BERKSHIRE HILLS BANCORP INC
Form 10-Q
August 09, 2016
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended: June 30, 2016

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: 001-15781

BERKSHIRE HILLS BANCORP, INC.
(Exact name of registrant as specified in its charter)

Delaware	04-3510455
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
24 North Street, Pittsfield, Massachusetts	01201
(Address of principal executive offices)	(Zip Code)

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

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 ý No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý No o

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

Large Accelerated Filer ý Accelerated Filer o Non-Accelerated Filer o Smaller Reporting Company o

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

The Registrant had 31,139,213 shares of common stock, par value $0.01 per share, outstanding as of August 4, 2016.

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PART I
ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

BERKSHIRE HILLS BANCORP, INC.
CONSOLIDATED BALANCE SHEETS

(In thousands, except share data)	June 30, 2016	December 31, 2015
Assets		
Cash and due from banks	$58,332	$72,918
Short-term investments	16,247	30,644
Total cash and cash equivalents	74,579	103,562
Trading security, at fair value	14,479	14,189
Securities available for sale, at fair value	1,073,370	1,154,457
Securities held to maturity (fair values of $141,544 and $136,904)	132,010	131,652
Federal Home Loan Bank stock and other restricted securities	68,242	71,018
Total securities	1,288,101	1,371,316
Loans held for sale	22,450	13,191
Commercial real estate	2,237,582	2,059,767
Commercial and industrial loans	1,034,559	1,048,263
Residential mortgages	1,843,600	1,815,035
Consumer loans	884,560	802,171
Total loans	6,000,301	5,725,236
Less: Allowance for loan losses	(41,397)	(39,308)
Net loans	5,958,904	5,685,928
Premises and equipment, net	86,274	88,072
Other real estate owned	595	1,725
Goodwill	339,929	323,943
Other intangible assets	9,057	10,664
Cash surrender value of bank-owned life insurance policies	127,000	125,233
Deferred tax assets, net	32,945	42,526
Other assets	103,825	64,926
Total assets	$8,043,659	$7,831,086
Liabilities		
Demand deposits	$1,050,220	$1,081,860
NOW deposits	489,734	510,807
Money market deposits	1,415,041	1,408,107
Savings deposits	611,627	601,761
Time deposits	2,090,102	1,986,600
Total deposits	5,656,724	5,589,135
Short-term debt	1,110,320	1,071,200
Long-term Federal Home Loan Bank advances	120,844	103,135
Subordinated borrowings	89,072	88,983
Total borrowings	1,320,236	1,263,318
Other liabilities	143,279	91,444
Total liabilities	$7,120,239	$6,943,897

(continued)

Shareholders' equity		
Common stock ($.01 par value; 50,000,000 shares authorized and 32,321,962 shares issued and 31,156,292 shares outstanding in 2016; 32,321,962 shares issued and 30,973,986 shares outstanding in 2015)	322	322
Additional paid-in capital	744,810	742,619
Unearned compensation	(8,798)	(6,997)
Retained earnings	203,382	183,885
Accumulated other comprehensive income	10,213	(3,305)
Treasury stock, at cost (1,056,739 shares in 2016 and 1,179,045 shares in 2015)	(26,509)	(29,335)
Total Shareholders' equity	923,420	887,189
Total liabilities and Shareholders' equity	$ 8,043,659	$ 7,831,086

The accompanying notes are an integral part of these consolidated financial statements.

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BERKSHIRE HILLS BANCORP, INC.
CONSOLIDATED STATEMENTS OF INCOME

(In thousands, except per share data)	Three Months Ended June 30, 2016	2015	Six Months Ended June 30, 2016	2015
Interest and dividend income				
Loans	$59,703	$51,504	$118,145	$95,949
Securities and other	9,315	8,899	19,349	17,205
Total interest and dividend income	69,018	60,403	137,494	113,154
Interest expense				
Deposits	7,378	5,292	14,537	10,241
Borrowings	4,199	2,474	7,819	4,783
Total interest expense	11,577	7,766	22,356	15,024
Net interest income	57,441	52,637	115,138	98,130
Non-interest income				
Loan related income	2,898	2,783	5,944	4,066
Mortgage banking income	1,335	1,546	2,156	2,799
Deposit related fees	6,291	6,442	12,400	12,119
Insurance commissions and fees	2,660	2,486	5,553	5,453
Wealth management fees	2,235	2,397	4,737	5,000
Total fee income	15,419	15,654	30,790	29,437
Other	(851)	(1,258)	(628)	(2,513)
(Loss) gain on sale of securities, net	(13)	2,384	23	2,418
Total non-interest income	14,555	16,780	30,185	29,342
Total net revenue	71,996	69,417	145,323	127,472
Provision for loan losses	4,522	4,204	8,528	8,055
Non-interest expense				
Compensation and benefits	24,664	24,503	50,378	46,314
Occupancy and equipment	6,560	7,243	13,250	14,351
Technology and communications	4,814	4,090	9,671	7,683
Marketing and promotion	737	800	1,410	1,513
Professional services	1,509	1,375	2,789	2,647
FDIC premiums and assessments	1,203	1,143	2,436	2,272
Other real estate owned and foreclosures	393	251	656	502
Amortization of intangible assets	787	934	1,606	1,835
Acquisition, restructuring and conversion related expenses	878	8,711	1,658	13,132
Other	4,723	4,975	9,514	8,924
Total non-interest expense	46,268	54,025	93,368	99,173
Income before income taxes	21,206	11,188	43,427	20,244
Income tax expense	5,249	1,144	11,469	1,441
Net income	$15,957	$10,044	$31,958	$18,803
Earnings per share:				
Basic	$0.52	$0.35	$1.05	$0.71
Diluted	$0.52	$0.35	$1.04	$0.70
Weighted average common shares outstanding:				

Basic	30,605	28,301	30,561	26,557
Diluted	30,765	28,461	30,725	26,713

The accompanying notes are an integral part of these consolidated financial statements.

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BERKSHIRE HILLS BANCORP, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Three Months Ended June 30,		Six Months Ended June 30,	
(In thousands)	2016	2015	2016	2015
Net income	$15,957	$10,044	$31,958	$18,803
Other comprehensive income, before tax:				
Changes in unrealized gain on securities available-for-sale	9,586	(16,071)	27,293	(6,734)
Changes in unrealized loss on derivative hedges	(884)	784	(5,390)	(3,117)
Changes in unrealized loss on pension	—	65	—	(1,466)
Income taxes related to other comprehensive income:				
Changes in unrealized gain on securities available-for-sale	(3,691)	6,100	(10,548)	2,495
Changes in unrealized loss on derivative hedges	355	(316)	2,163	1,256
Changes in unrealized loss on pension	—	(26)	—	591
Total other comprehensive income (loss)	5,366	(9,464)	13,518	(6,975)
Total comprehensive income	$21,323	$580	$45,476	$11,828

The accompanying notes are an integral part of these consolidated financial statements.

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BERKSHIRE HILLS BANCORP, INC.
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

(In thousands)	Common stock Shares	Common stock Amount	Additional paid-in capital	Unearned compensation	Retained earnings	Accumulated other comprehensive (loss) income	Treasury stock	Total
Balance at December 31, 2014	25,183	$ 265	$585,289	$ (6,147)	$156,446	$ 6,579	$(33,145)	$709,287
Comprehensive income:								
Net income	—	—	—	—	18,803	—	—	18,803
Other comprehensive loss	—	—	—	—	—	(6,975)	—	(6,975)
Total comprehensive income								11,828
Acquisition of Hampden Bancorp, Inc	4,186	42	114,562	—	—	—	—	114,604
Cash dividends declared ($0.38 per share)	—	—	—	—	(10,440)	—	—	(10,440)
Treasury stock purchased	—	—	—	—	—	—	—	—
Forfeited shares	(11)	—	28	254	—	—	(282)	—
Exercise of stock options	11	—	—	—	(165)	—	281	116
Restricted stock grants	174	—	283	(4,579)	—	—	4,296	—
Stock-based compensation	—	—	—	2,252	—	—	—	2,252
Net tax benefit related to stock-based compensation	—	—	26	—	—	—	—	26
Other, net	(22)	—	5	—	—	—	(527)	(522)
Balance at June 30, 2015	29,521	$ 307	$700,193	$ (8,220)	$164,644	$ (396)	$(29,377)	$827,151
Balance at December 31, 2015	30,974	$ 322	$742,619	$ (6,997)	$183,885	$ (3,305)	$(29,335)	$887,189
Comprehensive income:								
Net income	—	—	—	—	31,958	—	—	31,958
Other comprehensive income	—	—	—	—	—	13,518	—	13,518
Total comprehensive income								45,476
Acquisition of 44 Business Capital	45	—	—	—	—	—	1,217	1,217
Cash dividends declared ($0.40 per share)	—	—	—	—	(12,442)	—	—	(12,442)
Treasury stock adjustment (2)	—	—	1,645	—	—	—	(1,645)	—
Forfeited shares	(22)	—	68	526	—	—	(594)	—
Exercise of stock options	2	—	—	—	(19)	—	55	36
Restricted stock grants	180	—	496	(4,923)	—	—	4,427	—
Stock-based compensation	—	—	—	2,596	—	—	—	2,596
	—	—	(1)	—	—	—	—	(1)

Net tax benefit related to stock-based compensation								
Other, net	(23)	—	(17)	—	—	—	(634)	(651)
June 30, 2016 (1)	31,156	$ 322	$744,810	$ (8,798)	$203,382	$ 10,213	$(26,509)	$923,420

(1) The Company's common stock includes the elimination of $2.9 million (108,931 shares) of Berkshire Hills Bancorp stock held by a subsidiary.
(2) Treasury stock adjustment represents the sale of 60,000 shares of Berkshire Hills Bancorp stock held by the Company's subsidiary.

The accompanying notes are an integral part of these consolidated financial statements.

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BERKSHIRE HILLS BANCORP, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)	Six Months Ended June 30, 2016	2015
Cash flows from operating activities:		
Net income	$ 31,958	$ 18,803
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	8,528	8,055
Net amortization of securities	2,003	863
Change in unamortized net loan costs and premiums	(3,268)	836
Premises and equipment depreciation and amortization expense	4,237	4,282
Stock-based compensation expense	2,596	2,252
Accretion of purchase accounting entries, net	(4,801)	(3,071)
Amortization of other intangibles	1,606	1,835
Write down of other real estate owned	365	75
Excess tax loss from stock-based payment arrangements	(105)	(26)
Income from cash surrender value of bank-owned life insurance policies	(2,025)	(1,535)
Gain on sales of securities, net	(23)	(2,418)
Net (increase) in loans held for sale	(9,259)	(28,102)
Loss on disposition of assets	15	2,084
Loss on sale of real estate	57	400
Amortization of interest in	2,929	5,748

tax-advantaged projects		
Net change in other	(5,134)	(8,384)
Net cash provided by operating activities	29,679	1,697
Cash flows from investing activities:		
Net decrease in trading security	296	282
Proceeds from sales of securities available for sale	187,519	22,504
Proceeds from maturities, calls and prepayments of securities available for sale	83,883	94,561
Purchases of securities available for sale	(164,943)	(174,992)
Proceeds from maturities, calls and prepayments of securities held to maturity	4,288	1,875
Purchases of securities held to maturity	(4,786)	(45,520)
Net change in loans	(250,002)	(126,806)
Proceeds from surrender of bank-owned life insurance	258	431
Proceeds from sale of Federal Home Loan Bank stock	11,578	163
Purchase of Federal Home Loan Bank stock	(8,803)	(10,706)
Net investment in limited partnership tax credits	(4,122)	(2,500)
Proceeds from the sale of premises and equipment	226	541
Purchase of premises and equipment, net	(2,839)	(3,070)
Acquisitions, net of cash (paid) acquired	(55,542)	83,134
Proceeds from sale of other real estate	933	1,476
	(202,056)	(158,627)

Net cash used in
investing activities
(continued)

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	Six Months Ended June 30,	
(In thousands)	2016	2015
Cash flows from financing activities:		
Net increase (decrease) in deposits	98,604	206,354
Proceeds from Federal Home Loan Bank advances and other borrowings	4,449,120	3,896,000
Repayments of Federal Home Loan Bank advances and other borrowings	(4,391,925)	(3,801,362)
Exercise of stock options	37	116
Excess tax loss from stock-based payment arrangements	—	26
Common stock cash dividends paid	(12,442)	(10,440)
Net cash provided by financing activities	143,394	290,694
Net change in cash and cash equivalents	(28,983)	133,764
Cash and cash equivalents at beginning of year	103,562	71,754
Cash and cash equivalents at end of year	$74,579	$205,518
Supplemental cash flow information:		
Interest paid on deposits	$14,573	$10,290
Interest paid on borrowed funds	7,497	4,555
Income taxes paid, net	7,278	324
Acquisition of non-cash assets and liabilities:		
Assets acquired	56,976	730,868
Liabilities assumed	(108)	(611,601)
Other non-cash changes:		
Other net comprehensive income	13,518	(6,975)
Real estate owned acquired in settlement of loans	225	460

The accompanying notes are an integral part of these consolidated financial statements.

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NOTE 1. BASIS OF PRESENTATION

The consolidated financial statements (the “financial statements”) of Berkshire Hills Bancorp, Inc. and its subsidiaries (the “Company” or “Berkshire”) have been prepared in conformity with accounting principles generally accepted in the United States of America (“GAAP”). The Company is a Delaware corporation and the holding company for Berkshire Bank (the “Bank”), a Massachusetts-chartered trust company headquartered in Pittsfield, Massachusetts, and Berkshire Insurance Group, Inc. (“Berkshire Insurance Group” or “BIG”). These financial statements include the accounts of the Company, its wholly-owned subsidiaries and the Bank’s consolidated subsidiaries. In consolidation, all significant intercompany accounts and transactions are eliminated. The results of operations of companies or assets acquired are included only from the dates of acquisition. All material wholly-owned and majority-owned subsidiaries are consolidated unless GAAP requires otherwise.

In addition, these interim financial statements have been prepared in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X, and accordingly, certain information and footnote disclosures normally included in financial statements prepared according to U.S. GAAP have been omitted.

The results for any interim period are not necessarily indicative of results for the full year. These consolidated financial statements should be read in conjunction with the audited financial statements and note disclosures for Berkshire Hills Bancorp, Inc. (the “Company”) previously filed with the Securities and Exchange Commission in the Company’s Annual Report on Form 10-K for the year ended December 31, 2015. In management's opinion, all adjustments necessary for a fair statement are reflected in the interim periods presented.

Recently Adopted Accounting Principles
Effective January 1, 2016, the following new accounting guidance was adopted by the Company:
- ASU No. 2015-02, Consolidation (Topic 810) - Amendments to the Consolidation Analysis;
- ASU No. 2015-03, Interest-Imputation of Interest (Subtopic 835-30) - Simplifying the Presentation of Debt Issuance Costs;
- ASU No. 2015-05, Intangibles-Goodwill and Other-Internal-Use Software (Subtopic 350-40): Customer’s Accounting for Fees Paid in a Cloud Computing Arrangement; and
- ASU No. 2015-16, Business Combinations (Topic 805) - Simplifying the Accounting for Measurement - Period Adjustments.

The adoption of these accounting standards did not have a material impact on the Company's financial statements.

In March 2016, the FASB issued ASU No. 2016-09, “Improvement to Employee Share-Based Payment Accounting”. This ASU contains targeted amendments to the accounting for shared based payment transactions, including income tax consequences for awards, classification of awards as either equity or liabilities, and classification of activity on the statement of cash flows. Specifically, some of the requirements under the amendments include: (1) excess tax benefits and/or tax deficiencies, determined as the difference between compensation cost recognized for financial reporting purposes and the deduction for tax, be recognized in the income statement as income tax expense or benefit in the period in which they occur, removing historical equity treatment; (2) excess tax benefits are no longer separately classified as a financing activity but rather should be classified with other income tax cash flows as an operating activity on the statement of cash flows; (3) cash paid by an employer when withholding shares for tax withholding purposes should be classified as a financing activity. Additionally, regarding forfeitures, this guidance permits a company to make an entity-wide accounting policy election to either estimate the number of awards that are expected to vest (current GAAP) or account for forfeitures when they occur. ASU No. 2016-09 is effective for annual periods beginning after December 15, 2016. The Company adopted ASU No. 2016-09 in April 2016 and the adoption of this accounting standard did not have a material impact on the Company's consolidated financial statements. The

Company chose a modified retrospective approach and a policy election to account for forfeitures when they occur. This change resulted in a cumulative adjustment immaterial to all periods presented.

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Future Application of Accounting Pronouncements

In May 2014, the FASB issued ASU No. 2014-09 related to the recognition of revenue from contracts with customers. The new revenue pronouncement creates a single source of revenue guidance for all companies in all industries and is more principles based than current revenue guidance. The pronouncement provides a five-step model for a company to recognize revenue when it transfers control of goods or services to customers at an amount that reflects the consideration to which it expects to be entitled in exchange for those goods or services. The five steps are (1) identify the contract with the customer, (2) identify the separate performance obligations in the contract, (3) determine the transaction price, (4) allocate the transaction price to the separate performance obligations and (5) recognize revenue when each performance obligation is satisfied. The standard is effective for public entities for interim and annual reporting periods beginning after December 15, 2016; early adoption is not permitted. However, in August 2015, Accounting Standards Update No. 2015-14, “Deferral of the Effective Date” (“ASU 2015-14”) was issued and delayed the effective date of ASU 2014-09 to annual and interim periods in fiscal years beginning after December 15, 2017. Early adoption is permitted, but not before the original effective date (i.e., interim and annual reporting periods beginning after December 15, 2016). For financial reporting purposes, the standard allows for either full retrospective adoption, meaning the standard is applied to all of the periods presented, or modified retrospective adoption, meaning the standard is applied only to the most current period presented in the financial statements with the cumulative effect of initially applying the standard recognized at the date of initial application.

In March, April and May 2016, the FASB issued ASU No. 2016-08, “Principal versus Agent Considerations,” ASU No. 2016-10, “Identifying Performance Obligations and Licensing,” and ASU 2016-12, “Narrow-Scope Improvements and Practical Expedients,” respectfully. The updates are not intended to change the core principles of the standard; however, they attempt to clarify important aspects of the guidance and improve its operability. The amendments have the same effective date and transition requirements as the new revenue standard. The Company is currently evaluating the provisions of ASU No. 2014-09, and will be closely monitoring developments and additional guidance to determine the potential impact the new standard will have on the Company's consolidated financial statements.

In January 2016, the FASB issued ASU No. 2016-01, “Recognition and Measurement of Financial Assets and Financial Liabilities.” This ASU requires an entity to: i) measure equity investments at fair value through net income, with certain exceptions; (ii) present in other comprehensive income the changes in instrument-specific credit risk for financial liabilities measured using the fair value option; (iii) present financial assets and financial liabilities by measurement category and form of financial asset; (iv) calculate the fair value of financial instruments for disclosure purposes based on an exit price and; (v) assess a valuation allowance on deferred tax assets related to unrealized losses of AFS debt securities in combination with other deferred tax assets. The guidance provides an election to subsequently measure certain nonmarketable equity investments at cost less any impairment and adjusted for certain observable price changes. The guidance also requires a qualitative impairment assessment of such equity investments and amends certain fair value disclosure requirements. The guidance is effective for annual periods beginning after December 15, 2017. Early adoption is only permitted for the provision related to instrument specific credit risk. The Company is currently evaluating the impact of the new standard on the Company's consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, “Leases”. The new pronouncement improves the transparency and comparability of financial reporting around leasing transactions and more closely aligns accounting for leases with the recently issued International Financial Reporting Standard. The pronouncement affects all entities that are participants to leasing agreements. From a lessee accounting perspective, the ASU requires a lessee to recognize assets and liabilities on the balance sheet for operating leases and changes many key definitions, including the definition of a lease. The ASU includes a short-term lease exception for leases with a term of twelve months or less, in which a lessee can make an accounting policy election not to recognize lease assets and lease liabilities. Lessees will continue to differentiate between finance leases (previously referred to as capital leases) and operating leases, using classification criteria that are substantially similar to the previous guidance. For lessees, the recognition, measurement, and presentation of expenses and cash flows arising from a lease have not significantly changed from previous GAAP.

From a lessor accounting perspective, the guidance is largely unchanged, except for targeted improvements to align with new terminology under lessee accounting and with the

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updated revenue recognition guidance in Topic 606. For sale-leaseback transactions, for a sale to occur the transfer must meet the sale criteria under the new revenue standard, ASC 606. Entities will not be required to reassess transactions previously accounted under then existing guidance.

Additionally, the ASU includes additional quantitative and qualitative disclosures required by lessees and lessors to help users better understand the amount, timing, and uncertainty of cash flows arising from leases. ASU No. 2016-02 is effective for fiscal years beginning after December 31, 2018, and interim periods within those fiscal years. Lessees and lessors are required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach. The modified retrospective approach includes a number of optional practical expedients that entities may elect to apply as well as transition guidance specific to nonstandard leasing transactions. The Company is currently evaluating the provision of the ASU No. 2016-02 to determine the potential impact the new standard will have on the the Company's consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-05, "Effect of Derivative Contract Novations on Existing Hedge Accounting Relationships". This ASU clarifies that changes in the counterparty to a derivative instrument designated as a hedge do not alone require it to be de-designated and therefore discontinue the application of hedge accounting. Companies are still required to evaluate whether it is probable that a counterparty will perform under the contract as part of the ongoing effectiveness assessment for hedge accounting. The new guidance is effective for annual periods beginning after December 15, 2016 and entities may adopt on a prospective or modified retrospective basis. The adoption of this pronouncement is not expected to have a material impact on the Company's consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-06, "Contingent Put and Call Options in Debt Instruments" clarifying the assessment of whether contingent call (put) options that can accelerate the payment of principal on debt instruments are clearly and closely related to the economic characteristics and risks of their debt hosts, a criteria in assessing whether to bifurcate an embedded derivative. The new pronouncement clarifies the exercise contingency and the event triggering the contingency does not need to be evaluated in the clearly and closely analysis relative to interest rates or credit risks. Rather, the call or put would be evaluated as a derivative regardless of the exercise contingency. Further, if an entity is no longer required to bifurcate a put or call option per the new guidance, the entity has a one-time option to irrevocably elect to measure that debt instrument in its entirety at fair value with changes in fair value recognized in earnings. ASU No. 2016-06 is effective for annual periods beginning after December 15, 2016 and early adoption is permitted. The ASU should be applied using the modified retrospective basis to existing instruments as of the beginning of the annual period of adoption. The adoption of this pronouncement is not expected to have a material impact on the Company's consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-07 "Simplifying the Transition to the Equity Method of Accounting" which eliminates the requirement to retroactively adjust an investment that becomes subject to the equity method of accounting as a result of an increase ownership interest or degree of influence. Alternatively, an investor entity adds the cost of acquiring the additional interest in the investee to the current basis of the investor's previously held interest and adopts the equity method of accounting prospectively as of the qualifying date; no retroactive adjustment is required. Additionally, ASU No. 2016-07 specifies that when an available-for-sale equity security becomes qualified for the equity method of accounting, a company should recognize the unrealized holding gain or loss in accumulated other comprehensive income through earnings at the date the investment becomes qualified for use of the equity method. This guidance is effective for all entities for annual periods beginning after December 15, 2016, with early adoption permitted on a prospective basis. The adoption of this pronouncement is not expected to have a material impact on the Company's consolidated financial statements.

In June 2016, the FASB issued ASU No. 2016-13, "Measurement of Credit Losses on Financial Instruments." This ASU improves financial reporting by requiring timelier recording of credit losses on loans and other financial instruments.

The ASU requires companies to measure all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Forward-looking information will now be used in credit loss estimates. The ASU requires enhanced disclosures to provide better understanding surrounding significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of a company’s portfolio. These disclosures include qualitative

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and quantitative requirements that provide additional information about the amounts recorded in the financial statements. Additionally, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. Most debt instruments will require a cumulative-effect adjustment to retained earnings on the statement of financial position as of the beginning of the first reporting period in which the guidance is adopted (modified retrospective approach). However, there is instrument-specific transition guidance. ASU No. 2016-13 is effective for interim and annual periods beginning after December 15, 2019. Early application will be permitted for interim and annual periods beginning after December 15, 2018. The Company is evaluating the provisions of ASU No. 2016-13, and will closely monitor developments and additional guidance to determine the potential impact on the Company's consolidated financial statements.

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NOTE 2. ACQUISITION

44 Business Capital

On April 29, 2016, the Company acquired and assumed the business model, certain assets, and certain liabilities of 44 Business Capital, along with certain loans and other assets of Parke Bank's ("Parke") SBA 7(a) loan program operations. 44 Business Capital was a joint venture of Parke (51%) and a management group (49%), 44 Amigos LLC, located in Blue Bell, Pennsylvania. 44 Business Capital was engaged in originating, servicing, and selling SBA loans using Parke's SBA PLP preferred lender license.

The transaction includes acquiring assets, key people, systems, and processes necessary for a market participant to run operations as a business. In accordance with ASC 805-10-55, the transaction was recorded as a business combination, resulting in acquisition accounting in which all assets are acquired and liabilities are assumed at fair value.

The loans acquired by the Company were the unguaranteed portions of SBA loans of which $35.6 million were recorded as commercial real estate and $1.2 million were recorded as commercial & industrial. Servicing rights on a notional loan balance of $148 million were also acquired. The Company expects the acquisition to expand its SBA lending program on a super-regional and national basis with the intent of selling many of these loans on the secondary market. Additionally, the acquisition of 44 Business Capital expands the Company's product lines, creates cross-selling opportunities, and adds niche lending to its portfolio. 44 Business Capital will operate as a direct small business lending division reporting up through the Company's established small business department.

The following table provides a summary of the assets acquired and liabilities assumed and the associated fair value adjustments as recorded by the Company at acquisition:

(in thousands)	As Acquired	Fair Value Adjustments		As Recorded at Acquisition
Consideration paid:				
Company common stock issued to certain 44 Business Capital shareholders (44,840 shares)				$ 1,217
Cash paid to 44 Business Capital shareholders and Parke				55,649
Total consideration paid				$ 56,866
Recognized amounts of identifiable assets acquired and liabilities assumed, at fair value:				
Cash and short-term investments	$ 107	$ —		$ 107
Loans	42,627	(5,777)	(a)	36,850
Premises and equipment	69	(36)	(b)	$ 33
Other assets	3,076	639	(c)	3,715
Other liabilities	(108)	—		$ (108)
Total identifiable net assets	$ 45,771	$ (5,174)		$ 40,597
Goodwill				$ 16,269

Explanation of Certain Fair Value Adjustments

(a) The adjustment represents the write down of the book value of loans to their estimated fair value based on current interest rates and expected cash flows, which includes an estimate of expected loan loss inherent in the portfolio. Loans that met the criteria and are being accounted for in accordance with ASC 310-30 had a book value of $6.3 million and have a fair value $2.6 million. Non-impaired loans accounted for under ASC 310-10 had a book value of $36.4 million and have a fair value of $34.3 million. ASC 310-30 loans have a $708 thousand fair value adjustment discount that is accretable in earnings over an average estimated six-year life using the effective yield as determined on the date of acquisition. The effective yield is periodically adjusted for changes in expected flows.

ASC 310-10 loans have a $2.1 million fair value adjustment discount that is amortized into income over the remaining term of the loans using the effective interest method.

(b) The fair value of the equipment was assumed to approximate the net carrying value based on overall condition and age. The adjustment represents the immediate expensing of equipment not meeting the thresholds for

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capitalization in accordance with Company policy. The recorded amount will be depreciated over the remaining estimated economic lives of the assets.

(c) The adjustment represents the fair value write up of book value of the loan servicing right asset to its estimated fair value based on current interest rates and expected cash flows, which includes an estimate of cost of service and conditional prepayment rates applied to the underlying unpaid loan pool balance over the remaining life of the loans. The balance includes accrued interest of $221 thousand.

The fair values for loans acquired were estimated using cash flow projections based on the remaining maturity and repricing terms. Cash flows were adjusted by estimating future credit losses and the rate of prepayments. Projected monthly cash flows were then discounted to present value using a risk-adjusted market rate for similar loans. There was no carryover of the seller's allowance for credit losses associated with the loans that were acquired in the acquisition as the loans were initially recorded at fair value.

Information about the acquired loan portfolio subject to ASC 310-30 as of April 29, 2016 is, as follows (in thousands):

	ASC 310-30 Loans
Gross contractual receivable amounts at acquisition	$6,265
Contractual cash flows not expected to be collected (nonaccretable discount)	(3,000)
Expected cash flows at acquisition	3,265
Interest component of expected cash flows (accretable discount)	(708)
Fair value of acquired loans	$2,557

Goodwill capitalized, which is not amortized for book purposes, was assigned to the Company's banking reporting unit and is not deductible for tax purposes.

Direct acquisition and integration costs of the 44 Business Capital acquisition were expensed as incurred, and totaled $115 thousand during the six months ending June 30, 2016 and there were none for the same period of 2015. These costs totaled $21 thousand for the three months ended June 30, 2016 and there were none for the same period of 2015.

Pro Forma Information (unaudited)

The following table presents selected unaudited pro forma financial information reflecting the acquisition of 44 Business Capital assuming the acquisition was completed as of January 1, 2015. The unaudited pro forma financial information includes adjustments for scheduled amortization and accretion of fair value adjustments recorded at the acquisitions. These adjustments would have been different if they had been recorded on January 1, 2015, and they do not include the impact of prepayments. The unaudited pro forma financial information is presented for illustrative purposes only and is not necessarily indicative of the combined financial results of the Company and 44 Business Capital had the transaction actually been completed at the beginning of the periods presented, nor does it indicate future results for any other interim or full-year period. Pro forma basic and diluted earnings per common share were calculated using Berkshire's actual weighted-average shares outstanding for the periods presented plus the 45 thousand shares issued as a result of the 44 Business Capital acquisition. The unaudited pro forma information is based on the actual financial statements of Berkshire and 44 Business Capital for the periods shown until the date of acquisition, at which time 44 Business Capital operations became included in Berkshire's financial statements. For the period from the date of acquisition through June 30, 2016, 44 Business Capital's net revenue was $841 thousand and net income was $59 thousand.

The unaudited pro forma information, for the six months ended June 30, 2016 and 2015, set forth below reflects adjustments related to amortization and accretion of purchase accounting fair value adjustments and an estimated tax rate of 40 percent. Direct acquisition expenses incurred by the Company during 2016, as noted above, are reversed for the purposes of this unaudited pro forma information. The unaudited pro forma information does not include interest income from the unguaranteed portion of acquired loans. Furthermore, the unaudited pro forma

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information does not reflect management's estimate of any revenue-enhancing or anticipated cost-savings that could occur after June 30, 2016.

Information in the following table is shown in thousands, except earnings per share:

	Pro Forma (unaudited)	
	Six Months Ended June 30,	
	2016	2015
Net interest income	$115,269	$98,417
Non-interest income	32,338	31,650
Net income	32,652	19,417
Pro forma earnings per share:		
Basic	$1.07	$0.73
Diluted	$1.06	$0.73

NOTE 3. TRADING SECURITY

The Company holds a tax advantaged economic development bond accounted for at fair value. The security had an amortized cost of $11.7 million and $12.0 million, and a fair value of $14.5 million and $14.2 million, at June 30, 2016 and December 31, 2015, respectively. As discussed further in Note 13 - Derivative Financial Instruments and Hedging Activities, the Company has entered into a swap contract to swap-out the fixed rate of the security in exchange for a variable rate. The Company does not purchase securities with the intent of selling them in the near term, and there are no other securities in the trading portfolio at June 30, 2016.

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NOTE 4. SECURITIES AVAILABLE FOR SALE AND HELD TO MATURITY

The following is a summary of securities available for sale and held to maturity:

(In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
June 30, 2016				
Securities available for sale				
Debt securities:				
Municipal bonds and obligations	$ 103,645	$ 7,945	$—	$111,590
Agency collateralized mortgage obligations	662,505	17,125	(124)	679,506
Agency mortgage-backed securities	108,056	1,587	(30)	109,613
Agency commercial mortgage-backed securities	62,352	899	—	63,251
Corporate bonds	46,874	196	(1,367)	45,703
Trust preferred securities	11,599	192	(52)	11,739
Other bonds and obligations	3,164	58	—	3,222
Total debt securities	998,195	28,002	(1,573)	1,024,624
Marketable equity securities	42,470	7,557	(1,281)	48,746
Total securities available for sale	1,040,665	35,559	(2,854)	1,073,370
Securities held to maturity				
Municipal bonds and obligations	95,663	7,337	—	103,000
Agency collateralized mortgage obligations	67	8	—	75
Tax advantaged economic development bonds	35,954	2,189	—	38,143
Other bonds and obligations	326	—	—	326
Total securities held to maturity	132,010	9,534	—	141,544
Total	$ 1,172,675	$ 45,093	$(2,854)	$1,214,914
December 31, 2015				
Securities available for sale				
Debt securities:				
Municipal bonds and obligations	$ 99,922	$ 4,763	$(124)	$104,561
Agency collateralized mortgage obligations	833,633	4,957	(5,554)	833,036
Agency mortgage-backed securities	127,274	542	(987)	126,829
Agency commercial mortgage-backed securities	—	—	—	—
Corporate bonds	42,849	—	(1,827)	41,022
Trust preferred securities	11,719	182	—	11,901
Other bonds and obligations	3,175	—	(34)	3,141
Total debt securities	1,118,572	10,444	(8,526)	1,120,490
Marketable equity securities	30,522	5,331	(1,886)	33,967
Total securities available for sale	1,149,094	15,775	(10,412)	1,154,457
Securities held to maturity				
Municipal bonds and obligations	94,642	3,359	(34)	97,967
Agency collateralized mortgage obligations	68	3	—	71
Tax advantaged economic development bonds	36,613	1,924	—	38,537
Other bonds and obligations	329	—	—	329
Total securities held to maturity	131,652	5,286	(34)	136,904
Total	$ 1,280,746	$ 21,061	$(10,446)	$1,291,361

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The amortized cost and estimated fair value of available for sale ("AFS") and held to maturity ("HTM") securities, segregated by contractual maturity at June 30, 2016 are presented below. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations. Mortgage-backed securities are shown in total, as their maturities are highly variable. Equity securities have no maturity and are also shown in total.

	Available for sale		Held to maturity	
	Amortized	Fair	Amortized	Fair
(In thousands)	Cost	Value	Cost	Value
Within 1 year	$—	$—	$2,799	$2,810
Over 1 year to 5 years	4,102	4,180	17,139	18,186
Over 5 years to 10 years	32,730	33,345	13,821	14,421
Over 10 years	128,450	134,729	98,184	106,052
Total bonds and obligations	165,282	172,254	131,943	141,469
Marketable equity securities	42,470	48,746	—	—
Mortgage-backed securities	832,913	852,370	67	75
Total	$1,040,665	$1,073,370	$132,010	$141,544

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Securities with unrealized losses, segregated by the duration of their continuous unrealized loss positions, are summarized as follows:

	Less Than Twelve Months		Over Twelve Months		Total	
(In thousands)	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
June 30, 2016						
Securities available for sale						
Debt securities:						
Agency collateralized mortgage obligations	$ 4	$ 8,824	$ 120	$ 14,854	$ 124	$ 23,678
Agency mortgage-backed securities	15	4,053	15	734	30	4,787
Corporate bonds	1,160	22,536	207	4,423	1,367	26,959
Trust preferred securities	52	1,204	—	—	52	1,204
Total debt securities	1,231	36,617	342	20,011	1,573	56,628
Marketable equity securities	203	3,851	1,078	7,063	1,281	10,914
Total securities available for sale	1,434	40,468	1,420	27,074	2,854	67,542
Total	$ 1,434	$ 40,468	$ 1,420	$ 27,074	$ 2,854	$ 67,542
December 31, 2015						
Securities available for sale						
Debt securities:						
Municipal bonds and obligations	$ 9	$ 1,587	$ 115	$ 3,400	$ 124	$ 4,987
Agency collateralized mortgage obligations	2,958	304,907	2,596	136,988	5,554	441,895
Agency mortgage-backed securities	306	34,543	681	35,522	987	70,065
Corporate bonds	30	6,934	1,796	21,587	1,826	28,521
Trust preferred securities	1	1,269	—	—	1	1,269
Other bonds and obligations	—	108	34	3,032	34	3,140
Total debt securities	3,304	349,348	5,222	200,529	8,526	549,877
Marketable equity securities	534	2,908	1,352	5,729	1,886	8,637
Total securities available for sale	3,838	352,256	6,574	206,258	10,412	558,514
Securities held to maturity						
Tax advantaged economic development bonds	—	—	34	2,143	34	2,143
Total securities held to maturity	—	—	34	2,143	34	2,143
Total	$ 3,838	$ 352,256	$ 6,608	$ 208,401	$ 10,446	$ 560,657

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Debt Securities

The Company expects to recover its amortized cost basis on all debt securities in its AFS and HTM portfolios. Furthermore, the Company does not intend to sell nor does it anticipate that it will be required to sell any of its securities in an unrealized loss position as of June 30, 2016, prior to this recovery. The Company’s ability and intent to hold these securities until recovery is supported by the Company’s strong capital and liquidity positions as well as its historically low portfolio turnover.

The following summarizes, by investment security type, the basis for the conclusion that the debt securities in an unrealized loss position within the Company’s AFS and HTM portfolios were not other-than-temporarily impaired at June 30, 2016:

AFS collateralized mortgage obligations

At June 30, 2016, 4 out of the total 123 securities in the Company’s portfolios of AFS collateralized mortgage obligations were in unrealized loss positions. Aggregate unrealized losses represented 0.5% of the amortized cost of securities in unrealized loss positions. The Federal National Mortgage Association (“FNMA”), Federal Home Loan Mortgage Corporation (“FHLMC”), and Government National Mortgage Association (“GNMA”) guarantee the contractual cash flows of all of the Company’s collateralized mortgage obligations. The securities are investment grade rated and there were no material underlying credit downgrades during the quarter. All securities are performing.

AFS mortgage-backed securities

At June 30, 2016, 12 out of the total 82 securities in the Company’s portfolios of AFS residential mortgage-backed securities were in unrealized loss positions. Aggregate unrealized losses represented 0.6% of the amortized cost of securities in unrealized loss positions. The FNMA, FHLMC, and GNMA guarantee the contractual cash flows of all of the Company’s residential mortgage-backed securities. The securities are investment grade rated and there were no material underlying credit downgrades during the quarter. All securities are performing.

AFS corporate bonds

At June 30, 2016, 3 out of 9 securities in the Company’s portfolio of AFS corporate bonds were in an unrealized loss position. The aggregate unrealized loss represents 4.8% of the amortized cost of bonds in unrealized loss positions. The Company reviews the financial strength of all of these bonds and has concluded that the amortized cost remains supported by the expected future cash flows of these securities.

At June 30, 2016, $1.2 million of the total unrealized losses was attributable to a $17.6 million investment. The Company evaluated this security, with a Level 2 fair value of $16.4 million, for potential other-than-temporary impairment (“OTTI”) at June 30, 2016 and determined that OTTI was not evident based on both the Company’s ability and intent to hold the security until the recovery of its remaining amortized cost.

AFS trust preferred securities

At June 30, 2016 1 out of the 3 securities in the Company’s portfolio of AFS trust preferred securities were in an unrealized loss position. Aggregate unrealized losses represented 4.2% of the amortized cost of these securities in an unrealized loss position. The Company’s evaluation of the present value of expected cash flows on these securities supports its conclusions about the recoverability of these securities’ amortized cost basis. These securities are investment grade rated. The Company reviews the financial strength of all of the single issue trust issuers and has concluded that the amortized cost remains supported by the market value of these securities and they are performing.

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Marketable Equity Securities
In evaluating its marketable equity securities portfolio for OTTI, the Company considers its ability to more likely than not hold an equity security to recovery. The Company additionally considers other various factors including the length of time and the extent to which the fair value has been less than cost and the financial condition and near term prospects of the issuer. Any OTTI is recognized immediately through earnings.

At June 30, 2016, 9 out of the total 26 securities in the Company’s portfolio of marketable equity securities were in an unrealized loss position. The unrealized loss represented 10.5% of the amortized cost of the securities. The Company has the ability and intent to hold the securities until recovery of their cost basis and does not consider the securities other-than-temporarily impaired at June 30, 2016. As new information becomes available in future periods, changes to the Company’s assumptions may be warranted and could lead to a different conclusion regarding the OTTI of these securities.

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NOTE 5. LOANS

The Company's loan portfolio is segregated into the following segments: commercial real estate, commercial and industrial, residential mortgage, and consumer. Commercial real estate loans include construction, single and multi-family, and other commercial real estate classes. Commercial and industrial loans include asset based lending loans, lease financing, and other commercial business loan classes. Residential mortgage loans include classes for 1-4 family owner occupied and construction loans. Consumer loans include home equity, direct and indirect auto, and other. These portfolio segments each have unique risk characteristics that are considered when determining the appropriate level for the allowance for loan losses. A substantial portion of the loan portfolio is secured by real estate in western Massachusetts, southern Vermont, northeastern New York, and in the Bank's other New England lending areas. The ability of many of the Bank's borrowers to honor their contracts is dependent, among other things, on the specific economy and real estate markets of these areas.

Total loans include business activity loans and acquired loans. Acquired loans are those loans acquired from Parke Bank, Firestone Financial Corp., Hampden Bancorp, Inc., the New York branch acquisition, Beacon Federal Bancorp, Inc., The Connecticut Bank and Trust Company, Legacy Bancorp, Inc., and Rome Bancorp, Inc. The following is a summary of total loans:

	June 30, 2016			December 31, 2015		
(In thousands)	Business Activities Loans	Acquired Loans	Total	Business Activities Loans	Acquired Loans	Total
Commercial real estate:						
Construction	$218,607	$30,428	$249,035	$210,196	$43,474	$253,670
Single and multi-family	244,949	42,171	287,120	214,823	36,783	251,606
Other commercial real estate	1,354,086	347,341	1,701,427	1,209,008	345,483	1,554,491
Total commercial real estate	1,817,642	419,940	2,237,582	1,634,027	425,740	2,059,767
Commercial and industrial loans:						
Asset based lending	325,476	—	325,476	331,253	—	331,253
Other commercial and industrial loans	527,612	181,471	709,083	495,979	221,031	717,010
Total commercial and industrial loans	853,088	181,471	1,034,559	827,232	221,031	1,048,263
Total commercial loans	2,670,730	601,411	3,272,141	2,461,259	646,771	3,108,030
Residential mortgages:						
1-4 family	1,519,067	302,702	1,821,769	1,454,233	332,747	1,786,980
Construction	20,965	866	21,831	26,704	1,351	28,055
Total residential mortgages	1,540,032	303,568	1,843,600	1,480,937	334,098	1,815,035
Consumer loans:						
Home equity	310,565	49,346	359,911	307,159	53,446	360,605
Auto and other	414,486	110,163	524,649	311,328	130,238	441,566
Total consumer loans	725,051	159,509	884,560	618,487	183,684	802,171
Total loans	$4,935,813	$1,064,488	$6,000,301	$4,560,683	$1,164,553	$5,725,236

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The carrying amount of the acquired loans at June 30, 2016 totaled $1.1 billion. A subset of these loans was determined to have evidence of credit deterioration at acquisition date, which is accounted for in accordance with ASC 310-30. These purchased credit-impaired loans presently maintain a carrying value of $19.7 million (and a note balance of $38.2 million). These loans are evaluated for impairment through the periodic reforecasting of expected cash flows. Loans considered not impaired at acquisition date had a carrying amount of $1.0 billion.

At December 31, 2015, acquired loans maintained a carrying value of $1.2 billion and purchased credit-impaired loans totaled $21.4 million (note balance of $40.2 million). Loans considered not impaired at acquisition date had a carrying amount of $1.1 billion.

The following table summarizes activity in the accretable yield for the acquired loan portfolio that falls under the purview of ASC 310-30, Accounting for Certain Loans or Debt Securities Acquired in a Transfer:

	Three Months Ended June 30,	
(In thousands)	2016	2015
Balance at beginning of period	$6,464	$3,431
Acquisitions	708	4,178
Reclassification from nonaccretable difference for loans with improved cash flows	522	405
Reclassification to TDR	—	—
Accretion	(1,481)	(1,474)
Balance at end of period	$6,213	$6,540

	Six Months Ended June 30,	
(In thousands)	2016	2015
Balance at beginning of period	$6,925	$2,541
Acquisitions	708	4,178
Reclassification from nonaccretable difference for loans with improved cash flows	1,418	1,736
Reclassification to TDR	(185)	—
Accretion	(2,653)	(1,915)
Balance at end of period	$6,213	$6,540

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The following is a summary of past due loans at June 30, 2016 and December 31, 2015:

Business Activities Loans

(in thousands)	30-59 Days Past Due	60-89 Days Past Due	90 Days or Greater Past Due	Total Past Due	Current	Total Loans	Past Due > 90 days and Accruing
June 30, 2016							
Commercial real estate:							
Construction	$ —	$ —	$—	$—	$218,607	$218,607	$ —
Single and multi-family	11	—	518	529	244,420	$244,949	—
Other commercial real estate	1,210	—	5,593	6,803	1,347,283	$1,354,086	2,195
Total	1,221	—	6,111	7,332	1,810,310	1,817,642	2,195
Commercial and industrial loans:							
Asset based lending	—	—	—	—	325,476	$325,476	—
Other commercial and industrial loans	931	2,270	5,934	9,135	518,477	$527,612	127
Total	931	2,270	5,934	9,135	843,953	853,088	127
Residential mortgages:							
1-4 family	1,907	1,359	3,075	6,341	1,512,726	$1,519,067	487
Construction	—	—	44	44	20,921	$20,965	—
Total	1,907	1,359	3,119	6,385	1,533,647	1,540,032	487
Consumer loans:							
Home equity	1,374	5	1,760	3,139	307,426	$310,565	43
Auto and other	1,650	238	378	2,266	412,220	$414,486	—
Total	3,024	243	2,138	5,405	719,646	725,051	43
Total	$ 7,083	$ 3,872	$17,302	$ 28,257	$4,907,556	$4,935,813	$ 2,852

Business Activities Loans

(in thousands)	30-59 Days Past Due	60-89 Days Past Due	90 Days or Greater Past Due	Total Past Due	Current	Total Loans	Past Due > 90 days and Accruing
December 31, 2015							
Commercial real estate:							
Construction	$						