

BERKSHIRE HILLS BANCORP INC  
Form 10-K  
March 17, 2014  
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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, 2013**

**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.**

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(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of

**04-3510455**  
(I.R.S. Employer Identification No.)

incorporation or organization)

**24 North Street, Pittsfield, Massachusetts**  
(Address of principal executive offices)

**01201**  
(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**  
**Common stock, par value \$0.01 per share**

**Name of Exchange on which registered**  
**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  No

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  No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate 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  No

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.

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)

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Large Accelerated Filer

Accelerated Filer

Non-Accelerated Filer

Smaller Reporting Company

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates was approximately \$681 million, based upon the closing price of \$27.76 as quoted on the New York Stock Exchange 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 11, 2014 was 25,105,136.

**DOCUMENTS INCORPORATED BY REFERENCE:** Portions of the Proxy Statement for the 2014 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, plan, potential, estimate, project, believe, intend, anticipate, expect, target and similar expressions. These forward-looking statements are subject to 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. 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 Berkshire Bank ( the Bank ) and Berkshire Insurance Group. 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 (office count includes NY branches acquired in January 2014):

Berkshire's common shares are listed on the New York Stock Exchange under the trading symbol BHLB. At year-end 2013, Berkshire's closing stock price was \$27.27 and there were 25.036 million shares outstanding. Berkshire is a regional bank and financial services company providing the service capabilities of a larger institution and the focus and responsiveness of a local partner to its communities. The Company seeks to distinguish itself based on the following attributes:

- **Strong financial condition**
- **Diversified revenue drivers**
- **Established footprint in attractive markets**
- **Experienced leadership team**

- **AMEB culture**
- **Well positioned for growth**
- **Focused on long-term profitability goals and shareholder value**

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The Bank has 92 full-service banking 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 also has commercial and retail lending offices located in Eastern Massachusetts. The Bank's operations include those acquired as a result of four bank mergers in 2011 - 2012:

- 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

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- 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 acquired 20 branches in Central New York from Bank of America on January 17, 2014, with total deposits of approximately \$440 million at the date of acquisition.

The Bank serves the following regions:

- **Western New England**, with 31 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 Boston and New York City. The Pittsfield 2012 MSA GDP totaled \$5 billion. At year-end 2013, the Company had approximately \$1.0 billion in loans and \$1.5 billion in deposits in its Western New England Market.
- **New York**, with 39 banking offices serving the Albany Capital District and Central New York. 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 which began in 2005. 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 2014 branch acquisition is also primarily located in this market. The Albany/Schenectady 2012 MSA GDP was \$42 billion, and the Rome/Utica/Syracuse total 2012 MSA GDP was \$38 billion. At year-end 2013, Berkshire had approximately \$1.4 billion in loans and \$1.2 billion in deposits in the New York region. The New York branch purchase in January 2014 contributed an additional \$440 million in deposit balances.
- **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 2012 MSA GDP was \$105 billion. At year-end 2013, Berkshire had approximately \$0.7 billion in loans and \$0.9 billion in deposits in this region.
- **Eastern Massachusetts**, with several 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 from Worcester within the commuting and commerce area of Boston, east to Boston and its suburbs. 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 2013, including certain administrative balances, Berkshire had approximately \$1.1 billion in loans and \$0.2 billion in deposits in this region.

These regions are viewed as having favorable demographics and provide an attractive regional niche for the Bank to distinguish itself from larger national and super-regional banks, and from smaller community banks, while serving its market area. The Bank is the only locally headquartered regional bank serving this footprint. The Company views its footprint as comparatively stable, with modest economic growth prospects in rural areas and higher growth prospects



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in more developed areas. The strongest growth is expected to be in Eastern Massachusetts and the New York Capital District. The Company views itself as positioned to take advantage of the best growth opportunities as they develop across its geography. 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. 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 growth opportunities as they arise. 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.

In addition to business acquisitions, Berkshire's expansion has been based on team and talent recruitment. In 2013, this included the recruitment of a commercial banking team in Eastern Massachusetts as well as commercial bankers in the Syracuse and Hartford markets, a middle market leasing team, new small business banking leadership and regional expansion of the mortgage banking team. Shortly after year-end, the Company announced the recruitment of a new commercial market leader for its New York Region.

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.

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 is mining in order to better inform its strategic direction and business execution. Berkshire has also expanded its mobile banking and remote capture offerings and utilizes its internet website and online banking tools to extend the convenience that it offers to customers.

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. In 2013, Berkshire expanded the responsibilities of its Executive Vice President/Chief Risk Officer to also include the newly created position of Chief Administrative Officer. Through internal promotions, the Company named a new Executive Vice President/Commercial Banking, a new Senior Vice President/Chief Credit Officer, and a new Senior Vice President/Information Technology. The Company also recruited a new Senior Vice President/Principal Accounting Officer who was promoted to Executive Vice President/Chief Financial Officer shortly after year-end. Additionally, early in 2014 the Company recruited a new Senior Vice President/Treasurer.

**COMPANY WEBSITE AND AVAILABILITY OF SECURITIES AND EXCHANGE COMMISSION FILINGS**

Information regarding the Company is available through the Investor Relations tab at 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



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available free of charge at sec.gov and at 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.

**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. 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)	2013		2012		2011		2010		2009	
	Amount	Percent of Total	Amount	Percent of Total	Amount	Percent of Total	Amount	Percent of Total	Amount	Percent of Total
Residential mortgages	\$ 1,384.3	33%	\$ 1,324.3	33%	\$ 1,020.4	34%	\$ 645.0	30%	\$ 609.0	31%
Commercial mortgages	1,417.1	34	1,413.5	35	1,156.2	39	925.6	43	851.8	43
Commercial business	687.3	16	600.1	15	410.3	14	286.1	13	186.0	10
Total commercial loans	2,104.4	50	2,013.6	50	1,566.5	53	1,211.7	56	1,037.8	53
Consumer	691.8	17	650.7	17	369.6	13	285.5	14	314.8	16
Total loans	\$ 4,180.5	100%	\$ 3,988.6	100%	\$ 2,956.5	100%	\$ 2,142.2	100%	\$ 1,961.6	100%
Allowance for loan losses	(33.3)		(33.2)		(32.4)		(31.9)		(31.8)	
Net loans	\$ 4,147.2		\$ 3,955.4		\$ 2,924.1		\$ 2,110.3		\$ 1,929.8	

**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 2013, the Bank's adjustable rate mortgage portfolio totaled \$401 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. As part of its business activities, the Bank also enters into commercial loan participations with regional banks and purchases and sells commercial loans in its footprint.

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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 its 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.

The Bank's commercial lending team in Central/Eastern Massachusetts serves the commercial middle market with 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 direct and indirect automobile loan portfolios are growing. 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 2013. 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
<b>Construction mortgage loans:</b>				
Residential	\$ 5,773	\$ 17,397	\$	\$ 23,170
Commercial	39,514	99,503		139,017
Commercial business loans	207,164	356,694	123,435	687,293
<b>Total</b>	<b>\$ 252,451</b>	<b>\$ 473,594</b>	<b>\$ 123,435</b>	<b>\$ 849,480</b>

For the \$597 million of loans above which mature in more than one year, \$105 million of these loans are fixed-rate and \$492 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.

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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

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on a review of certain factors including risk ratings, recourse, loan-to-value ratios and material policy exceptions. The 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 \$26 million each, or 5.3% of total risk based capital. Total year-end commercial construction loans outstanding were 29% of the Bank's risk based capital at year-end. The Bank's portfolio management objective has been to reduce these concentrations. The FDIC has established monitoring guidelines of 100% for this ratio. 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 2013 if nonaccruing loans had been current according to their original terms, amounted to \$1.3 million. Included in the amount is \$34 thousand related to troubled debt restructurings. The amount of interest income on those loans that was recognized in net income in 2013 was \$0.7 million. Included in this amount

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is \$101 thousand related to troubled debt restructurings. Interest income on accruing troubled debt restructurings totaled \$0.4 million for 2013. The total carrying value of troubled debt restructurings was \$10.8 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 to prior periods.

## Item 1 - Table 3 - Problem Assets and Accruing TDR

(In thousands)	2013	2012	2011	2010	2009
<b>Non-accruing loans:</b>					
Residential mortgages	\$ 7,868	\$ 7,466	\$ 7,010	\$ 2,173	\$ 3,304
Commercial mortgages	13,739	12,617	14,280	9,488	31,917
Commercial business	2,355	3,681	990	1,305	3,115
Consumer	3,493	1,748	1,954	746	364
Total non-performing loans	27,455	25,512	24,234	13,712	38,700
Real estate owned	2,758	1,929	1,900	3,386	30
Total non-performing assets	\$ 30,213	\$ 27,441	\$ 26,134	\$ 17,098	\$ 38,730
<b>Troubled debt restructurings (accruing)</b>					
Troubled debt restructurings (accruing)	\$ 8,344	\$ 3,641	\$ 1,263	\$ 7,829	\$ 17,818
Accruing loans 90+ days past due	\$ 9,223	\$ 18,977	\$ 10,184	\$ 1,054	\$ 91
Total non-performing loans/total loans	0.66%	0.64%	0.82%	0.64%	1.97%
Total non-performing assets/total assets	0.53%	0.52%	0.65%	0.59%	1.43%

**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). At the time of acquisition, no allowance for loan losses is assigned to loans acquired in business combinations. These loans 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)	2013	2012	2011	2010	2009
Balance at beginning of year	\$ 33,208	\$ 32,444	\$ 31,898	\$ 31,816	\$ 22,908
<i>Charged-off loans:</i>					
Residential mortgages	2,426	2,647	1,322	409	2,016
Commercial mortgages	5,026	4,229	4,046	6,403	27,596
Commercial business	2,917	697	1,443	2,685	5,945
Consumer	2,467	1,877	885	1,188	3,586
Total charged-off loans	12,836	9,450	7,696	10,685	39,143
<i>Recoveries on charged-off loans:</i>					
Residential mortgages	399	103	231	213	
Commercial mortgages	549	52	189	794	22
Commercial business	211	96	109	1,094	64
Consumer	414	373	150	140	235
Total recoveries	1,573	624	679	2,241	321
Net loans charged-off	11,263	8,826	7,017	8,444	38,822
Allowance attributed to loans acquired by merger					
Provision for loan losses	11,378	9,590	7,563	8,526	47,730
Transfer of commitment reserve					
Balance at end of year	\$ 33,323	\$ 33,208	\$ 32,444	\$ 31,898	\$ 31,816
<i>Ratios:</i>					
Net charge-offs/average loans	0.29%	0.26%	0.27%	0.42%	1.96%
Recoveries/charged-off loans	12.25	6.60	8.82	20.97	0.82
Net loans charged-off/allowance for loan losses	33.80	26.58	21.63	26.47	109.81
Allowance for loan losses/total loans	0.80	0.83	1.10	1.49	1.62
Allowance for loan losses/non-accruing loans	121.37	130.17	133.88	232.63	82.21

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

Residential mortgages	\$ 7,562	0.55%	\$ 6,444	0.49%	\$ 3,420	0.34%	\$ 3,200	0.50%	\$ 3,169
Commercial business	5,770	0.85	5,707	0.95	4,566	1.11	6,498	2.27	6,099

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

Residential mortgages	\$ 7,562	33.11%	\$ 6,444	33.20%	\$ 3,420	34.51%	\$ 3,200	30.11%	\$ 3,169	31.05%
Commercial business	5,770	9.08	5,707	15.05	4,566	13.88	6,498	13.35	6,099	9.48

**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 three to five 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 2013. 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

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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

(In thousands)	2013		2012		2011	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value	Amortized Cost	Fair Value
<b>Securities available for sale</b>						
Municipal bonds and obligations	\$ 77,852	\$ 77,671	\$ 79,498	\$ 84,757	\$ 73,436	\$ 77,854
Mortgage-backed securities	610,326	601,429	318,245	321,685	289,084	292,707
Other bonds and obligations	61,123	58,975	35,241	34,436	30,702	28,186
Marketable equity securities	20,041	21,973	22,467	25,291	20,236	21,009
<b>Total securities available for sale</b>	<b>\$ 769,342</b>	<b>\$ 760,048</b>	<b>\$ 455,451</b>	<b>\$ 466,169</b>	<b>\$ 413,458</b>	<b>\$ 419,756</b>
<b>Securities held to maturity</b>						
Municipal bonds and obligations	\$ 4,244	\$ 4,244	\$ 8,295	\$ 8,295	\$ 10,349	\$ 10,349
Mortgage-backed securities	73	75	76	83	79	83
Tax advantaged economic development bonds	40,260	41,101	41,678	43,137	47,869	49,348
Other bonds and obligations	344	344	975	975	615	615
<b>Total securities held to maturity</b>	<b>\$ 44,921</b>	<b>\$ 45,764</b>	<b>\$ 51,024</b>	<b>\$ 52,490</b>	<b>\$ 58,912</b>	<b>\$ 60,395</b>
<b>Trading account security</b>	<b>\$ 13,096</b>	<b>\$ 14,840</b>	<b>\$ 13,610</b>	<b>\$ 16,893</b>	<b>\$ 14,096</b>	<b>\$ 17,395</b>
<b>Restricted equity securities</b>	<b>\$ 50,282</b>	<b>\$ 50,282</b>	<b>\$ 39,785</b>	<b>\$ 39,785</b>	<b>\$ 37,118</b>	<b>\$ 37,118</b>

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

(In thousands)	2013		2012		2011	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value	Amortized Cost	Fair Value
U.S. Treasuries, other Government agencies and corporations	\$ 630,442	\$ 623,478	\$ 340,789	\$ 347,058	\$ 309,399	\$ 313,799
Municipal bonds and obligations	135,451	137,855	143,080	153,082	145,750	154,946
Other bonds and obligations	111,749	109,601	76,001	75,197	68,435	65,919

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Total Securities	\$	877,642	\$	870,934	\$	559,870	\$	575,337	\$	523,584	\$	534,664
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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 2013 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 3-5 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		More than One Year to Five Years		More than Five Years to Ten Years		More than Ten Years		Total	
	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield
Municipal bonds and obligations	\$ 1.1	1.69%	\$ 4.5	4.92%	\$ 18.9	6.30%	\$ 57.6	5.66%	\$ 82.1	5.71%
Mortgage-backed securities	0.0	6.04	11.3	3.19	10.5	2.02	588.6	2.18	610.4	2.20
Other bonds and obligations	3.0	5.22	6.1	3.14	62.3	4.30	30.3	5.01	101.7	4.47
Total	\$ 4.1	4.26%	\$ 21.9	3.53%	\$ 91.7	4.45%	\$ 676.5	2.60%	\$ 794.2	2.85%

**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

Demand	\$	655.7	17%	%	529.0	15%	%	377.9	14%	%
Money market		1,389.2	35	0.9	1,189.1	34	0.4	833.3	31	0.7
Time		1,085.8	28	1.2	1,056.0	31	1.6	902.6	33	1.8

At year-end 2013, the Bank had time deposit accounts in amounts of \$100 thousand or more maturing as follows:

Item 1 - Table 9 - Maturity of Deposits &gt; \$100,000

Maturity Period	Amount	Weighted Average Rate
Three months or less	\$ 74,379	1.49%
Over 3 months through 6 months	66,935	1.04
Over 6 months through 12 months	88,193	1.03
Over 12 months	281,239	1.48
Total	\$ 510,746	1.34%

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 to fix the interest rate on some of its borrowings, most of which are designated as cash flow hedges. The Company also offers interest rate swaps to commercial loan customers who wish to fix the interest rates on their loans, and the Company backs these swaps with offsetting swaps with national bank counterparties. These swaps are designated as economic hedges. Additionally the Company's mortgage banking activities also result in derivatives. Interest rate lock commitments are provided on applications for residential mortgages intended for resale and are accounted for as non-hedging derivatives. The Company arranges offsetting forward sales commitments for most of these rate-locks with national bank counterparties, which are designated as economic hedges.

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 third-party firms which assist in marketing derivative transactions, executing transactions, and providing information for bookkeeping and accounting purposes.

At year-end 2013, the Company held derivative financial instruments with a total notional amount of \$905 million, including cash flow hedges consisting of interest rate swaps on Federal Home Loan Bank borrowings totaling \$410 million. In conjunction with the New York branch acquisition, the Company terminated these cash flow hedges in the first quarter of 2014, and recorded an after-tax charge of approximately \$5.1 million which had no significant effect on stockholders' equity since the after-tax unrealized loss on these hedges was already recorded in other comprehensive income in stockholders' equity. Also during the first quarter of 2014, the Company entered into \$300 million of new cash flow hedges based on an analysis of its current interest rate sensitivity.

**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 2012, the Wealth Management business line expanded with the integration of the Renaissance Investment Group in the Legacy merger. At year-end 2013, assets under management totaled \$1.3 billion (including custodial and investment accounts). 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.

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**PERSONNEL**

At year-end 2013, the Company had 939 full time equivalent employees. Total employees decreased from 1,012 at the start of the year due to merger integration and restructuring initiatives. 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.

**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**

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The Company 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 depository institutions or branches of other 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, the Company 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,

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whether by the Commissioner, the Massachusetts legislature, the FDIC, the Federal Reserve Board or Congress, could have a material adverse impact on the Company, 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 the Company, was eliminated. At the same time, responsibility for the regulation and supervision of savings and loan holding companies, such as the Company, was transferred 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 the Company, mandated regulations requiring 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.

The Consumer Financial Protection Bureau has finalized the rule implementing the Ability to Pay requirements of the Dodd-Frank Act. The regulations generally require creditors to make a reasonable, good faith determination as to a borrower's ability to repay most residential mortgage loans. The final rule establishes a safe harbor for certain Qualified Mortgages, which contain certain features deemed less risky and omit certain other characteristics considered to enhance risk. The Ability to Repay final rules were effective January 10, 2014.

Many of the provisions of the Dodd-Frank Act are subject to delayed effective dates and/or require the issuance of implementing regulations. The regulatory process is ongoing and the 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 depository institution, 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

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Massachusetts-chartered institution 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 institutions 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 institution 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 institution'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 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 an institution may not exceed 20.0% of the total of the institution's capital, which is defined under Massachusetts law as the sum of the institution'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 from or otherwise becoming indebted to, their institution, 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 institution 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 institution in an amount permissible under the institution's loan to one borrower limit.

The loans described above require approval of the majority of the members of the institution'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 institution.

**Investment Activities.** In general, Massachusetts-chartered institutions 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 institutions may also 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 institution 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 institution 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 institution's business in a manner which is unsafe, unsound or contrary to the depositors interests or been negligent in

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the performance of their duties. In addition, upon finding that a institution 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 institution 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 DIF has recently advised the Bank that its excess deposits covered by the DIF have grown to a size at which DIF policy requires that the Bank either secure a substantial reinsurance policy, with the DIF as loss payee, or withdraw from the DIF. The Bank is evaluating its options and may withdraw from the DIF. The withdrawal from the DIF would not affect the Bank's federal deposit insurance. Under Massachusetts law, withdrawal from the DIF will require the Bank to convert from a Massachusetts savings bank to a Massachusetts trust company charter. The Company believes that the powers of a Massachusetts trust company and a Massachusetts savings bank are generally similar. The charter conversion would have some regulatory consequences for the Bank, such as the loss of grandfathered authority under federal law to invest in certain equity securities (although the Company itself can continue to make such investments). On balance, however, the Company does not believe that the Bank's change in charter, should it occur, will have a material impact on its business.

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.

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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,

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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.

In July 2013, the FDIC and the other federal bank regulatory agencies issued a final rule that will 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. Among other things, the rule establishes a new common equity Tier 1 minimum capital requirement (4.5% of risk-weighted assets); sets the leverage ratio at a uniform 4% of total assets; increases the minimum Tier 1 capital to risk-based assets requirement (from 4% to 6% of risk-weighted assets); and assigns a higher risk weight (150%) to exposures that are more than 90 days past due or are on nonaccrual status and to certain commercial real estate facilities that finance the acquisition, development or construction of real property. The final rule also requires unrealized gains and losses on certain available-for-sale securities holdings to be included for purposes of calculating regulatory capital requirements unless a one-time opt-out is exercised. The rule limits a banking organization's capital distributions and certain discretionary bonus payments to executive officers if the banking organization does not hold a capital conservation buffer consisting of 2.5% of common equity Tier 1 capital to risk-weighted assets in addition to the amount necessary to meet its minimum risk-based capital requirements. The final rule also implements the Dodd-Frank Act's directive to apply to savings and loan holding companies consolidated capital requirements that are not less stringent than those applicable to their subsidiary institutions. The final rule is effective January 1, 2015. The capital conservation buffer will be phased in from January 1, 2016 to January 1, 2019, when the full capital conservation buffer will be effective.

As a savings and loan holding company, the Company is not currently subject to any separate regulatory capital requirements, although that will change as of January 1, 2015, as is described in a subsequent section. 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 2013, the Bank met each of its capital requirements.

**Interstate Banking and Branching.** Federal law permits an institution, such as the Bank, to acquire another 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, Connecticut and Tennessee, as well as Massachusetts. At its interstate branches, the Bank may conduct any activity authorized under Massachusetts law that is permissible either for an institution 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, the Connecticut Commissioner of Banking and the Tennessee Commissioner of Financial Institution may exercise certain regulatory authority over the Bank's branches in their respective states.

**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%



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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%.

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.

At December 31, 2013, the Bank met the criteria for being considered well-capitalized as defined in the prompt corrective action regulations.

In connection with the final capital rule described earlier, the federal banking agencies have adopted revisions to the prompt corrective action framework, effective January 1, 2015. Under the revised prompt corrective action requirements, insured depository institutions would be required to meet the following in order to qualify as well capitalized: (1) a common equity Tier 1 risk-based capital ratio of at least 6.5%; (2) a Tier 1 risk-based capital ratio of at least 8% (increased from 6%); (3) a total risk-based capital ratio of at least 10% (unchanged) and (4) a Tier 1 leverage ratio of 5% or greater (unchanged).

**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 an institution and any companies which are controlled by such parent holding company are affiliates of the institution. Generally, Section 23A limits the extent to which the institution or its subsidiaries may engage in covered transactions, such as loans, with any one affiliate to 10% of such institution'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 institution 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 institution's employees and does not give preference to the insider over the employees. Federal law places additional limitations on loans to executive officers.

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**Enforcement.** The FDIC has extensive enforcement authority over insured institutions, including the Bank. This enforcement authority includes, among other things, the ability to assess civil money penalties, issue cease and desist orders and 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 institution 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 limits. The FDIC insures deposits up to the standard maximum deposit insurance amount ( SMDIA ) of \$250,000. 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 \$100,000 to \$250,000. The Dodd-Frank Act provided for temporary unlimited coverage of certain noninterest bearing transaction accounts, but such unlimited coverage expired 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 and certain adjustments set forth in FDIC regulations. Institutions deemed to present higher risk to the insurance fund pay higher assessments. The overall assessment range, including prospective adjustments, is 2.5 to 45 basis points. Assessment rates are scheduled to decline as the FDIC fund 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.

FDIC insured institutions are also required to pay assessments to the FDIC to fund interest payments on bonds issued by the Financing Corporation, an agency of the federal government established to recapitalize a predecessor 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 base of the fund. For the quarter ended December 31, 2013, the Financing Corporation assessment amounted to 0.64 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 FDIC deposit insurance.

The Dodd-Frank Act increased the minimum target federal deposit insurance fund 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 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.



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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. It has improved marginally in subsequent quarters, though it is still much lower than 2008 levels.

**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, which was made by the Bank, allows the parent holding company to be regulated as a savings and loan holding company, rather than as a bank holding company under the federal Bank Holding Company Act. As such, the Company is registered as a savings and loan holding company 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 Company 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 institution. By regulation, the Federal Reserve Board may restrict or prohibit the Bank from paying dividends. The Federal Reserve Board generally exercises its regulatory authority over the Company through the Federal Reserve Bank of Boston.

Federal law authorizes unitary savings and loan holding companies to engage in activities permitted for a financial holding company under federal law 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 and 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.

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 be 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), an 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,



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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 2013, the Bank maintained at least 65% of its portfolio assets in qualified thrift investments and met the QTL Test.

Savings and loan holding companies have historically not been subjected to consolidated regulatory capital requirements. The Dodd-Frank Act, however, required the Federal Reserve Board to promulgate consolidated capital requirements for bank and savings and loan holding companies that are no less stringent, both quantitatively and in terms of components of capital, than those applicable to their subsidiary depository institutions. Instruments such as cumulative preferred stock and trust-preferred securities, which are currently includable within Tier 1 capital, within certain limits by bank holding companies, would no longer be includable as Tier 1 capital, subject to certain grandfathering. The previously discussed final rule regarding regulatory capital requirements implements the Dodd-Frank Act's directives as to holding company capital requirements. Consolidated regulatory capital requirements identical to those applicable to the subsidiary depository institutions will apply to holding companies as of January 1, 2015. As is the case with institutions themselves, the capital conservation buffer will be phased in between 2016 and 2019. The Dodd-Frank Act also extended the source of strength doctrine, which has long applied to bank holding companies, to savings and loan holding companies as well. The Federal Reserve Board has promulgated 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 also applicable to savings and loan holding companies. 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 holding company to pay dividends may be restricted if a subsidiary depository institution becomes undercapitalized. In addition, a subsidiary institution of a saving and loan holding company must file prior notice with the Federal Reserve Board, and receive its nonobjection, before paying dividends to the parent savings and loan holding company. Federal Reserve Board guidance also provides for regulatory review of certain stock redemption and repurchase proposals. These regulatory policies could affect the ability of the Company to pay dividends, engage in stock redemptions or repurchases or otherwise engage in capital distributions.

As noted previously, the Bank may withdraw from the DIF and such withdrawal would trigger the Bank's conversion from a Massachusetts savings bank to a Massachusetts trust company charter. The charter conversion would cause the Company to become a bank holding company, rather than a savings and loan company, which requires the prior approval of the Federal Reserve Board. The Company contemplates that it would elect financial holding company status upon becoming a bank holding company in order to allow it to engage in a broader range of nonbanking activities. The most significant regulatory consequence of becoming a bank holding company is that the Federal Reserve Board's bank holding company consolidated regulatory capital requirements would become immediately applicable. The Company believes that it currently meets the bank holding company capital requirements and expects that becoming a bank holding company would not materially impact its business. With the Company as a bank holding company, rather than a savings and loan holding company, the Bank would no longer need to comply with the QTL Test.

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**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 depository institution 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 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 the Company 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. Any such legislation may impact the business of the Company and the Bank.

### **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 2013, 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 statutes and regulations applicable to depository institutions 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;

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- 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
- 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 depository institutions within their jurisdiction, the agencies evaluate the record of the depository 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 depository institutions from engaging in business with foreign shell banks; require depository 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 depository 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. The Company 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.

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**State**

The Company reports income on a calendar year basis to the Commonwealth of Massachusetts. The Massachusetts income tax rate for financial institutions was 9.0% in 2013 and 9.5% in 2012. 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.

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**

The risks set forth below, in addition to the other risks described in this Annual Report on Form 10-K, may adversely affect our business, financial condition and operating results. In addition to the risks set forth below and the other risks described in this annual report, there may also be additional risks and uncertainties that are not currently known to us or that we currently deem to be immaterial that could materially and adversely affect our business, financial condition or operating results. As a result, past financial performance may not be a reliable indicator of future performance, and historical trends should not be used to anticipate results or trends in future periods. Further, to the extent that any of the information contained in this Annual Report on Form 10-K constitutes forward-looking statements, the risk factors set forth below also are cautionary statements identifying important factors that could cause our actual results to differ materially from those expressed in any forward-looking statements made by or on behalf of us.

**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 markets generally exhibit low growth conditions and stubbornly high unemployment. Federal monetary policy continues to be unusually stimulative, which has distorted financial markets and contributed to ongoing low interest rates and record stock market prices. Federal policy gridlock, uncertainties about presidential initiatives, and state and local fiscal challenges contribute to business planning uncertainties. 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 recessionary lows. 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.

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***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 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 Related to Accounting for Acquired Loans May Differ From Actual Results.***

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. In 2013, the Company recorded significant income resulting from collections of acquired impaired loans which exceeded the fair value estimates originally established. Additionally, accounting for acquired loans involves ongoing assessments of the timing and amount of expected loan collections. Numerous



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assumptions and estimates are integral to purchased loan accounting, and actual results could be different from prior estimates.

***New regulations could restrict our ability to originate and sell mortgage loans.***

The CFPB has issued a rule designed to clarify for lenders how they can avoid monetary damages under the Dodd-Frank Act, which would hold lenders accountable for ensuring a borrower's ability to repay a mortgage. Loans that meet this qualified mortgage definition will be presumed to have complied with the new ability-to-repay standard. Under the CFPB's rule, a qualified mortgage loan must not contain certain specified features, including:

- excessive upfront points and fees (those exceeding 3% of the total loan amount, less bona fide discount points for prime loans);
- interest-only payments;
- negative-amortization; and
- terms longer than 30 years.

Also, to qualify as a qualified mortgage, a borrower's total debt-to-income ratio may not exceed 43%. Lenders must also verify and document the income and financial resources relied upon to qualify the borrower for the loan and underwrite the loan based on a fully amortizing payment schedule and maximum interest rate during the first five years, taking into account all applicable taxes, insurance and assessments. The CFPB's rule on qualified mortgages could limit our ability or desire to make certain types of loans or loans to certain borrowers, or could make it more expensive/and or time consuming to make these loans, which could limit our growth or profitability.

**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 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. In 2013, revenues decreased in the second half of the year due to changes related to loans and operations acquired in the prior two years.

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 negotiated the purchase of 20 branches in Central New York in 2013, and completed this acquisition shortly after year-end 2013. The amount of deposits acquired was significantly below the amount at the time of the purchase agreement. If there is continued attrition of deposit balances or difficulties in integrating the acquired operations, the expected benefits of this acquisition may not be realized.

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.

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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 and/or potential future expansion initiatives.

***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 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. Potential problems with the management of technology security and operational risks may affect regulatory compliance, which could affect operating costs and expansion plans.

***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. Our expanded mortgage lending and mortgage banking operations have also exposed us to more counterparty transactions including the use of third parties to participate in the management



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of interest rate risk and mortgage sales and hedging. Financial and operational risks are inherent in these counterparty relationships.

***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. As a result of recent revenue declines and expense restructuring activities, the Company could experience changes in the retention of existing employees.

***Management Changes Could Affect Operations.***

In 2013, there were changes in executive and senior management, including vacancy periods during times of transition. Existing senior managers were promoted to executive management positions with the expectation that there would be better focus on core competencies. Transitions in the management team introduce control risks in the oversight of operating activities and in the planning and execution of strategic objectives.

***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 Retail Lending Operations Expose Us to New Operating Risks.***

In 2012, the Bank acquired the business assets of an established residential mortgage origination company in Eastern Massachusetts. The acquired mortgage operations have been integrated and expanded in the Bank's footprint. Following record business volumes in 2012, mortgage business volumes contracted substantially in 2013 which affected mortgage banking profitability and necessitated a restructuring of expenses and operations.

The Bank acquired consumer lending operations with the Beacon Federal acquisition in the fourth quarter of 2012. The Bank has centralized its franchise consumer lending in these acquired Syracuse operations, including indirect automobile lending and home equity lending. The Company views these acquired consumer lending operations as a significant opportunity to expand its franchise consumer lending.

These changes expose us to operating risks. The conduct of these new activities also expose the Bank to the risk of loan losses, losses related to interest rate risk management, compliance, litigation, and other risks common in consumer lending operations.

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***Derivatives and Counterparty Risks Have Increased.***

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 when interest rates change suddenly and if the intended hedging objectives are not achieved as a result of market or counterparty behaviors. The sudden change in interest rates in 2013 contributed to lower mortgage banking profitability in 2013.

The Bank expanded its use of interest rate swaps in 2013 related to hedging its borrowings and providing commercial loan customers with fixed interest rate payment options. Following the completion of the New York branch acquisition shortly after year-end 2013, all outstanding interest rate swaps related to Federal Home Loan Bank loans were terminated and new borrowings and interest rate swaps were entered into based on an analysis of the current interest rate profile and objectives. These terminations in hedge management were due to changed circumstances and the Company's ability to utilize its hedge accounting methods depends on its ability to forecast related economic and financial factors which could limit its ability to utilize these methods in the event of future unforeseen events.

***The 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. Potential problems with new systems could involve regulatory compliance risk, potentially resulting in higher operating costs or limitations on operating activities. The new systems involve new costs with the new vendor, which could exceed expectations and impact profitability and future vendor relations.

**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. The

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Company's long term plan anticipates asset growth at a faster rate than deposit growth, which may result in increased reliance on wholesale or nontraditional funding sources. If deposits in new markets do not remain at planned levels, this could increase the possible reliance on wholesale or nontraditional funding sources.

***The Company Has Exceeded Certain Massachusetts Depositors Insurance Fund Size Thresholds, Which May Result In Changes to the Company and the Bank's Operations.***

Due to ongoing growth, the Company has exceeded certain Massachusetts Depositors Insurance Fund size thresholds and is evaluating its alternatives. Should Berkshire Bank determine to withdraw from participation in the Depositors Insurance Fund, the Bank would be required, under Massachusetts law, to convert from a Massachusetts savings bank to a Massachusetts trust company and, under federal law, the Company would be required to convert from a savings and loan holding company to a bank holding company. Such a charter conversion and holding company change would affect the overall powers and obligations of the Company and the Bank. The Bank is considering available alternatives to a charter conversion. None of these issues would affect the Bank's federal deposit insurance coverage by the FDIC and a potential withdrawal from the DIF supplemental insurance program would be expected to include a notice and transition time period for currently insured accounts. Withdrawal from DIF could have negative impact to future deposit acquisition or retention. The Company expects that any related charter changes, would be managed in an orderly manner without significant impact to business operations.

***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.

**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. The Company principally manages interest rate risk by managing its volume and mix of earning assets and funding liabilities. In a changing interest rate environment, the Company may not be able to manage this risk effectively. If the Company is unable to manage interest rate risk effectively, its business, financial condition and results of operations could be materially harmed. Changes in interest rates can also affect the demand for the Company's 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 the Company's ability to originate real estate loans, the value of its assets and its ability to realize gains from the sale of our assets, all of which ultimately affect our earnings. In 2013, factors related to market interest rates affected the retention of bank loans and mortgage banking revenues acquired in recent business

combinations.

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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. The Company concluded that, as of year-end 2013, any unrealized losses are temporary in nature, and it has the intent and ability to hold these investments for a time necessary to recover its 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 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. The Company has an investment in the stock of the Federal Home Loan Bank of Boston, which currently provides 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. At year-end 2013, the initial promulgation of a regulatory change known as the Volker Rule would have required the write-down of a pooled trust preferred security in the Bank's portfolio. This promulgation was modified, eliminating any potential accounting impacts for the Company. Future regulatory pronouncements could affect the securities portfolio and its carrying value.

**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.

The Company is 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. It may need to raise additional capital in the future to support 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 operations and the execution of the strategic plan, which includes further expanding operations through internal growth and acquisitions.

The Dodd-Frank Act made extensive changes in the regulation of insured depository institutions. 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.

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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 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.

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

In July 2013, 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 the adoption of new rules that revise and replace the agencies' capital rules as these federal agencies move forward with implementing capital requirements in response to agreements reached by the Basel Committee on Banking Supervision ( Basel III ). The Company is assessing the potential impact of these rules, including the impact on capital sources and capital returns.

***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.*

The level of interest and trading in the Company's 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 operating results; changes in interest rates; changes in the legal or regulatory environment; press releases, announcements or publicity relating to the Company or its competitors or relating to trends in its industry; changes in expectations as to 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 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.

**ITEM 1B. UNRESOLVED STAFF COMMENTS**

None.

**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 (Albany area), New York; Central New York; Northern Connecticut; and Central/Eastern Massachusetts. The Company has 92 full-service branches in Massachusetts, New York, Connecticut, and Vermont (including one branch in Tennessee held for sale following a bank acquisition).

The Company also has 7 regional headquarters. The 7 regional locations are full-service commercial offices located in Pittsfield, Massachusetts; Springfield, Massachusetts; Albany, New York; Syracuse, New York; Hartford, Connecticut; Westborough, Massachusetts; and Burlington, Massachusetts. In addition, the Company has 5 residential mortgage lending locations in Central/Eastern, Massachusetts.

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Berkshire Insurance Group operates from 12 locations in Western Massachusetts and Syracuse, New York in both standalone premises as well as in rented space located in the Bank's premises.

In January 2014, Berkshire completed the acquisition of 20 New York branches from Bank of America, reaching more communities between Albany and Syracuse. As part of the acquisition, two branches were consolidated in Central New York. Berkshire continues to look to consolidate to decrease operating expenses where appropriate and consolidated its commercial banking team into a new regional headquarters in Burlington, Massachusetts. The

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Company also opened a new office in Loudonville, New York in January 2014, as part of its ongoing organic expansion.

In 2013, the Company identified five branches that were consolidated as part of the Company's ongoing initiative to reduce operating costs and achieve greater efficiency following its acquisitions. These locations are in communities in and around the Company's existing footprint and were consolidated due to the proximity with other locations and other business strategies.

Berkshire continues to expand 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. Berkshire currently has 14 branches based on this design. In many cases, this branch design also includes a multimedia community room which is offered for use by nonprofit community groups.

**ITEM 3. LEGAL PROCEEDINGS**

At December 31, 2013, 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 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.

Table of Contents**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 sales price information and dividends declared per share of common stock in 2013 and 2012.

	High	Low	Dividends Declared
<b>2013</b>			
First quarter	\$ 26.01	\$ 23.38	\$ 0.18
Second quarter	27.84	24.62	0.18
Third quarter	29.38	24.34	0.18
Fourth quarter	27.86	24.50	0.18
<b>2012</b>			
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

 **Holders**

The Company had approximately 3,420 holders of record of common stock at March 7, 2014.

**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.

Table of Contents**Purchases of Equity Securities by the Issuer and Affiliated Purchases**

There were no purchases of equity securities during the fourth quarter of 2013 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 March 26, 2013, the Company authorized the purchase of up to 500 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 2013, there were 118 thousand shares that remain unpurchased under this plan.

Period	Total number of shares purchased	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, 2013		\$		118,113
November 1-30, 2013				118,113
December 1-31, 2013				118,113
Total		\$		118,113

**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 and the KBW Regional Bank 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, 2008.

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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Index	Period Ending					
	12/31/08	12/31/09	12/31/10	12/31/11	12/31/12	12/31/13
Berkshire Hills Bancorp, Inc.	100.00	69.00	76.22	78.89	87.46	102.79
NYSE Composite Index	100.00	124.80	138.34	129.88	146.66	180.65
PHLX KBW Regional Banking Index	100.00	75.78	89.58	83.19	91.89	132.00

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.

Table of Contents**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,				
	2013	2012	2011	2010	2009
<b>Selected Financial Data:</b>					
Total assets	\$ 5,672,799	\$ 5,296,809	\$ 3,992,257	\$ 2,882,298	\$ 2,700,991
Securities	870,091	573,871	533,181	405,953	420,966
Loans	4,180,523	3,988,654	2,956,570	2,142,162	1,961,658
Allowance for loan losses	(33,323)	(33,208)	(32,444)	(31,898)	(31,816)
Goodwill and intangibles	270,662	274,258	223,364	173,079	176,100
Deposits	3,848,529	4,100,409	3,101,175	2,204,441	1,986,762
Borrowings and subordinated notes	1,064,107	448,088	237,402	260,301	306,668
Total stockholders equity	678,062	667,265	551,808	387,323	385,148
<b>Selected Operating Data:</b>					
Total interest and dividend income	\$ 203,741	\$ 175,939	\$ 138,260	\$ 112,277	\$ 115,476
Total interest expense	34,989	32,551	31,740	35,330	45,880
Net interest income	168,752	143,388	106,520	76,947	69,596
Service charges and fee income	50,525	51,265	33,727	29,859	28,181
All other non-interest income (loss)	7,707	2,791	2,076	(108)	(3,004)
Total net revenue	226,984	197,444	142,323	106,698	94,773
Provision for loan losses	11,378	9,590	7,563	8,526	47,730
Total non-interest expense	157,359	140,806	116,442	82,137	78,571
Income tax expense (benefit) - continuing operations	17,104	13,223	1,884	2,420	(15,597)
Net (loss) income from discontinued operations		(637)	914		
Net income (loss)	\$ 41,143	\$ 33,188	\$ 17,348	\$ 13,615	\$ (15,931)
Less: Cumulative preferred stock dividend and accretion					1,030
Less: Deemed dividend from preferred stock repayment					2,954
<b>Net income (loss) available to common stockholders</b>	\$ 41,143	\$ 33,188	\$ 17,348	\$ 13,615	\$ (19,915)
Dividends per common share	\$ 0.72	\$ 0.69	\$ 0.65	\$ 0.64	\$ 0.64
Basic earnings per common share	1.66	1.49	0.97	0.98	(1.51)
Diluted earnings per common share	1.65	1.49	0.97	0.98	(1.51)
Weighted average common shares outstanding - basic	24,802	22,201	17,885	13,862	13,189
Weighted average common shares outstanding - diluted	24,965	22,329	17,952	13,896	13,189

(1) For the years 2011 and 2010, the above schedule has been adjusted for prior year lease adjustments.



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	At or For the Years Ended December 31,				
	2013	2012	2011	2010	2009
<b>Selected Operating Ratios and Other Data:</b>					
<i>Share Data:</i>					
Book value per share	\$ 27.08	\$ 26.53	\$ 26.09	\$ 27.52	\$ 27.68
Market price at year end	\$ 27.27	\$ 23.86	\$ 22.19	\$ 22.11	\$ 20.68
<i>Performance Ratios:</i>					
Return on average assets	0.78%	0.73%	0.50%	0.50%	(0.74)%
Return on average equity	6.09	5.66	3.64	3.55	4.83
Interest rate spread	3.47	3.47	3.38	3.01	2.61
Net interest margin	3.63	3.62	3.57	3.28	3.00
Non-interest income/total net revenue	25.65	27.38	27.16	27.88	26.57
Non-interest expense/average assets	2.97	3.11	3.34	2.99	2.93
Dividend payout ratio	41.57	46.31	67.01	65.16	N/M
<i>Growth Ratios:</i>					
Total loans	4.81	34.91	38.02	9.20	(2.27)
Total deposits	(6.14)	32.22	40.68	10.96	8.59
Total net revenues	14.96	38.73	33.39	12.58	(8.15)
<i>Asset Quality Ratios:</i>					
Net loans charged-off/average total loans	0.29	0.26	0.27	0.42	1.96
Allowance for loan losses/total loans	0.80	0.83	1.10	1.49	1.62
Net loans charged-off - Business activities/average total loans- Business activities	0.24	0.34	0.32	0.42	1.96
Allowance for loan losses - Business activities/total loans - Business Activities	0.93	1.21	1.41	1.49	1.62
<i>Capital Ratios:</i>					
Tier 1 capital to average assets - bank	7.99	7.46	8.41	8.04	7.86
Total capital to risk-weighted assets - bank	11.62	11.79	11.29	10.61	10.71
Stockholders equity/total assets	11.95	12.60			