in fourth quarter yields and costs are indicative of changes in the run rate of these data from the end of 2011 to the end of 2012. The Company operated in an ongoing low interest rate environment, with further lows in long term rates in the second half of 2012.

The yield on earning assets decreased by 18 basis points to 4.43% in 2012, with the negative impact of asset repricings partially offset by the higher yield on acquired loans. This yield was 4.49% in the fourth quarter of the year, which was unchanged from the fourth quarter of the prior year due to the benefit of Beacon assets acquired in the fourth quarter of 2012. The cost of funds decreased by 24 basis points in 2012 to 0.84%, reflecting lower deposit and borrowings costs. The cost of deposits decreased from 0.87% in 2011 to 0.65% in 2012, and declined to 0.59% in the fourth quarter of the year. This reflected the reductions in rates paid on all major categories of deposits, reducing the cost of interest bearing deposits by 0.23%. Lower deposit costs also reflected the strong growth rate in non-interest bearing demand deposits during the year. The Company believes that it has additional potential opportunities to lower deposit costs while continuing to increase its balances. The cost of borrowings trended down through the third quarter of 2012 and then increased to 2.80% in the last quarter of the year. This was due to the $75 million in subordinated debt financing issued for the Beacon acquisition at the end of the third quarter with a 6.875% coupon.

The Company adheres to disciplines in pricing its assets and liabilities in order to maintain an appropriate net interest margin and return on equity, while also achieving its asset/liability objectives. The Company strives to maintain a modestly asset sensitive interest rate risk profile so that long term earnings will benefit when interest rates increase from the very low levels that have existed in the most recent years. The current low level of interest rates is generally leading to tighter interest margins in the banking industry. The Company therefore plans to continue to adjust its pricing and to pursue volume growth in conjunction with its long term net interest margin objectives.

Non-Interest Income. Most of Berkshire s non-interest income is fee income, which generally represents operating business conducted with customers in Berkshire s markets. The Company pursues growth in market share and wallet share across its business lines, including banking, insurance, and wealth management. In commercial banking, Berkshire pursues commercial business loans with relationships that provide non-interest bearing demand deposit balances and that utilize fee services including electronic banking and cash management services. Berkshire acquired mortgage banking operations in 2012 and experienced record mortgage origination in the second half of the year due to record low interest rates. Mortgage banking became the second largest source of non-interest income in 2012 and was the largest source in the second half of the year. The industry also experienced unusually high margins in mortgage banking operations during the year. Berkshire is pursuing further expansion of this business line to offset potential reversion of market volumes and margins towards historic levels.

Non-interest income totaled $54 million in 2012 and increased by $18 million (51%) over the prior year. This increase included the full year benefit of the Rome and Legacy acquisitions and a partial year benefit of the CBT, Greenpark, and Beacon acquisitions. The $18 million increase included $13 million in growth in mortgage banking income. Excluding mortgage banking income, all other non-interest income increased by $5 million (14%) primarily due to the benefit of business combinations, and included the benefit of gains in the sale of seasoned loans and payments from new insurance and merchant processing vendors.

Mortgage origination income totaled $13.6 million in 2012 compared to $0.4 million in 2011. Most mortgage production in both years was fixed rate and Berkshire sells most of its fixed rate production to the secondary markets. Income on mortgages held for sale is recorded when mortgage applications are rate locked based on hedges and forward commitments at that time. Mortgage revenue is reported net of the direct costs of origination. Including the acquired mortgage operations, the Company estimated that the mortgage revenue recorded on loans originated for sale in 2012 was in the range of 1.10% - 1.15% of the mortgage amounts.

All other loan related income totaled $3.9 million in 2012, and included $1.6 million in commercial loan servicing fees and $0.9 million in interest rate swap income recorded on commercial lending activity. Deposit related fee income measured 0.45% of average deposit balances in 2012, compared to 0.50% in 2011. This

reduction included the impact of deposits of acquired banks which had a lower proportion of fee producing deposit products and commercial balances. Deposit fee income included overdraft fees which decreased as a percentage of average deposits due to the impact of acquisitions and regulatory changes.

Insurance fee income decreased by 2% in 2012. Due to changing industry conditions, the Company converted a significant portion of its policies to new carriers and surpassed its expectations for account retention. Insurance income has become less seasonal as a result of this change. Insurance income in 2012 included approximately $1.0 million related to successful account transition management, which offset a decrease in contingency income due to adverse claims experience resulting from weather events in 2011. Wealth management income increased by 25% primarily due to a full year benefit of Legacy operations acquired in July 2011. Fourth quarter wealth management fee income increased by 13% in 2012 compared to 2011, due to account growth and improved securities market prices on which much of the income is indexed. Total assets under management, including investment account balances, increased by 14 % to $1.1 billion at year-end 2012, reflecting gains based on service and investment performance.

The Company reported net gains totaling $1.5 million in 2012 and $2.1 million in 2011 which were primarily related to gains recorded at the time of the acquisition of merged banks as a result of common stock investments which had been made prior to merger discussions as part of the Company s ongoing program to invest in common stock of regional community banks. In 2012, the Company reported $1.3 million in all other non-interest income. This included the benefit of income on bank owned life insurance policies. This benefit was partially offset by losses on tax shelter limited partnership interests; these losses are more than offset by the benefit to income tax expense due to income tax credits from these partnerships, which include low income housing and wind and solar power generation. Due to the seasoning of these participations, the related loss decreased, resulting in the increase in all other non-interest income.

Provision for Loan Losses. The provision for loan losses is a charge to earnings in an amount sufficient to maintain the allowance for loan losses at a level deemed adequate by the Company. The level of the allowance is a critical accounting estimate, which is subject to uncertainty. The level of the allowance was included in the discussion of financial condition. The provision for loan losses totaled $10 million in 2012, compared to $8 million in 2011. The provision for loan losses exceeded net loan charge-offs in both years, and resulted in an increase in the allowance for loan losses that was generally related to higher reserves on acquired loans as previously reported in the loan loss allowance discussion.

Non-Interest Expense. Total non-interest expense increased in 2012 by $24 million (21%) to $141 million. This included a full year s impact from 2011 acquisitions together with a partial year impact from 2012 acquisitions. Non-interest expense included conversion and merger related expenses totaling $18 million in 2012 and $20 million in 2011. Merger related expense included compensation and severance costs, professional services, and premises related charges. Conversion expense was primarily related to the Company s core systems conversion in September 2012. Merger and conversion expenses in the last two years were within the range of management s expectations, and the Company expects to achieve its cost saving targets for the Beacon acquisition in 2013 after the acquired operations are fully integrated.

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As previously discussed, Berkshire does not view these merger and conversion expenses as elements of its ongoing operating expenses. Excluding these amounts, non-interest expense increased by $26 million 27% to $123 million. In comparison, total net revenue increased by 39% and Berkshire generated positive operating leverage which contributed to improved profitability. For each acquisition, Berkshire established cost savings targets which were an element of its expected return on investment. The Company believes that it is on track to achieve the cost savings estimates that were established for these mergers. Expense growth in both years included the impact of investments in business expansion, including new branches, and targeted resource additions in certain business lines and infrastructure development. Due to changes in its revenue mix and the impact of merger related, conversion and non-recurring items, the Company relies on non-GAAP measures to assess the efficiency of its operations. The Company believes that its efficiency is improving in accordance with its objectives, as a product of the positive operating leverage and resulting in benefits to its measures of return on equity which were previously discussed.

Most major categories of expense increased due to the additional expenses related to acquired operations. Full time equivalent staff totaled 1,012 employees at year-end 2012 compared to 760 at year-end 2011 (excluding staff related to discontinued operations). FDIC insurance expense continued to decrease in relation to average deposits. Expense of other real estate owned decreased from higher levels in 2011 that resulted from write-downs of properties that were subsequently liquidated. Amortization of intangible assets increased to $5.3 million in 2012 from $4.2 million in the prior year, due primarily to the core deposit intangibles recorded for the bank acquisitions in both years.

Income Tax Expense on Continuing Operations. The effective tax rate on income from continuing operations was 28% in 2012, compared to 10% in 2011. The increase in rate is primarily due to the higher level of pretax income and the lower proportionate benefit of tax advantaged income from investments and bank owned life insurance. These two items provided a 7% reduction in the effective tax rate in 2012, compared to the 35% federal statutory rate. Additionally, the benefit from tax credit limited partnerships and other items offset the 4% effective rate of state income taxes.

Discontinued Operations. Discontinued operations consisted of eight former Legacy branches held for sale in the second half of 2011. Four branches in Berkshire County were divested in the fourth quarter of 2011 for a net gain. The related effective tax rate was 80% due to the non-deductibility of goodwill for income tax purposes in determining the taxable gain on divestiture. Four branches in New York were divested in January 2012 with a loss resulting from conversion expenses. Discontinued operations provided $0.05 in earnings per share in 2011 and a loss of $0.03 in 2012.

Results of Segment and Parent Operations. Berkshire Hills Bancorp (the Parent) has two subsidiary operating segments banking and insurance. Results in the banking segment generally followed the levels and trends of consolidated results, which have been previously discussed. In the insurance segment, a 3% decrease in revenues was offset by a reduction in expenses so that net income was little changed between 2012 and 2011. The Parent s net interest income included dividends from the banking and insurance segment and non-interest income includes undistributed earnings of these segments. Parent non-interest expense included professional fees related to the bank acquisitions. Most of the Parent s revenues are non-taxable revenues from subsidiaries, and the Parent therefore receives a tax benefit related to the taxable loss generated by its expenses.

Total Comprehensive Income. Total comprehensive income includes net income together with other comprehensive income, which was $1.9 million in 2012 and $1.5 million in 2011. Other comprehensive income in both years primarily resulted from unrealized securities gains related to lower market interest rates. Improved results in 2012 were partly offset by a $2.1 million increase in the unrealized loss on derivative hedges due to higher volumes and lower rates in 2012. In 2011, results were net of a $1.1 million net loss on pensions acquired in business combinations.

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Quarterly Results. Quarterly results for 2012 and 2011 are presented in a note to the consolidated financial statements. Quarterly results of operations have been significantly affected by acquisitions, with acquired operations recorded beginning on the acquisition date and merger related expenses being recorded most significantly in periods proximate to the acquisition date. Most categories of revenue and expense increased as a result of these acquisitions, and earnings per share were affected by new shares issued as merger consideration. In the second half of 2011, the Company designated eight Legacy branches as discontinued operations; including conversion expenses, these operations operated at a loss pending divestiture, which resulted in a divestiture gain on four Berkshire County branches in the fourth quarter of 2011 and a divestiture loss on four New York branches in the first quarter of 2012. Quarterly results of operations include revisions as noted in the Revision to Financial Statements note in the consolidated financial statements in 2012 and 2011.

Net interest income increased in each quarter of 2012 due to growth in earning assets resulting from acquisitions and business activities. The acquisition of Greenpark Mortgage operations increased fee income beginning in May. Strong mortgage refinancing demand in the second half of the year further boosted fee income while depressing the net interest margin due to the write-off of mortgage premiums and deferred costs on balances refinanced. A $1.4 million net securities gain was recorded in the fourth quarter due primarily to gains on Beacon stock investments recognized on the merger date. The provision for loan losses increased modestly in the second half of 2012 and net loan charge-offs also increased modestly. As noted above, merger related expenses contributed to changes in non-interest expense, along with charges for the Company s core systems conversion which was completed in September. The effective income tax rate increased during the year as pretax income increased and the proportional benefit of tax preferences decreased. The effective tax rate decreased in the final quarter due to lower pretax income as a result of Beacon merger related charges.

In 2011, in addition to the impact of the acquisitions, net interest income benefited from an improvement in the net interest margin which primarily reflected lower funding costs as deposit rates were reduced in the ongoing low interest rate environment. Changes in the loan loss provision reflected small changes in the loan loss allowance analysis. Third quarter non-interest income included gains recorded on existing investments in Legacy common stock. Quarterly non-interest expense included the impact of the merger related charges noted above. The effective income tax rate for continuing operations decreased to 8% in the second half of the year from 18% in the first half of the year due primarily to the timing of the Legacy acquisition and the related branch divestiture, and costs related to those activities.

COMPARISON OF OPERATING RESULTS FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010

Berkshire s results in 2011 included Rome operations acquired on April 1, 2011 and Legacy operations acquired on July 21, 2011. As a result, most categories of revenue and expense increased due to these acquisitions. Earnings per share were affected by the issuance of 7.0 million additional Berkshire common shares related to these acquisitions. All references to revenue and expense in this discussion exclude discontinued operations of Legacy branches.

Net income increased by $3.7 million (27%) to $17.3 million in 2011, compared to $13.6 million in 2010. Earnings per share decreased slightly to $0.97 from $0.98 due to the additional shares issued for the bank acquisitions. Results in 2011 included $10.4 million in after-tax impact from conversion and merger related items and discontinued operations, compared to $0.4 million for such items in the prior year. Excluding these items, earnings per share benefited from positive operating leverage resulting from revenue growth and disciplined expense management, together with the accretive benefit of the Rome and Legacy acquisitions.

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Merger related items were within the range of the Company s expectations. Merger related expenses consisted primarily of severance and benefit related costs related to the change in control of the acquired entities. Merger expenses also included professional fees and contract termination costs.

Total Net Revenue. Total net revenue increased by $36 million (33% compared to the comparable prior period measure) to a record level of $142 million in 2011. Net revenue per share increased by 3% to $7.93 in 2011. Fee income was 24% of net revenue in 2011, compared to 28% in the prior year, as the acquired banks had a higher reliance on net interest income as a revenue source.

Net Interest Income. Net interest income increased by $30 million (38%) to $107 million in 2011 compared to 2010, including the benefit of the bank acquisitions net of discontinued operations. The net interest margin improved to 3.57% in 2011 compared to 3.28% in 2010. The average yield on earning assets decreased to 4.61% in 2011, compared to 4.73% in the prior year, reflecting the ongoing impact of the low interest rate environment on portfolio yields and on the market interest rates assigned to acquired assets. Net interest income in 2011 included $3.2 million in net credits to interest income for accretion of net discounts on acquired loans. In the ongoing low interest rate environment, the cost of interest bearing liabilities decreased to 1.23% in 2011 compared to 1.72% in the prior year. The cost of deposits decreased to 0.87% in 2011 compared to 1.28% in the prior year.

Non-Interest Income. Non-interest income increased by $6 million (20%) to $36 million in 2011 compared to 2010, including the benefit of the bank acquisitions net of discontinued operations. Deposit related fees increased by $2.8 million (25%) in 2011. Compared to average deposit balances, deposit fees measured 0.50% of average deposits in 2011, compared to 0.53% in the prior year, due primarily to the full year impact of the 2010 adoption of Regulation E affecting overdraft fees. Insurance fee income was flat in 2011, with certain volume gains being offset by ongoing soft insurance premium pricing conditions and lower contingency revenues. The acquired banks had no significant insurance revenues. Wealth management revenues increased by 31% primarily due to the benefit of acquired Legacy operations. Year-end total wealth and investment assets under management increased to nearly $1 billion in 2011 including the acquired Legacy portfolio.

Non-interest income included bank owned life insurance income and losses on tax credit related equity limited partnership interests. Bank owned life insurance income is based on increases in the cash surrender value of these insurance policies. This income was $2.3 million in 2011, compared to $1.4 million in 2010, primarily reflecting the additional acquired policies from the merged banks. Losses on tax credit partnership interests totaled $1.9 million in 2011, compared to $1.4 million in 2010. These losses were more than offset by credits to current period income tax expense which are based on government programs to subsidize the related investments, which include low income housing and solar energy installations. The Company also reported $2.1 million in non-recurring gains in 2011 which primarily related to gains recorded on equity investments in Rome and Legacy which had been made prior to merger discussions as part of the Company s ongoing program to invest in common stock of regional community banks.

Provision for Loan Losses. The provision for loan losses is a charge to earnings in an amount sufficient to maintain the allowance for loan losses at a level deemed adequate by the Company. The level of the allowance is a critical accounting estimate, which is subject to uncertainty. The provision for loan losses totaled $8 million in 2011, compared to $9 million in 2010. The provision for loan losses exceeded net loan charge-offs in both years, and resulted in an increase in the allowance for loan losses that was generally related to loan growth.

Non-Interest Expense. Total non-interest expense increased by $34 million (42%) to $116 million in 2011 compared to 2010. Most categories of non-interest expense increased as a result of the Rome and Legacy acquisitions in 2011. Non-interest expense in 2011 included $20 million in system conversion and merger related expenses. These expenses included $9 million in compensation and severance related expenses, $5 million in professional services, and $3 million in premises related charges, together with accruals for systems conversion costs. Excluding these items, non-interest expense increased by $15 million (18%). Berkshire estimated that by year-end 2011, it had achieved its targeted recurring non-interest expense savings of 35% related to Rome operations and 42% related to Legacy operations.

At the beginning of the second quarter, the FDIC implemented new banking industry deposit insurance assessment rates and formulas. This change reduced FDIC insurance expense, which measured 0.12% of average deposits in 2011, compared to 0.17% in 2010. Expense of other real estate owned increased in 2011 primarily due to write-downs of foreclosed real estate. Amortization of intangible assets increased due primarily to the core deposit intangibles recorded for the bank acquisitions.

Income from Continuing Operations. Income from continuing operations increased by $3 million (21%) to $16 million in 2011 compared to 2010. The effective tax rate on income from continuing operations was 10% in 2011 compared to 15% in 2010. Results in 2011 and prior years included the impact of an accounting error correction related to the tax credit limited partnerships which was not material to the financial statements. This tax credit, which equated to a 7% effective credit to the 2011 effective tax rate, was previously reported as a component of non-interest income. The decrease in 2011 also reflected the benefit of non-taxable gains on the Rome and Legacy acquisitions.

Income from Discontinued Operations. Income from discontinued operations was $914 thousand in 2011. Discontinued operations related to branches held for divestiture in the second half of 2011. Four of these branches were divested in the fourth quarter and the remaining four were divested in January 2012. The divestiture in 2011 resulted in a $5.0 million pre-tax gain. The tax rate on discontinued operations was 80% due to the non-deductibility of goodwill for income tax purposes in determining the taxable gain on divestiture. Primarily as a result of this higher tax rate on discontinued operations, the effective tax rate on total continuing and discontinued operations increased to 25% in 2011 from 15% in the prior year.

Results of Segment and Parent Operations. Results in the banking segment generally followed the levels and trends of consolidated results, which have been previously discussed. In the insurance segment, revenues decreased by 1% due to ongoing soft pricing conditions and reduced contingency fees in the industry. Expenses decreased by 7%, and as a result, insurance segment net income increased by 27%. The Parent s net interest income included dividends from the insurance segment. Parent non-interest expense increased due primarily to professional fees related to the bank acquisitions. Most of the parent s revenues are non-taxable revenues from subsidiaries, and the Parent therefore receives a tax benefit related to the taxable loss generated by its expenses.

Total Comprehensive Income. The Company recorded comprehensive income of $19 million due primarily to $17 million in net income discussed previously. Comprehensive income in 2010 was $10 million, including net income of $14 million which was partially offset by an other comprehensive loss relating to unrealized losses on derivatives instruments due to ongoing low interest rates.

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LIQUIDITY AND CASH FLOWS

Liquidity is the ability to meet cash needs at all times with available cash or by conversion of other assets to cash at a reasonable price and in a timely manner. At year-end 2012, the parent company had $40 million in cash and equivalents, compared to $16 million at the start of the year. This cash was held on deposit in the Bank. The primary ongoing source of funding for the parent company is dividend payments from the Bank and from Berkshire Insurance Group. These subsidiaries paid $17 million in dividends to the parent in 2012. Additional potential sources of liquidity are proceeds from borrowings and capital offerings, and from stock option exercises. In 2012, the Company issued $75 million in subordinated notes to fund merger cash consideration. The Company also arranged a $10 million unsecured line of credit for working capital purposes; this line was fully utilized at year-end. The main uses of liquidity are the payment of common stockholder dividends, routine operating expenses, debt service on outstanding borrowings and debentures, purchases of treasury stock, and business acquisitions. The Company generally expects to maintain cash on hand equivalent to normal cash uses, including common stock dividends, for at least a one year period. Sources and uses of cash at the parent are reported in the condensed financial statements of the parent company included in the notes to the consolidated financial statements. There are certain restrictions on the payment of dividends by the Bank as discussed in the Stockholders Equity note to the consolidated financial statements. As of year-end 2012, the statutory limit on future dividend payments by the Bank totaled $41 million. This amount is based on retained earnings of the Bank and is expected to be supplemented by future bank earnings in accordance with the statutory formula.

The Bank s primary source of liquidity is customer deposits and the main use of liquidity is the funding of loans and lending commitments. Additional routine sources are borrowings, repayments of loans and investment securities, and the sale and repayments of investment securities. In 2012, the primary uses of funds were loan growth and an increase in mortgage loans held for sale. The primary sources of funds were deposit growth and borrowings. The Bank closely monitors its liquidity position on a daily basis. Sources of borrowings include advances from the FHLBB and borrowings at the Federal Reserve Bank of Boston. As of year-end 2012, based on its arrangements and collateral amounts, the Bank had potential borrowing capacity totaling $622 million with the Federal Home Loan Bank of Boston. The Bank is also expanding its relationships with correspondent banks and securities firms to maintain availability for overnight borrowings and repurchase agreements. The Bank utilizes the mortgage secondary market as a source of funds for residential mortgages which are sold into that market. Secondary market counterparties include federal mortgage agencies and national financial institutions. The Bank also utilizes national bank counterparties for derivative instruments that it uses in conjunction with its borrowing and mortgage banking activities.

In all three of the most recent years, deposit growth has exceeded loan growth. In 2011 and 2010, excess funds from deposit growth were used to pay down borrowings. In 2012, the Company decided to take advantage of capital market conditions by utilizing fixed rate subordinated debt rather than common equity for merger consideration. The Company also utilized overnight funds to support its expanded mortgage banking operations. As a result, the use of borrowings increased in 2012. One general measure of liquidity is the loan/deposit ratio, which was affected by the activities described above, together with the impact of financial instruments acquired in business combinations. This ratio stood at 97% at year-end 2012, compared to 95% at the start of the year and indicated a favorable but slightly less liquid position as a result of the year s events. For the industry, a key challenge has been growth in liquidity - as savings activities in the economy have outpaced investment activities. Banks have had to carry more of their deposit funds in liquid cash and securities, rather than in loans. Due to its acquisition activities, the Company has been able to build its balance of loans and loans held for sale in addition to the volume generated from loan operations. The Company believes that it is continuing to improve its access to sources of liquidity and capital. In 2012, this included major expansions in secondary market and loan sales outlets along with financial derivatives sources, expansion of fed funds sources, continued de novo branch expansion, the initiation of a parent company line of credit, the private

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placement of institutional subordinated debt which qualifies as regulatory capital, and the higher volume of issued and outstanding common stock. Through its business combinations, Berkshire now has branches in new geographic markets which are a potential source of new deposit funding in the future.

The greatest sources of uncertainty affecting liquidity are deposit withdrawals and usage of loan commitments, which are influenced by interest rates, economic conditions, and competition. Due to the unusual and prolonged low interest rate environment, there is uncertainty about the behavior of deposits if interest rates increase at some future time as anticipated. The Company believes that its market positioning and relationship focus will generally enhance the stability of its deposits, and it also models various scenarios for the purpose of contingency liquidity planning. The Company has had success in building commercial deposits, including large balances from certain sources. The Company monitors its deposit concentrations to manage the impact of possible changes in these sources. At the end of 2012, the unlimited FDIC insurance on bank transaction account balances terminated as scheduled under statute. The Company does not anticipate that there will be a significant impact from this change. Additionally, the Bank offers 100% insurance on all deposit balances as a result of the combination of FDIC insurance and the Massachusetts Depositors Insurance Fund. Due to its growth, the Bank may need to consider alternatives to its use of this supplementary insurance and its liquidity planning as expanded as a result. The Bank relies on competitive rates, customer service, and long-standing relationships with customers to manage deposit and loan liquidity. Based on its historical experience, management believes that it has adequately provided for deposit and loan liquidity needs. Both liquidity and capital resources are managed according to policies approved by the Board of Directors and executive management and the Board reviews liquidity metrics and contingency plans on a regular basis.

CAPITAL RESOURCES

The Bank must satisfy various regulatory capital requirements. Regulatory capital requirements are discussed in the Regulation and Supervision section of Item 1, in the Risk Factors discussion, and in the Stockholders Equity note to the consolidated financial statements. Please also see management s discussion of financial condition for additional information about liquidity and capital at year-end 2012. In November, 2012, the Company renewed a universal shelf registration with the Securities and Exchange Commission for the issuance of up to $150 million in securities, including debt securities, common stock, or preferred stock. The Company did not issue any securities under the previous registration, and does not have any specific plans for issuances under the current registration.

Berkshire views its earnings and related internal capital generation as a primary source of capital to support dividends and growth of the franchise. Additionally, the Company generally uses the issuance of common stock as the primary source of consideration for bank acquisitions, and such acquisitions may result in net increases or decreases in its capital ratios. In 2012, the bank acquisitions resulted in a net increase in the Company s capital ratios due to the use of subordinated debt to achieve a more favorable blended cost of capital. Berkshire s long term objective is to generate a double digit annual return on equity, and the Company evaluates lending, investment, and acquisition decisions with this objective as a benchmark. In the fourth quarter of 2011, Berkshire s Board of Directors established a new Capital Committee, which is responsible for assisting the Board in planning for future capital needs and for ensuring compliance with regulations pertaining to capital structure and levels. In 2012, Berkshire increased its outstanding shares by 19% from 21.1 million to 25.1 million due to the issuance of merger consideration. The Company believes that this provides further liquidity and visibility to its common stock, and that the market for its stock is an additional capital resource over the long run. Additionally, the Company continues to monitor market conditions for Tier Two regulatory capital such as preferred stock or subordinated debt, which are additional potential future capital resources to the Company and/or the Bank.

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AVERAGE BALANCES, INTEREST, AVERAGE YIELDS/COST AND RATE/VOLUME ANALYSIS

Tables with the above information are presented in Item 6 of this report.

CONTRACTUAL OBLIGATIONS

The year-end 2012 contractual obligations were as follows:

Item 7-7A - Table 1 - Contractual Obligations

(In thousands)	Total	Less than One Year	One to Three Years	Three to Five Years	After Five Years
FHLBB borrowings (1)	$ 348,471	$ 246,067	$ 30,280	$ 31,645	$ 40,479
Subordinated notes	89,617				89,617
Operating lease obligations (2)	137,106	6,505	13,303	13,546	103,752
Purchase obligations (3)	73,528	16,396	21,868	17,632	17,632
Total Contractual Obligations	$ 648,722	$ 268,968	$ 65,451	$ 62,823	$ 251,480

Merger related obligations are not included.

(1) Consists of borrowings from the Federal Home Loan Bank. The maturities extend through 2027 and the rates vary by borrowing.

(2) Consists of leases, bank branches and ATMs through 2036.

(3) Consists of obligations with multiple vendors to purchase a broad range of services.

Further information about borrowings and lease obligations is in the notes on borrowings and commitments to the financial statements. Other obligations increased, including the impact of business combinations, system upgrades, and overall business expansion.

OFF-BALANCE SHEET ARRANGEMENTS

In the normal course of operations, Berkshire engages in a variety of financial transactions that, in accordance with generally accepted accounting principles are not recorded in the Company s financial statements. These transactions involve, to varying degrees, elements of credit, interest rate and liquidity risk. Such transactions are used primarily to manage customers requests for funding and take the form of loan commitments and lines of credit. A further presentation of the Company s off-balance sheet arrangements is presented in the notes to the consolidated financial statements and in the above discussion relating to payments due under contractual obligations. Information about derivative financial instruments and hedging activities is reported in the related note to the consolidated financial statements, and was included in management s discussion of changes in financial condition.

FAIR VALUE MEASUREMENTS

The most significant fair value measurements recorded by the Company are those related to assets and liabilities acquired in business combinations. These measurements are discussed further in the mergers and acquisitions note to the consolidated financial statements.

The Company makes further measurements of fair value of certain assets and liabilities, as described in the related note in the financial statements. Recurring fair values of financial instruments primarily relate to securities and derivative instruments. A valuation hierarchy is utilized based on generally accepted accounting principles. Measurements based on Level 3 inputs rely the most on subjective management judgments. Level 3 recurring measurements relate primarily to the $17 million fair value of a local tax advantaged economic development bond issued to a Berkshire County non-profit, which is classified as a trading security. Changes in the fair value of this security are recorded in non-interest income, as are offsetting changes in the accompanying interest rate swap. Non-recurring fair value measurements primarily relate to securities held to maturity, restricted equity securities, impaired loans, and goodwill and other

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intangibles. When measurement is required, these measures are generally based on Level 3 inputs. Non-recurring fair values of financial instruments relate primarily to impairment analysis of economic development bonds recorded as held-to-maturity, restricted equity securities, and loans. Fair value measurements of non-financial assets and liabilities primarily relate to impairment analyses of intangibles and goodwill. The Company performed an impairment analysis of its goodwill in 2012 and and determined that there was no impairment.

The Company also provides a summary of estimated fair values of financial instruments at each quarter-end. The category of financial assets with the most significant difference between carrying value and fair value is the net loan category, which is valued based entirely on Level 3 analysis. The fair value of loans is estimated to be at a $49 million (1%) premium to carrying value at year-end 2012, compared to a 2% premium at year-end 2011 and a 3% premium at year-end 2010. The premium value of loans has narrowed based on higher prepayment speeds and lower replacement yields despite the benefit of ongoing improvement in the credit profile of the portfolio. Additionally, as the portfolio had grown due to the acquisition of loans in business combinations which are recorded at fair value, the fair value premium related to loans recorded at cost has declined as a percentage of the whole portfolio. The excess fair value of deposits over carrying amount increased modestly due to the impact of lower market interest rates despite continuing decreases in the cost of time deposits. As a result of the lower loan premium and higher deposit value, there was a decline in the net economic value of equity related to those instruments, based solely on the measures used for the purpose of this analysis. This change reflects the mounting pressure on net interest margins in the industry, but does not take into account the non-interest income generated by these customer relationships or the long term intangible value of the Company s franchise in its markets.

IMPACT OF INFLATION AND CHANGING PRICES

The financial statements and related financial data presented in this Form 10-K have been prepared in conformity with accounting principles generally accepted in the United States of America, which require the measurement of financial position and operating results in terms of historical dollars, without considering changes in the relative purchasing power of money over time due to inflation. Unlike many industrial companies, substantially all of the assets and liabilities of the Bank are monetary in nature. As a result, interest rates have a more significant impact on the Bank s performance than the general level of inflation. Interest rates may be affected by inflation, but the direction and magnitude of the impact may vary. A sudden change in inflation (or expectations about inflation), with a related change in interest rates, would have a significant impact on our operations.

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IMPACT OF NEW ACCOUNTING PRONOUNCEMENTS

Please refer to the note on Recent Accounting Pronouncements in Note 1 to the consolidated financial statements for a detailed discussion of new accounting pronouncements.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

MANAGEMENT OF INTEREST RATE RISK AND MARKET RISK ANALYSIS

Qualitative Aspects of Market Risk. The Company s most significant form of market risk is interest rate risk. The Company seeks to avoid fluctuations in its net interest income and to maximize net interest income within acceptable levels of risk through periods of changing interest rates. The Company maintains an Asset/Liability Committee that is responsible for reviewing its asset/liability policies and interest rate risk position. This Committee meets monthly and reports trends and interest rate risk position to the Risk Management Committee and Board of Directors on a quarterly basis. The extent of the movement of interest rates is an uncertainty that could have a negative impact on the Company s earnings. The Company has managed interest rate risk by emphasizing assets with shorter-term repricing durations, periodically selling long term fixed-rate assets, promoting low cost core deposits, and using FHLBB advances to structure its liability repricing durations. The Company also uses interest rate swaps in order to enhance its interest rate risk position and manage its balance sheet.

Quantitative Aspects of Market Risk. The Company uses a simulation model to measure the potential change in net interest income that would result from both an instantaneous or ramped change in market interest rates assuming a parallel shift along the entire yield curve. The chart below shows the analysis of a ramped change. Loans, deposits and borrowings were expected to reprice at the repricing or maturity date. The Company uses prepayment guidelines set forth by market sources as well as Company generated data where applicable. Cash flows from loans and securities are assumed to be reinvested based on current operating conditions and strategies. Other assumptions about balance sheet mix are generally held constant. No material changes have been made to the methodologies used in the model.