

BERKSHIRE HILLS BANCORP INC
Form 10-K
March 16, 2007

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2006

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

For the transition period from _____ to _____

Commission File Number: 0-58514

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

Delaware
(State or other jurisdiction of
incorporation or organization)

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

**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: None

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

**Common Stock, par
value \$0.01 per share**
(Title of class)

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 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, or a non-accelerated filer. See definition of "large accelerated filer and accelerated filer" in rule 12b-2 of the Exchange Act. (Check one):
Large Accelerated filer Accelerated filer Non-accelerated filer

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 \$255 million, based upon the closing price of \$35.48 as quoted on the NASDAQ Global Select Market as of the last business day of the registrant's most recently completed second fiscal quarter.

The number of shares outstanding of the registrant's common stock as of March 7, 2007 was 8,760,526.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the 2007 Annual Meeting of Shareholders are incorporated by reference in Part III of this Form 10-K.

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PART I

ITEM 1. BUSINESS

FORWARD-LOOKING STATEMENTS

This report contains forward-looking statements that are based on assumptions and may describe future plans, strategies and expectations of Berkshire Hills Bancorp, Inc. and Berkshire Bank. This document may include forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These forward-looking statements, which are based on certain assumptions and describe future plans, strategies, and expectations of the Company, are generally identified by use of the words “anticipate,” “believe,” “estimate,” “expect,” “intend,” “plan,” “project,” “seek,” “strive,” “try,” or future or conditional verbs such as “will,” “would,” “should,” “could,” “may,” or similar expressions. Although we believe that our plans, intentions and expectations, as reflected in these forward-looking statements are reasonable, we can give no assurance that these plans, intentions or expectations will be achieved or realized. Our ability to predict results or the actual effects of our plans and strategies are inherently uncertain. Actual results, performance or achievements could differ materially from those contemplated, expressed or implied by the forward-looking statements contained in this Form 10-K. Important factors that could cause actual results to differ materially from our forward-looking statements are set forth under Item 1A. - “Risk Factors” in this Form 10-K, and in other reports filed with the Securities and Exchange Commission. There are a number of factors, many of which are beyond our control, that could cause actual conditions, events, or results to differ significantly from those described in the forward-looking statements. These factors include, but are not limited to: general economic conditions, either nationally or locally in some or all of the areas in which we conduct our business; conditions in the securities markets or the banking industry; changes in interest rates and energy prices, which may affect our net income or future cash flows; changes in deposit flows, and in demand for deposit, loan, and investment products and other financial services in our local markets; changes in real estate values, which could impact the quality of the assets securing our loans; changes in the quality or composition of the loan or investment portfolios; changes in competitive pressures among financial institutions or from non-financial institutions; the ability to successfully integrate any assets, liabilities, customers, systems, and management personnel we may acquire into our operations and our ability to realize related revenue synergies and cost savings within expected time frames; our timely development of new and competitive products or services in a changing environment, and the acceptance of such products or services by our customers; the outcome of pending or threatened litigation or of other matters before regulatory agencies, whether currently existing or commencing in the future; changes in accounting principles, policies, practices, or guidelines; changes in legislation and regulation; operational issues and/or capital spending necessitated by the potential need to adapt to industry changes in information technology systems on which we are highly dependent; changes in the monetary and fiscal policies of the U.S. Government, including policies of the U.S. Treasury and the Federal Reserve Board; war or terrorist activities; and other economic, competitive, governmental, regulatory, and geopolitical factors affecting the Company’s operations, pricing, and services. Additionally, the timing and occurrence or non-occurrence of events may be subject to circumstances beyond our control. You should not place undue reliance on these 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, Inc. is a Delaware corporation and the holding company for Berkshire Bank. Established in 1846, Berkshire Bank is one of Massachusetts’ oldest and largest independent banks and is the largest banking institution based in Western Massachusetts. The Bank is headquartered in Pittsfield, Massachusetts and operates 27 full-service banking offices serving communities throughout Western Massachusetts and in Northeastern New York. The Bank operates in three regions:

The Berkshire County Region, with eleven offices in Berkshire County.

The Pioneer Valley Region with ten offices along the Connecticut River valley north and west of Springfield in Massachusetts. The Company entered this region through the acquisition of Woronoco Bancorp Inc. in June 2005.

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·The New York Region serving Albany and the surrounding area in Northeastern New York. This region represents a de novo expansion by the Bank. At year end 2006, it had six offices, with another four offices scheduled to open in the first half of 2007.

These three regions are viewed as having favorable demographics and provide an attractive regional niche for the Bank to distinguish itself as the preferred choice compared to larger super-regional banks and smaller community banks. The Company is pursuing growth through acquisitions, de novo branching, product development, and organic growth. The Company is considering possible expansion into Southern Vermont and Northern Connecticut. The Bank entered the Pioneer Valley area of Massachusetts in 2005 with the acquisition of Woronoco Bancorp, Inc. The Company made acquisitions of insurance and financial planning providers in 2004 and 2005, followed by the acquisition of five affiliated insurance agencies in the fourth quarter of 2006. These insurance acquisitions were merged and integrated into the Berkshire Insurance Group, which was made a subsidiary of the Company. The Company aspires to be "America's Most Exciting Bank". It has set out to change the financial service experience, and its vision is to establish itself as a world-class financial services company through an engaging and exciting environment where customers want to do business and employees want to work.

The Bank is a full-scale provider of deposit, lending, investment, and insurance products by a team of employees with extensive experience in banking, insurance, and investment management. The Company stresses quality control, including using Six Sigma tools to improve operational effectiveness and efficiency. It is enhancing its credit and risk management functions to maintain strong asset quality and careful interest rate management. It stresses a culture of teamwork and performance excellence to produce customer satisfaction to support its strategic growth and profitability.

COMPANY WEBSITE AND AVAILABILITY OF SECURITIES AND EXCHANGE COMMISSION FILINGS

The Company's Internet website is www.berkshirebank.com. The Company makes available free of charge on or through its website, its 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 as soon as reasonably practicable after the Company electronically files such material with the Securities and Exchange Commission. 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 Banknorth, and Citizens 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 pricing of loan and deposit products and wealth management services. The location and convenience of branch offices is also a significant competitive factor, particularly regarding new offices. The Bank has recently designated regional headquarters led by regional presidents as an important component of its market management. The Company has recently revised its vision - to establish itself as a world-class financial services company through an engaging and exciting environment where customers want to do business and employees want to work. This brand and culture statement is expected to drive customer emotional engagement, loyalty, market share and profitability.

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 Board, legislative tax policies and governmental budgetary matters. The majority of the Bank's loans are made in its market areas and are secured by real estate in its primary markets. Lending activities are therefore affected by activity in these real estate markets. The Bank does not engage in subprime lending activities targeted towards borrowers in high risk categories. The Bank monitors and limits 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

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the event of sustained rate increases. Despite the 4.25% increase in the prime interest rate over the two years ending in June 2006, such higher losses have not yet been recorded but were determined to be inherent in the portfolio, which resulted in an increase in the loan loss allowance in 2006.

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.

(Dollars in millions)	2006		2005		2004		2003		2002	
	Amount	Percent of Total	Amount	Percent of Total	Amount	Percent of Total	Amount	Percent of Total	Amount	Percent of Total
Residential mortgages	\$ 599.2	36%	\$ 549.8	39%	\$ 235.2	28%	\$ 265.5	34%	\$ 241.6	33%
Commercial mortgages	567.1	33	410.7	29	260.5	32	206.4	26	157.1	22
Commercial business	189.8	11	158.7	11	150.9	18	166.3	21	165.3	23
Total commercial loans	756.9	44	569.4	40	411.4	50	372.7	47	322.4	45
Consumer	342.9	20	301.0	21	181.5	22	154.0	19	159.0	22
Total loans	1,699.0	100%	1,420.2	100%	828.1	100%	792.2	100%	723.0	100%
Allowance for loan losses	(19.4)		(13.0)		(9.3)		(9.0)		(10.3)	
Net loans	\$ 1,679.6		\$ 1,407.2		\$ 818.8		\$ 783.2		\$ 712.7	

Residential mortgages. The Bank originates first mortgage loans to individuals, secured by one-to-four family residences in its markets. The Bank originates both fixed-rate and adjustable-rate mortgages to finance primary and secondary residences, as well as non-owner occupied properties. The Bank also provides construction and land development first mortgage loans to individuals. The Bank also offers jumbo loan products and FHA/VA related products. Berkshire Bank generally underwrites, processes, and closes its residential mortgages following conforming secondary market guidelines.

The Bank 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. Residential construction loans totaled \$32 million at year-end 2006.

The Bank normally holds most adjustable-rate mortgages for its own portfolio. It generally sells most 15 and 30 year fixed-rate mortgages on a servicing released flow basis, although some are retained in portfolio. Forward sale commitments are made when customers rate-lock their applications. Sometimes the Bank also sells or securitizes some existing residential mortgages to adjust interest rate risk or to provide liquidity. Residential mortgages are viewed as having the least credit risk and the narrowest lending margins among the Bank's lending products.

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 terms of up to 25 years and

with interest rates that adjust periodically (primarily from floating to five years).

Berkshire 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 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.

The Bank also originates commercial construction loans for residential and commercial properties. These loans generally have an interest-only phase during construction and then convert to permanent financing. Berkshire Bank also originates land loans for the purpose of holding or developing the land for sale. Land loans are normally three year notes with principal due at maturity. Commercial construction loans totaled \$130 million at year-end 2006.

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

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operation or management of the properties, repayment of such loans may be affected by adverse conditions in the real estate market or the economy. Additionally, construction lending often involves the disbursement of substantial funds with repayment dependent, in part, on the success of the ultimate project rather than on established cash flows. If the Bank is forced to foreclose on a construction project before or at completion, there is a higher risk of credit loss. Berkshire Bank seeks to minimize these risks through strict adherence to its underwriting standards and portfolio management processes.

Commercial Business Loans. The Bank offers secured commercial term loans with repayment terms which are normally limited to the lesser of the expected useful life of the asset being financed, generally not exceeding seven years. Berkshire 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 lending policies regarding debt-service coverage ability and guarantees are similar to those which govern commercial real estate lending. 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. Berkshire Bank generally does not make unsecured commercial loans.

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 appraise and may fluctuate in value. The Bank gives additional consideration to the borrower's credit history and capacity to help mitigate these risks. Commercial loans are often a central component of a total commercial banking relationship, and are therefore an important component of the Bank's lending activities.

Consumer Loans. Berkshire Bank's consumer lending strategy is focused on indirect automobile loans and home equity loans. The Bank offers fixed-rate automobile loans with terms of up to 72 months for new and recent model used cars and up to 66 months for older model used cars. The Bank generally makes such loans up to 100% of the retail value shown in the *NADA Used Car Guide*. This program is targeted towards prime grade credits. The Bank does not offer subprime lending programs. The automobile loans have produced a higher loan charge-off rate than the Bank's residential mortgage and home equity loans. Collections are more sensitive to changes in borrower financial circumstances, and the collateral can be depreciated or damaged prior to repossession. Additionally, collections are more subject to the limitations of federal and state laws. Automobile loans outstanding totaled \$196 million at year-end 2006. The Bank originates indirect loans through a network of automobile dealers in its market, as well as through a conduit sales finance company sourced from franchised automobile dealerships.

The Bank's home equity lines of credit are typically secured by second mortgages on borrowers' residences. Home equity lines have an initial revolving period up to ten years, followed by an amortizing term up to fifteen 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. 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 more sensitivity to rate changes and more possible compression of collateral coverage on second liens. The Bank also includes all other consumer loans in this portfolio total, including personal secured and unsecured loans and overdraft protection facilities. Home equity and other loans outstanding at year-end 2006 totaled \$147 million.

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Maturity and Sensitivity of Loan Portfolio. The following table shows contractual final maturities of selected loan categories at year-end 2006. The contractual maturities do not reflect premiums, discounts, and deferred costs, and do not reflect prepayments.

Contractual Maturity (In thousands)	One Year or Less	More than One to Five Years	More Than Five Years	Total
Construction mortgage loans:				
Residential	\$ 1,669	\$ 30,653	\$ -	\$ 32,322
Commercial	23,293	106,505	-	129,798
Commercial business loans	92,771	46,053	50,934	189,758
Total	\$ 117,733	\$ 183,211	\$ 50,934	\$ 351,878

For the \$234 million total of loans above which mature in more than one year, \$40 million of these loans are fixed-rate and \$194 million are adjustable rate.

Loan Administration. Lending activities are governed by a loan policy approved by the Board of Directors. Internal staff perform post-closing loan documentation review, quality control and ongoing loan review. The Bank assigns a risk rating to all commercial loans, and loan review staff perform an ongoing program of loan and risk rating reviews. Management also employs an independent third party for loan reviews, as discussed in “Allowance for Loan Losses.”

The Bank’s lending activities follow written, non-discriminatory underwriting standards and loan origination procedures established by Berkshire Bank’s Board of Directors and management. The Board of Directors has approved individual and combined lending approval authorities up to specified limits. Above those limits, the Board of Directors established Regional Loan Committees with commercial approval authority generally up to \$5 million. Management’s Executive Loan Committee is responsible for commercial loan approval above \$5 million and residential mortgage approval above \$2 million. The Bank’s lending activities are conducted by its salaried and commissioned loan personnel and through its relationships with automobile dealers. From time to time, the Bank will purchase whole loans or participations in loans. These loans are underwritten according to Berkshire Bank’s underwriting criteria and procedures and are generally serviced by the originating lender under terms of the applicable participation agreement. The Bank from time to time will sell or securitize residential mortgages in the secondary market based on prevailing market interest rate conditions and an analysis of the composition and risk of the loan portfolio, the Bank’s interest rate risk profile and liquidity needs. 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 ninety days from approval; some commercial commitments are made for longer terms. Total lending commitments, including lines and letters of credit, were \$456 million at year-end 2006.

The loan policy sets certain limits on concentrations of credit and requires periodic reporting of concentrations to the Bank’s Board. Loans outstanding to the ten largest relationships totaled \$155 million at year-end 2006. All of these relationships were rated in the three lowest risk commercial risk rating categories used by the Bank. Total year-end commercial construction loans outstanding were 74% of the Bank’s risk based capital at year-end, and total commercial mortgage outstandings (excluding certain owner-occupied loans) were estimated at 265% of risk based capital. The FDIC has recently established monitoring guidelines of 100% and 300% for these ratios, respectively. Above these guidelines, additional monitoring and risk management controls are required. Based on commitments outstanding at year-end 2006, the Bank may exceed these monitoring guidelines for one or both of these ratios in 2007, and the Bank is proactively establishing additional monitoring and risk management controls as set forth by the FDIC. The commercial construction and development loans primarily involve lodging, leisure, and retail properties. For the majority of these loans, the Bank provides permanent or semi-permanent financing after the construction

period. The Bank also finances residential and condominium construction and development projects. The total number of units without committed end sales does not exceed sixty units.

Problem Assets. While Berkshire Bank generally prefers to work with borrowers to resolve problems, Berkshire Bank generally will initiate foreclosure or other proceedings no later than the 90th day of a delinquency, as necessary, to

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minimize any potential loss. Management reports to the Board of Directors monthly delinquent loans and nonperforming assets. 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 auto loans are maintained on accrual until they reach 120 days delinquent, and then they are generally charged-off.

Real estate acquired by Berkshire 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. At year-end 2006, Berkshire Bank had no foreclosed real estate.

The following table sets forth additional information on year-end problem assets.

<i>(Dollars in thousands)</i>	2006	2005	2004	2003	2002
Nonaccruing loans:					
Residential mortgages	\$ 15	\$ 261	\$ 327	\$ 348	\$ 230
Commercial mortgages	308	271	147	496	-
Commercial business	7,203	553	523	1,887	2,850
Consumer	66	101	155	468	661
Total nonperforming loans	7,592	1,186	1,152	3,199	3,741
Real estate owned	-	-	-	-	1,500
Total nonperforming assets	\$ 7,592	\$ 1,186	\$ 1,152	\$ 3,199	\$ 5,241
Troubled debt restructurings					
Troubled debt restructurings	\$ 5,268	\$ 1,234	\$ 510	\$ 214	\$ -
Accruing loans 90+ days past due	281	110	65	306	590
Total nonperforming loans/total loans					
Total nonperforming loans/total loans	0.45%	0.08%	0.14%	0.40%	0.52%
Total nonperforming assets/total assets					
Total nonperforming assets/total assets	0.35%	0.06%	0.09%	0.26%	0.36%

Asset Classification and Delinquencies. The Bank performs an internal analysis of its loan portfolio and assets to classify such loans and assets similar to the manner in which such loans and assets are classified by the federal banking regulators. There are four classifications for problem assets: loss, doubtful, substandard and special mention. An asset classified as "Loss" is normally 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. Nonaccruing loans are normally classified as substandard. "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."

At year-end 2006, there were no loan balances classified as loss. The balance of loans classified as doubtful was \$228 thousand. Loans classified as substandard totaled \$23.7 million. The largest three substandard commercial relationships totaled \$10.6 million and were in the process of collection. The largest substandard loan totaled \$6.0 million and was in collection through bankruptcy proceedings. This loan is secured by business assets and had a \$0.5 million impaired loan reserve at year-end. Loans classified as substandard are collectively regarded as having the potential to be nonperforming in the future. Loans rated special mention totaled \$34.4 million at year end 2006. Loans delinquent 30 - 90 days totaled \$4.1 million at year-end 2006. Troubled debt restructurings totaled \$5.3 million at year-end 2006, which was increased from \$1.2 million at the prior year-end due primarily to restructurings related to

certain substandard loans.

Allowance for Loan Losses. Berkshire Bank maintains an allowance for loan losses to absorb losses inherent in the loan portfolio. 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 and an unallocated component for estimated model imprecision.

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The loan portfolio and other credit exposures are regularly reviewed by management to evaluate the adequacy of the allowance for loan losses. The methodology for assessing the appropriateness of the allowance includes comparison to actual losses, peer group comparisons, industry data and economic conditions. In addition, management employs an independent third party to perform an annual review of all of Berkshire Bank's commercial loan relationships exceeding \$1 million, all material credits on Berkshire Bank's watch list or classified as substandard, and a random sampling of new loans. The regulatory agencies, as an integral part of their examination process, also periodically review Berkshire Bank's allowance for loan losses. Such agencies may require Berkshire Bank to make additional provisions for estimated losses based upon judgments different from those of management.

In assessing the allowance for loan losses, loss factors are applied to various pools of outstanding loans. Loss factors are based on management's judgment of losses inherent in the portfolio, including past loan loss experience, known and inherent risks in the nature and volume of the portfolio, information about specific borrower situations and estimated collateral values and economic conditions. The loss factors may be adjusted for significant factors that, in management's judgment, affect the losses inherent in the portfolio as of the evaluation date. Generally, nonaccruing commercial loans are deemed impaired and evaluated for specific valuation allowances. Berkshire Bank primarily segregates the loan portfolio according to the primary loan types: residential mortgages, commercial mortgages, commercial business loans and consumer loans, and also evaluates commercial construction loans as a pool. Reserves are assigned to impaired loans, and this is normally based on the fair value of collateral since most impaired loans are deemed to be collateral dependent. In 2006, the Company adjusted its loan loss allowance based on new loss factors which emerged during the year, as is further described in Item 7 of this Form 10-K.

In addition, management assesses the allowance using factors that cannot be associated with specific credit or loan categories. These factors include management's subjective evaluation of local and national economic and business conditions, portfolio concentration and changes in the character and size of the loan portfolio. The allowance methodology reflects management's objective that the overall allowance appropriately reflects a margin for the imprecision necessarily inherent in estimates of expected credit losses.

Although management believes that it uses the best information available to establish the allowance for loan losses, 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 deteriorate as a result of the factors discussed above. Any material increase in the allowance for loan losses may adversely affect Berkshire Bank's financial condition and results of operations. In 2006, the allowance was reduced by \$425 thousand representing the transfer to liabilities of reserves for losses on unfunded credit commitments.

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

<i>(Dollars in thousands)</i>	2006	2005	2004	2003	2002
Balance at beginning of year	\$ 13,001	\$ 9,337	\$ 8,969	\$ 10,308	\$ 11,034
<i>Charged-off loans:</i>					
Residential mortgages	27	-	-	-	-
Commercial mortgages	-	-	138	-	510
Commercial business	461	432	218	157	444
Consumer	1,288	1,110	1,846	4,207	9,074
Total charged-off loans	1,776	1,542	2,202	4,364	10,028
<i>Recoveries on charged-off loans:</i>					
Commercial business	43	55	296	440	178
Consumer	667	517	709	1,125	2,944
Total recoveries	710	572	1,005	1,565	3,122
Net loans charged-off	1,066	970	1,197	2,799	6,906
Allowance attributed to loans acquired by merger	-	3,321	-	-	-
Provision for loan losses	7,860	1,313	1,565	1,460	6,180
Transfer of commitment reserve	(425)	-	-	-	-
Allowance for loan losses, balance at end of year	\$ 19,370	\$ 13,001	\$ 9,337	\$ 8,969	\$ 10,308
Ratios:					
Net loans charged-off/average total loans	0.07%	0.08%	0.15%	0.35%	0.87%
Recoveries/charged-off loans	39.98	37.09	45.64	35.86	31.13
Net loans charged-off/allowance for loan losses	5.50	7.46	12.82	31.21	67.00
Allowance for loan losses/total loans	1.14	0.92	1.13	1.13	1.43
Allowance for loan losses/nonperforming loans	2.55 x	10.96 x	8.11 x	2.80 x	2.76 x

The following table presents year-end data for the approximate allocation of the allowance for loan losses by loan categories at the dates indicated and the percentage of loans in each category. 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.

	2006	2005	2004	2003	2002
	Percent of Loans in Each Category	Percent of Loans in Each Category	Percent of Loans in Each Category	Percent of Loans in Each Category	Percent of Loans in Each Category
	Amount Allocated to	Amount Allocated to	Amount Allocated to	Amount Allocated to	Amount Allocated to

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<i>(Dollars in thousands)</i>	Total Loans		Total Loans		Total Loans		Total Loans		Total Loans	
Residential mortgages	\$ 1,845	36%	\$ 1,649	39%	\$ 435	28%	\$ 491	34%	\$ 446	33%
Commercial mortgages	9,939	33	5,933	29	3,828	32	2,945	26	1,843	22
Commercial business	5,199	11	3,517	11	3,344	18	3,362	21	3,369	23
Consumer	2,387	20	1,902	21	1,730	22	2,171	19	4,650	22
Total	\$ 19,370	100%	\$ 13,001	100%	\$ 9,337	100%	\$ 8,969	100%	\$ 10,308	100%

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INVESTMENT SECURITIES ACTIVITIES

The investment securities portfolio is primarily used to provide for Berkshire Bank's cash flow needs, to provide adequate liquidity to protect the safety of customer deposits, to manage interest rate risk, and to earn a reasonable return on investment. The average maturity or repricing and the types of securities maintained are based upon the composition, maturity, and quality of the loan portfolio, interest rate risk and Berkshire Bank's liquidity position and deposit structure.

The Risk Management Committee of the Board of Directors is responsible for developing and reviewing Berkshire Bank's investment policy. Investment decisions are made in accordance with the Bank's investment policy and are based upon the quality of a particular investment, its inherent risks, the Bank's liquidity needs, prospects for yield and/or appreciation and the potential tax consequences. General investment strategies are developed and authorized by the Risk Management Committee. The execution of specific investment actions and the day-to-day oversight of the Bank's investment portfolio rests with the President and the Treasurer. The Board of Directors receives a monthly report of all securities transactions made during the previous month.

The majority of the Bank's investments have been in mortgage-backed securities issued or guaranteed by U.S. Government sponsored enterprises. The Bank has focused on adjustable-rate pass-through mortgage-backed securities that have limited extension risk, such as five and seven-year hybrid securities and 10-year fixed-rate mortgage-backed securities. These securities typically have an average duration of 3-5 years. Securities acquired as a result of the Woronoco acquisition also were primarily U.S. Government sponsored enterprise pass-through mortgage-backed securities, although these securities were mostly backed by fixed rate loans. Nearly all the mortgage-backed securities owned by the Bank are issued by Fannie Mae or Freddie Mac. No other issuer concentrations exceeding 10% of stockholders' equity existed at year-end 2006. The Bank also purchases municipal bonds and obligations, and purchases and originates industrial revenue bonds. Some of these securities support local municipal relationships and these securities provide a tax-advantaged yield. Subsequent to the deleveraging in 2006, municipal bonds and obligations became the largest category of investments. Other corporate bonds are primarily investment grade trust preferred securities issued by financial institutions. The equity securities portfolio consists primarily of investments in the common stock of the Federal Home Loan Bank of Boston. The Bank has substantially liquidated its actively managed portfolio of exchange traded equity securities of bank, utility and industrial stocks.

In 2005 and 2006, the Bank executed deleveraging programs to reduce leverage, improve yield, and improve interest rate sensitivity. The 2005 deleveraging was in conjunction with the Woronoco acquisition. Berkshire Bank's investment policy allows the use of certain hedging strategies, including the purchase of options in an effort to increase the return and decrease the risk on the securities portfolio.

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The following table presents the year-end amortized cost and fair value of Berkshire Bank's securities, by type of security, for the years indicated:

<i>(In thousands)</i>	2006		2005		2004	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Available for sale securities						
U.S. Government agencies	\$ -	\$ -	\$ 69	\$ 63	\$ 1,106	\$ 1,113
Municipal bonds and obligations	63,788	64,503	63,701	63,673	19,169	19,172
Mortgage-backed securities	85,102	84,334	264,705	258,504	323,956	322,585
Other bonds and obligations	20,392	20,439	24,356	24,703	9,418	9,429
Equity securities	24,687	24,930	41,667	43,933	24,210	32,122
Total available for sale securities	\$ 193,969	\$ 194,206	\$ 394,498	\$ 390,876	\$ 377,859	\$ 384,421
Held to maturity securities						
Municipal bonds and obligations	\$ 35,572	\$ 35,286	\$ 23,851	\$ 23,851	\$ 25,227	\$ 25,227
Mortgage-backed securities	4,396	4,400	6,057	5,912	4,715	4,672
Total held to maturity securities	\$ 39,968	\$ 39,686	\$ 29,908	\$ 29,763	\$ 29,942	\$ 29,899

The following table summarizes year-end 2006 amortized cost, weighted average yields and contractual maturities of debt securities. Yields are stated on a book basis (not fully taxable equivalent).

<i>(Dollars in millions)</i>	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	\$ 9.2	4.20%	\$ 1.4	3.62%	\$ 5.3	3.78%	\$ 83.5	4.36%	\$ 99.4	4.30%
Mortgage-backed securities	-	-	4.3	4.18	12.6	5.16	72.6	5.09	89.5	5.06
Other bonds and obligations	-	-	-	-	3.0	5.18	17.4	5.99	20.4	5.88
Total	\$ 9.2	4.20%	\$ 5.7	4.04%	\$ 20.9	4.81%	\$ 173.5	4.83%	\$ 209.3	4.78%

DEPOSIT ACTIVITIES AND OTHER SOURCES OF FUNDS

Deposits are the major source of funds for Berkshire Bank's lending and investment activities. Deposit accounts are the primary product and service interaction with the Bank's customers. The Bank also uses borrowings from the Federal Home Loan Bank of Boston (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. In 2005, the Company created a trust subsidiary to issue \$15.0 million in trust preferred securities, which provided funds which were invested in the Bank as additional paid in capital, thereby increasing its regulatory capital.

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. Berkshire 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. Money market accounts have increased in popularity due to their interest rate structure. Savings accounts include traditional passbook

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and statement accounts. The Bank's time accounts provide maturities from three months to five years. Additionally, the Bank offers a variety of retirement deposit accounts to personal and business customers. The Bank added brokered time deposit accounts with the acquisition of Woronoco Bancorp. These brokered deposits are being allowed to runoff.

The following table presents information concerning average balances and weighted average interest rates on Berkshire Bank's deposit accounts for the years indicated.

<i>(Dollars in millions)</i>	2006			2005			2004		
	Average Balance	Percent of Total Average Deposits	Weighted Average Rate	Average Balance	Percent of Total Average Deposits	Weighted Average Rate	Average Balance	Percent of Total Average Deposits	Weighted Average Rate
Demand	\$ 174.5	12%	-%	\$ 149.6	13%	-%	\$ 103.7	12%	-%
NOW	137.8	9	1.09	121.7	11	0.39	97.9	11	0.09
Money market	284.4	19	3.41	209.0	18	2.13	160.3	19	1.29
Savings	210.6	14	0.90	205.8	18	0.90	168.5	20	0.77
Time	651.7	46	4.28	445.2	40	3.20	321.0	38	2.78
Total	\$ 1,459.0	100%	2.81%	\$ 1,131.3	100%	1.86%	\$ 851.4	100%	1.46%

At year-end 2006, Berkshire Bank had time deposit accounts in amounts of \$100 thousand or more maturing as follows:

Maturity Period	Amount	Weighted Average Rate
<i>(Dollars in thousands)</i>		
Three months or less	\$ 58,527	4.49%
Over 3 months through 6 months	85,460	4.94
Over 6 months through 12 months	85,703	4.96
Over 12 months	92,094	4.80
Total	\$ 321,784	4.82%

The FHLBB functions as a central reserve bank providing credit for member institutions. As an FHLBB member, Berkshire Bank is required to own capital stock of the FHLBB. FHLBB borrowings are generally secured by most of the member'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 also utilized notes payable and junior subordinated debentures as additional funds sources.

WEALTH MANAGEMENT SERVICES

The Bank's Asset Management/Trust Group provides consultative trust relationship management to individuals, businesses, and institutions, with an emphasis on personal investment management to individuals. The group has built a track record over more than a decade with its dedicated in-house investment management team. At year-end 2006, assets under management totaled \$494 million. The group also provides brokerage and investment management services in association with Commonwealth Financial Network.

INSURANCE

Expanding on its existing insurance operations, and those acquired as part of the Woronoco Bancorp acquisition in 2005, Berkshire Insurance Group, Inc. acquired five agencies with eight locations at the end of October 2006. The resulting agency has 94 full-time equivalent employees in ten locations in Berkshire, Franklin and Hampden Counties of Massachusetts. Berkshire Insurance Group is one of the largest insurance agencies in Western Massachusetts. One of the acquired agencies was a Best Practices and Five Star designee which bolstered the administrative and efficiency expertise, and one of the agencies had a strong sales selection, training and oversight process in place. The newly appointed executive team draws on over 175 years of independent agency management and sales experience and manages a combined sales force of fifteen agents. Berkshire Insurance Group sells all lines of insurance (personal,

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commercial, employee benefits, and life insurance) in western Massachusetts, southern Vermont, and northwestern Connecticut. The group is preparing to enter the New York market for commercial insurance in the second quarter of 2007, and is also licensed in New Hampshire, Maine, Pennsylvania, Florida, New Jersey, Colorado, and North Carolina. Berkshire Insurance Group is instituting an aggressive cross sell program of insurance and banking products through all offices and branches.

GOVERNMENT BANKING

Berkshire Bank offers full-service government banking for cities, towns and municipal school districts in its primary markets and southern Vermont. The Bank offers municipalities all aspects of financial advisory services for the sale of notes and bonds, actively working with bond counsel, rating agencies, consulting agencies and bond buyers. Additionally, the Bank offers a wide range of municipal deposit products and checking accounts. In October 2005, Berkshire Bank opened Berkshire Municipal Bank, an FDIC-insured, New York-chartered limited purpose commercial bank, organized principally to accept deposits from New York municipalities and other governmental entities.

PERSONNEL

At year-end 2006, the Company had 522 full-time equivalent employees, representing an increase of 123 (31%) from 399 at year-end 2005. This growth was primarily due to the insurance company acquisitions in the fourth quarter. Year-end personnel included 94 full-time equivalent employees in Berkshire Insurance Group and 428 in the Bank. The employees are not represented by a collective bargaining unit and the Bank will strive to continue its strong relationship with its employees.

SUBSIDIARY ACTIVITIES

Berkshire Hills Bancorp, Inc. wholly owns three active subsidiaries: Berkshire Bank, Berkshire Insurance Group, and Berkshire Hills Capital Trust I. The capital trust subsidiary was created under Delaware law in 2005 to facilitate the issuance of trust preferred securities. The Berkshire Insurance Group is incorporated in Massachusetts. It was contributed to the Company by the Bank in October, 2006 in conjunction with the insurance agency purchases, and was previously discussed under "Insurance". The Company also owns one dormant Massachusetts subsidiary, Berkshire Hills Technology, Inc., which discontinued operations in 2004.

Berkshire Bank is a Massachusetts chartered savings bank which wholly owns five subsidiaries. The Bank owns three subsidiaries which are qualified as "securities corporations" for Massachusetts income tax purposes: North Street Securities Corporation, Woodland Securities, Inc., and Gold Leaf Securities Corporation. Berkshire Bank also owns Berkshire Municipal Bank, which was previously discussed under "Government Banking". Additionally, the Bank owns the inactive subsidiary, Berkshire Financial Planning, Inc., which ceased offering brokerage services in 2004. Except for Berkshire Municipal Bank, all subsidiaries of Berkshire Bank are incorporated in Massachusetts.

During 2005, the Company acquired Woronoco Bancorp. Between the acquisition date and the end of the year, all of the Woronoco subsidiaries were merged into existing Berkshire entities, except for Woronoco Insurance Group, Inc., which was acquired by Berkshire Bank and renamed Berkshire Insurance Group, Inc.

SEGMENT REPORTING

Management monitors the revenue streams of the various products and services in evaluating the Company's operations and financial performance. All of the Company's operations are considered by management to be aggregated in one reportable operating segment. Prior to its discontinuation, the operations of Berkshire Hills

Technology, Inc., were evaluated on a stand-alone basis.

REGULATION AND SUPERVISION

The following discussion describes elements of an extensive regulatory framework applicable to savings and loan holding companies and banks and specific information about the Company and its subsidiaries. Federal and state regulation of savings banks and their holding companies is intended primarily for the protection of depositors and the Deposit Insurance Fund rather than for the protection of stockholders and creditors.

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GENERAL

As a savings and loan holding company, Berkshire Hills is required by federal law to file reports with, and otherwise comply with the rules and regulations of, the Office of Thrift Supervision (“OTS”). As a savings bank chartered by the Commonwealth of Massachusetts, Berkshire Bank is subject to extensive regulation, examination and supervision by the Massachusetts Commissioner of Banks (the “Commissioner”), as its primary regulator, and the Federal Deposit Insurance Corporation (“FDIC”), as the deposit insurer. Berkshire Bank is a member of the Federal Home Loan Bank system and, with respect to deposit insurance, of the Bank Insurance Fund managed by the FDIC. Berkshire Bank must file reports with the Commissioner and the FDIC concerning its activities and financial condition in addition to obtaining regulatory approvals prior to entering into certain transactions such as mergers with, or acquisitions of, other savings institutions. The Commissioner and/or the FDIC conduct periodic examinations to test Berkshire Bank’s safety and soundness and compliance with various regulatory requirements. The regulatory structure gives the regulatory authorities extensive discretion in connection with their supervisory and enforcement activities and examination policies, including policies with respect to the classification of assets and the establishment of adequate loan loss reserves for regulatory purposes. Any change in such regulatory requirements and policies, whether by the Commissioner, the FDIC or Congress, could have a material adverse impact on the Company, the Bank and their operations. Certain regulatory requirements applicable to Berkshire Bank and to the Company 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 Berkshire Bank and Berkshire Hills and is qualified in its entirety by reference to the actual laws and regulations.

MASSACHUSETTS BANKING LAWS AND SUPERVISION

Massachusetts savings banks are regulated and supervised by the Massachusetts Commissioner of Banks (the “Commissioner”), who oversees regular bank examinations. The Commissioner’s approval is required to establish or close branches, to merge with another bank, to form a holding company, to issue stock or to undertake many other activities. Any Massachusetts bank that does not operate in accordance with the Commissioner’s regulations, policies and directives may be sanctioned. The Commissioner may suspend or remove directors or officers of a bank who have violated the law, conducted a bank’s business in a manner that is unsafe, unsound or contrary to the depositors’ interests, or been negligent in the performance of their duties. In addition, the Commissioner has the authority to appoint a receiver or conservator if it is determined that the bank is conducting its business in an unsafe or unauthorized manner, and under certain other circumstances.

All Massachusetts-chartered savings banks are required to be members of the Depositors Insurance Fund, a private deposit insurer, which insures all deposits in member banks in excess of FDIC deposit insurance limits. Member banks are required to pay fund assessments. In addition, the Mutual Savings Central Fund acts as a source of liquidity to its members in supplying them with low-cost funds, and purchasing qualifying obligations from them.

Berkshire Bank must adhere to the Massachusetts banking laws, which govern activities such as authorized investments, lending activities and dividend payments. In particular, a Massachusetts savings bank may only pay dividends on its capital stock if such payment would not impair the bank’s capital stock. No dividends may be paid to stockholders of a bank if such dividends would reduce stockholders’ equity of the bank below the amount of the liquidation account required by the Massachusetts conversion regulations. Additionally, the Commissioner may restrict the payment of dividends by a bank if it is determined that such payment would result in safety and soundness concerns.

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 Berkshire 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 assets of 3%. For all other institutions, the minimum leverage capital ratio

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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 a percentage of certain nonfinancial equity investments.

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

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

As a savings and loan holding company regulated by the OTS, Berkshire Hills is not subject to any separate regulatory capital requirements. Berkshire Bank's regulatory capital is included in the Stockholders' Equity note of the Company's financial statements in Item 8 of this report. For the dates shown, Berkshire Bank met each of its capital requirements.

INTERSTATE BANKING AND BRANCHING

Federal law permits a bank, such as Berkshire Bank, to acquire an institution by merger in a state other than Massachusetts unless the other state has opted out. Federal law also authorizes de novo branching into another state if the host state enacts a law expressly permitting out of state banks to establish such branches within its borders. At its New York branches, Berkshire Bank may conduct any activity that is authorized under Massachusetts law that is permissible either for a New York savings bank (subject to applicable federal restrictions) or a New York branch of an out-of-state national bank. The New York State Superintendent of Banks may exercise certain regulatory authority over the Bank's New York branches.

PROMPT CORRECTIVE REGULATORY ACTION

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

The FDIC has adopted regulations to implement the prompt corrective action legislation. An institution is deemed to be "well capitalized" if it has a total risk-based capital ratio of 10% or greater, a Tier 1 risk-based capital ratio of 6% or greater, and a leverage ratio of 5% or greater. An institution is "adequately capitalized" if it has a total risk-based capital ratio of 8% or greater, a Tier 1 risk-based capital ratio of 4% or greater and generally a leverage ratio of 4% or greater. An institution is "undercapitalized" if it has a total risk-based capital ratio of less than 8%, a Tier 1 risk-based capital ratio of less than 4%, or generally a leverage ratio of less than 4% (3% or less for institutions with the highest examination rating). An institution is deemed to be "significantly undercapitalized" if it has a total risk-based capital ratio of less than 6%, a Tier 1 risk-based capital ratio of less than 3%, or a leverage ratio of less than 3%. An institution is considered to be "critically undercapitalized" if it has a ratio of tangible equity (as defined in the regulations) to total assets that is equal to or less than 2%. As of December 31, 2006, Berkshire Bank met the conditions to be classified as a "well capitalized" institution.

“Undercapitalized” banks must adhere to growth, capital distribution (including dividend) and other limitations and are required to submit a capital restoration plan. No institution may make a capital distribution, including payment as a dividend, if it would be “undercapitalized” after the payment. A bank’s compliance with such plans is required to be guaranteed by its parent holding company in an amount equal to the lesser of 5% of the institution’s total assets when deemed undercapitalized or the amount needed to comply with regulatory capital requirements. If an “undercapitalized” bank fails to submit an acceptable plan, it is treated as if it is “significantly undercapitalized.” “Significantly undercapitalized” banks must comply with one or more of a number of additional restrictions, including but not limited to an order by the FDIC to sell sufficient voting stock to become adequately capitalized, requirements to reduce assets

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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.

TRANSACTIONS WITH AFFILIATES

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

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

ENFORCEMENT

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

INSURANCE OF DEPOSIT ACCOUNTS

The Bank’s deposits are insured up to applicable limits by the Deposit Insurance Fund of the Federal Deposit Insurance Corporation. The Deposit Insurance Fund is the successor to the Bank Insurance Fund and the Savings Association Insurance Fund, which were merged in 2006. The Federal Deposit Insurance Corporation recently amended its risk-based assessment system for 2007 to implement authority granted by the Federal Deposit Insurance Reform Act of 2005 (“Reform Act”). Under the revised system, insured institutions are assigned to one of four risk categories based on supervisory evaluations, regulatory capital levels and certain other factors. An institution’s assessment rate depends upon the category to which it is assigned. Risk category I, which contains the least risky depository institutions, is expected to include more than 90% of all institutions. Unlike the other categories, Risk Category I contains further risk differentiation based on the Federal Deposit Insurance Corporation’s analysis of financial ratios, examination component ratings and other information. Assessment rates are determined by the Federal Deposit Insurance Corporation and currently range from five to seven basis points for the healthiest institutions (Risk Category I) to 43 basis points of assessable deposits for the riskiest (Risk Category IV). The Federal Deposit Insurance Corporation may adjust rates uniformly from one quarter to the next, except that no single adjustment can exceed three basis points. No

institution may pay a dividend if in default of the FDIC assessment.

The Reform Act also provided for a one-time credit for eligible institutions based on their assessment base as of December 31, 1996. Subject to certain limitations with respect to institutions that are exhibiting weaknesses, credits can be used to offset assessments until exhausted. The Bank's one-time credit is expected to approximate \$1.1 million. The Reform Act also provided for the possibility that the Federal Deposit Insurance Corporation may pay dividends to insured institutions once the Deposit Insurance fund reserve ratio equals or exceeds 1.35% of estimated insured deposits.

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In addition to the assessment for deposit insurance, institutions are required to make payments on bonds issued in the late 1980s by the Financing Corporation to recapitalize a predecessor deposit insurance fund. This payment is established quarterly and during the calendar year ending December 31, 2006 averaged 1.28 basis points of assessable deposits.

The Reform Act provided the Federal Deposit Insurance Corporation with authority to adjust the Deposit Insurance Fund ratio to insured deposits within a range of 1.15% and 1.50%, in contrast to the prior statutorily fixed ratio of 1.25%. The ratio, which is viewed by the Federal Deposit Insurance Corporation as the level that the fund should achieve, was established by the agency at 1.25% for 2007.

The Federal Deposit Insurance Corporation 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.

Insurance of deposits may be terminated by the Federal Deposit Insurance Corporation 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 the Federal Deposit Insurance Corporation or the Office of Thrift Supervision. The management of the Bank does not know of any practice, condition or violation that might lead to termination of deposit insurance.

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. Berkshire Bank, as a member, is required to acquire and hold shares of capital stock in the Federal Home Loan Bank of Boston. Berkshire Bank was in compliance with this requirement with an investment in Federal Home Loan Bank of Boston stock at year-end 2006 of \$21.8 million.

The Federal Home Loan Banks are required to provide funds for certain purposes including contributing funds for affordable housing programs. These requirements 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. For the years 2006, 2005, 2004, 2003, and 2002, cash dividends from the Federal Home Loan Bank of Boston to Berkshire Bank amounted to approximately \$1.6 million, \$1.3 million, \$0.5 million, \$0.2 million and \$0.3 million, respectively.

HOLDING COMPANY REGULATION

Federal law allows a state savings bank that qualifies as a "Qualified Thrift Lender," discussed below, to elect to be treated as a savings association for purposes of the savings and loan holding company provisions of federal law. Such election allows its holding company to be regulated as a savings and loan holding company by the OTS rather than as a bank holding company by the Federal Reserve Board. Berkshire Bank made such election and the Company is a non-diversified unitary savings and loan holding company within the meaning of federal law. As such, the Company is registered with the OTS and must adhere to the OTS's regulations and reporting requirements. In addition, the OTS may examine, supervise and take enforcement action against the Company and has enforcement authority over the Company and its non-savings institution subsidiaries. Among other things, this authority permits the OTS to restrict or prohibit activities that are determined to be a serious risk to the subsidiary savings institution. Additionally, Berkshire Bank is required to notify the OTS at least 30 days before declaring any dividend to the Company. By regulation, the OTS may restrict or prohibit the Bank from paying dividends.

As a unitary savings and loan holding company, the Company is generally unrestricted under existing laws as to the types of business activities in which it may engage. The Gramm-Leach-Bliley Act of 1999 provided that unitary savings and loan holding companies may only engage in activities permitted to a financial holding company under that legislation and those permitted for a multiple savings and loan holding company. Unitary savings and loan companies existing prior to May 4, 1999, such as the Company, were grandfathered as to the unrestricted activities. The Company would become subject to activities restrictions upon the acquisition of another savings institution that is held as a separate subsidiary.

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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 OTS. In evaluating applications by holding companies to acquire savings associations, the OTS considers 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 funds, the convenience and needs of the community and competitive factors.

To be regulated as a savings and loan holding company by the OTS (rather than as a bank holding company by the Federal Reserve Board), the Bank must qualify as a Qualified Thrift Lender. To qualify as a Qualified Thrift Lender, the Bank must maintain compliance with the test for a “domestic building and loan association,” as defined in the Internal Revenue Code, or with a Qualified Thrift Test. Under the Qualified Thrift Lender Test, a savings institution is required to maintain at least 65% of its “portfolio assets” (total assets less: (1) specified liquid assets up to 20% of total assets; (2) intangibles, including goodwill; and (3) the value of property used to conduct business) in certain “qualified thrift investments” (primarily residential mortgages and related investments, including certain mortgage-backed and related securities) in at least 9 months out of each 12-month period. At year-end 2006, Berkshire Bank maintained 77% of its portfolio assets in qualified thrift investments. Berkshire Bank also met the QTL test in each of the prior twelve months and, therefore, met the QTL Test.

Acquisition of the Company. Under the Federal Change in Bank Control Act, a notice must be submitted to the OTS if any person (including a company), or group acting in concert, seeks to acquire “control” of a savings and loan holding company. Under certain circumstances, 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 OTS 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 the following: any company may become a bank holding company; any bank holding company acquires 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 merges with another bank holding company. The Company is a bank holding company for purposes of Massachusetts law. The Company has no current plan or arrangement to acquire ownership or control, directly or indirectly, of 25% or more of the voting stock of another banking institution.

BERKSHIRE MUNICIPAL BANK

In 2005, Berkshire Bank established a new subsidiary, Berkshire Municipal Bank, as a state chartered limited purpose commercial bank in New York, to accept deposits of municipalities and other governmental entities in the State of New York. Berkshire 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.

FEDERAL AND MASSACHUSETTS INCOME TAXATION

The Company and the Bank report their income on a calendar year basis using the accrual method of accounting. The federal income tax laws apply to the Company and Berkshire Bank in the same manner as to other corporations with some exceptions, including particularly Berkshire Bank's reserve for bad debts discussed below. 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.

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Prior to 1995, the Bank was permitted to use certain favorable provisions to calculate deductions from taxable income for annual additions to its bad debt reserve. Federal legislation in 1996 repealed this reserve method and required savings institutions to recapture or take into income certain portions of their accumulated bad debt reserves. Approximately \$844 thousand of the Bank's accumulated bad debt reserves will not be recaptured into taxable income unless the Bank makes a "nondividend distribution" to the Company, including distributions in excess of the Bank's current and accumulated earnings and profits. In the event of a nondividend distribution, approximately 150% of the amount of the distribution up to \$844 thousand would be includable in income for federal income tax purposes, resulting in an increase in tax of \$346 thousand assuming a marginal federal and state tax rate of 41%. The Bank does not intend to pay dividends that would result in a recapture of any portion of its bad debt reserves.

The Massachusetts excise tax rate for savings banks is currently 10.5% of federal taxable income, adjusted for certain items. Taxable income includes gross income as defined under the Internal Revenue Code, plus interest from municipal obligations of any state, less deductions, but not the credits, allowable under the provisions of the Internal Revenue Code, except no deduction is allowed for bonus depreciation or state income taxes. Carryforwards and carrybacks of net operating losses are not allowed. A qualifying limited purpose corporation is generally entitled to special tax treatment as a "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.

ITEM 1A. RISK FACTORS

An investment in our common stock involves risk. You should carefully consider the risks described below and all other information contained in this annual report on Form 10-K before you decide to buy our common stock. It is possible that risks and uncertainties not listed below may arise or become material in the future and affect our business.

Lending

Our emphasis on commercial lending may expose us to increased lending risks, which could hurt our profits.

Our commercial loan portfolio, which consists of commercial real estate loans, construction and development loans and commercial business loans has increased from \$569 million at year-end 2005 to \$757 million at year-end 2006. A significant portion of this growth has included construction and development loans that may have higher risk, and loans in new markets, where the Company has less historic knowledge of the market. Also, commercial loans are more sensitive to economic downturns and the possible impact of higher interest rates. Such sensitivity includes potentially higher default rates and possible diminution of collateral values. Some of the growth in commercial loans is also attributable to larger loan sizes and larger relationship exposures, which can have a greater impact on profits in the event of adverse loan performance. Commercial lending also involves more development financing, which is dependent on the future success of new operations. Additionally, the Company has expanded its commercial lending team to accomplish this growth, and this has the potential to increase risk relating to underwriting and administrative controls as new lenders are integrated into the control environment. These and other factors may result in errors in judging the collectibility of commercial loans, which may lead to additional provisions or charge-offs. Construction lending depends largely upon the accuracy of the initial estimate of the property's value at completion of construction and the estimated cost (including interest) of construction. During the construction phase, a number of factors could result in delays and cost overruns. If the estimate of construction costs proves to be inaccurate, the Company may be required to advance funds beyond the amount originally committed to permit completion of the building. If the estimate of value proves to be inaccurate, the Company may be confronted, at or before the maturity of the loan, with a building having a value which is insufficient to assure full repayment. If the Company is forced to foreclose on a building before or at completion due to a default, there can be no assurance that it will be able to recover all of the

unpaid balance of, and accrued interest on, the loan as well as related foreclosure and holding costs.

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 to provide for loans in our portfolio that may not be repaid in their entirety. We believe that our allowance for loan losses is maintained at a level adequate to absorb probable losses inherent in our loan portfolio as of the corresponding balance sheet date. However, our allowance for loan losses may not be sufficient to cover actual loan losses, and future provisions for loan losses could materially adversely affect our operating results.

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In evaluating the adequacy of our allowance for loan losses, we consider numerous quantitative factors, including our historical charge-off experience, growth of our loan portfolio, changes in the composition of our loan portfolio and the volume of delinquent and criticized loans. In addition, we use information about specific borrower situations, including their financial position and estimated collateral values, to estimate the risk and amount of loss for those borrowers. Finally, we also consider many qualitative factors, including general and economic business conditions, the local residential real estate market, the interest rate environment, fiscal and monetary policy of the United States government, energy prices, commercial real estate conditions, the duration of the current business cycle, current general market collateral valuations, trends apparent in any of the factors we take into account and other matters, which are by nature more subjective and fluid. Our estimates of the risk of loss and amount of loss on any loan are complicated by the significant uncertainties surrounding our borrowers' abilities to successfully execute their business models through changing economic environments, competitive challenges and other factors. Because of the degree of uncertainty and susceptibility of these factors to change, our actual losses may vary from our current estimates.

Based on our review of the above-mentioned factors, we recorded a provision for loan losses of \$7.9 million for the year ended December 31, 2006 to bring our allowance for loan losses at year-end 2006 to \$19.4 million, which was 1.14% of total loans. 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.

A downturn in the local economy or a decline in real estate values could hurt our profits.

Approximately 77% of our loans were secured by real estate as of year-end 2006. In recent years, there has been a significant increase in real estate values in our market area. A decline in real estate values could expose us to a greater risk of loss. Because the majority of our borrowers and depositors are individuals and businesses located and doing business in our market areas, our success depends to a significant extent upon economic conditions in our market areas. Adverse economic conditions in our market areas could reduce our growth rate, affect the ability of our customers to repay their loans and generally effect our financial condition and results of operations. Conditions such as inflation, recession, unemployment, high interest rates, short money supply, scarce natural resources, international disorders, terrorism and other factors beyond our control may adversely affect our profitability. We are less able than a larger institution to spread the risks of unfavorable local economic conditions across a large number of diversified economies. Any sustained period of increased payment delinquencies, foreclosures or losses caused by adverse market or economic conditions in our market areas could adversely affect the value of our assets, revenues, results of operations and financial condition. Moreover, we cannot give any assurance we will benefit from any market growth or favorable economic conditions in our primary market areas if they do occur.

Growth

Our geographic expansion and growth, if not successful, could negatively impact earnings.

We plan to achieve significant growth both organically and through acquisitions. We have recently expanded into new geographic markets and anticipate that we will expand into additional new geographic markets as we transform ourselves into a regional bank. The success of this expansion will depend on our ability to continue to maintain and develop an infrastructure appropriate to support such growth. Also, our success will depend on the acceptance by customers of us and our services in these new markets and, in the case of expansion through acquisitions, the success of acquisitions depends on many factors, including the long-term retention of key personnel and acquired customer relationships. The profitability of our expansion strategy also will depend on whether the income we generate in the new markets will offset the increased expenses of operating a larger entity with increased personnel, more branch

locations and additional product offerings. We expect that it may take a period of time before certain of our new branches can become profitable, especially in areas in which we do not have an established physical presence. During this period, operating these new branches may negatively impact net income. Additionally, in connection with our expansion, we will need to increase our operational and financial procedures, systems and controls. If we have difficulty in doing so, it could harm our business, results of operations and financial condition.

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Competition from financial institutions and other financial service providers may adversely affect our growth and profitability.

The banking business is highly competitive and we experience competition in each of our markets from many other financial institutions. We compete with commercial banks, credit unions, savings and loan associations, mortgage banking firms, consumer finance companies, securities brokerage firms, insurance companies, money market funds, and other mutual funds, as well as other super-regional, national and international financial institutions that operate offices in our primary market areas and elsewhere.

We compete with these institutions both in attracting deposits and in making loans. This competition has made it more difficult for us to make new loans and has occasionally forced us to offer higher deposit rates. Price competition for loans and deposits might result in our earning less on our loans and paying more on our deposits, which reduces net interest income. Many of our competitors are larger financial institutions. While we believe we can and do successfully compete with these other financial institutions in our primary markets, we may face a competitive disadvantage as a result of our smaller size, smaller resources and smaller lending limits, lack of geographic diversification and inability to spread our marketing costs across a broader market.

Our continued pace of growth may require us to raise additional capital in the future, but that capital may not be available when it is needed.

We are required by federal and state regulatory authorities to maintain adequate levels of capital to support our operations. We may at some point need to raise additional capital to support our 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. Accordingly, if needed, we cannot assure you of our ability to raise additional capital on terms acceptable to us. If we cannot raise additional capital when needed, our ability to execute our strategic plan, which includes further expanding our operations through internal growth and acquisitions could be materially impaired.

Interest Rates

Fluctuations in interest rates could reduce our profitability and affect the value of our assets.

Like other financial institutions, we are subject to interest rate risk. Our primary source of income is net interest income, which is the difference between interest earned on loans and investments and the interest paid on deposits and borrowings. We expect that we will periodically experience imbalances in the interest rate sensitivities of our assets and liabilities and the relationships of various interest rates to each other. Over any defined period of time, our interest-earning assets may be more sensitive to changes in market interest rates than our interest-bearing liabilities, or vice versa. In addition, the individual market interest rates underlying our loan and deposit products (*e.g.*, prime) may not change to the same degree over a given time period. In any event, if market interest rates should move contrary to our position, our earnings may be negatively affected. In addition, loan volume and quality and deposit volume and mix can be affected by market interest rates. Changes in levels of market interest rates could materially adversely affect our net interest spread, asset quality, origination volume and overall profitability.

Interest rates have recently been at historically low levels. However, since June 30, 2004, the U.S. Federal Reserve has increased its target for the federal funds rate seventeen times, from 1.00% to 5.25%. While these short-term market interest rates (which we use as a guide to price our deposits) have increased, longer-term market interest rates (which we use as a guide to price our longer-term loans) have not. This “flattening” of the market yield curve has had a negative impact on our interest rate spread and net interest margin to date. If short-term interest rates continue to rise, and if rates on our deposits and borrowings continue to reprice upwards faster than the rates on our long-term loans and

investments, we would experience further compression of our interest rate spread and net interest margin, which would have a negative effect on our net interest income and hence our profitability.

We principally manage interest rate risk by managing our volume and mix of our earning assets and funding liabilities. In a changing interest rate environment, we may not be able to manage this risk effectively. If we are unable to manage interest rate risk effectively, our business, financial condition and results of operations could be materially harmed.

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Changes in the level of interest rates also may negatively affect our ability to originate real estate loans, the value of our assets and our ability to realize gains from the sale of our assets, all of which ultimately affect our earnings.

Our investment portfolio includes securities that are sensitive to interest rates and variations in interest rates may adversely impact our profitability.

Our securities portfolio is comprised of mortgage-backed securities, which are insured or guaranteed by U.S. government agencies or government-sponsored enterprises, and U.S. government securities, as well as municipal bonds and obligations and other bonds. These securities are sensitive to interest rate fluctuations. The unrealized gains or losses in our available-for-sale portfolio are reported as a separate component of stockholders' equity until realized upon sale. As a result, future interest rate fluctuations may impact stockholders' equity, causing material fluctuations from quarter to quarter. Failure to hold our securities until maturity or until market conditions are favorable for a sale could adversely affect our financial condition, profitability and prospects.

Liquidity

Our wholesale funding sources may prove insufficient to replace deposits at maturity and support our 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. As we continue to grow, we are likely to become more dependent on these sources, which include Federal Home Loan Bank advances and proceeds from the sale of loans. At December 31, 2006, we had approximately \$330 million of FHLBB advances outstanding. 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 interest rates. 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.

Our ability to service our debt, pay dividends and otherwise pay our obligations as they come due is substantially dependent on capital distributions from Berkshire Bank, and these distributions are subject to regulatory limits and other restrictions.

A substantial source of our income from which we service our debt, pay our obligations and from which we can pay dividends is the receipt of dividends from Berkshire Bank. The availability of dividends from Berkshire Bank is limited by various statutes and regulations. It is possible, depending upon the financial condition of Berkshire Bank, and other factors, that the applicable regulatory authorities could assert that payment of dividends or other payments is an unsafe or unsound practice. If Berkshire 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 Berkshire Bank would adversely affect our business, financial condition, results of operations and prospects.

Operational

We operate in a highly regulated environment and may be adversely affected by changes in laws and regulations.

Berkshire Hills Bancorp is subject to extensive regulation, supervision and examination by the Office of Thrift Supervision, its chartering authority, and Berkshire Bank is subject to extensive supervision and examination by the Massachusetts Division of Banks, its chartering authority, and the Federal Deposit Insurance Corporation, as insurer of Berkshire Bank's deposits. Such regulations and supervision govern the activities in which an institution and its

holding company may engage, and are intended primarily for the protection of the insurance fund and depositors. Regulatory authorities have extensive discretion in their supervisory and enforcement activities, including the imposition of restrictions on operations, the classification of assets and determination of the level of allowance for loan losses. Any change in such regulation and oversight, whether in the form of regulatory policy, regulations, legislation or supervisory action may have a material impact on our operations. Berkshire Hills Bancorp primarily depends on Berkshire Bank for dividends as a source of funds to service its indebtedness and to pay dividends to stockholders. Such dividends may be restricted or prohibited by regulatory authorities.

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We are subject to security and operational risks relating to our use of technology that could damage our reputation and our business.

Security breaches in our internet banking activities could expose us to possible liability and damage our reputation. Any compromise of our security also could deter customers from using our internet banking services that involve the transmission of confidential information. We rely on standard internet security systems to provide the security and authentication necessary to effect secure transmission of data. These precautions may not protect our systems from compromises or breaches of our security measures that could result in damage to our reputation and our business. Additionally, our data processing and telecommunications utilize third party software, hardware, and support. If our third party providers encounter difficulties or if we have difficulty in communicating with third parties, it will significantly affect our ability to adequately process and account for customer transactions, which would significantly affect our business operations.

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

Our acquisitions have resulted in significant goodwill, which if it becomes impaired would be required to be written down, which would negatively impact earnings.

We acquired Woronoco Bancorp, Inc. in 2005, and have purchased insurance and financial planning businesses in the last two years, including the five insurance agencies we acquired on October 31, 2006. We will pursue additional opportunities for acquisitions in the future, including acquisitions in adjacent states. The success of acquisitions depends on many factors, including the long term retention of key personnel and acquired customer relationships. We recorded goodwill and other intangible assets in conjunction with the Woronoco Bancorp acquisition and in connection with the insurance agency acquisitions, and such assets may be recorded in future acquisitions. If these assets were to become impaired, we would be required to write them down.

Trading

The trading history of our common stock is characterized by low trading volume. The value of your investment may be subject to sudden decreases due to the volatility of the price of our common stock.

Our common stock trades on The NASDAQ Global Select Market. The average daily trading volume of our common stock was approximately 29,400 shares. We cannot predict the extent to which investor interest in us will lead to a more active trading market in our common stock or how liquid that market might become. A public trading market having the desired characteristics of depth, liquidity and orderliness depends upon the presence in the marketplace of willing buyers and sellers of our common stock at any given time, which presence is dependent upon the individual decisions of investors, over which we have no control.

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The market price of our common stock may be highly volatile and subject to wide fluctuations in response to numerous factors, including, but not limited to, the factors discussed in other risk factors and the following:

- actual or anticipated fluctuations in our operating results;
- changes in interest rates;
- changes in the legal or regulatory environment in which we operate;
- press releases, announcements or publicity relating to us or our competitors or relating to trends in our industry;
- changes in expectations as to our future financial performance, including financial estimates or recommendations by securities analysts and investors;
- future sales of our common stock;
- changes in economic conditions in our marketplace, general conditions in the U.S. economy, financial markets or the banking industry, and
- other developments affecting our competitors or us.

These factors may adversely affect the trading price of our common stock, regardless of our actual operating performance, and could prevent you from selling your common stock at the price you desire. In addition, the stock markets, from time to time, experience extreme price and volume fluctuations that may be unrelated or disproportionate to the operating performance of companies. These broad fluctuations may adversely affect the market price of our common stock, regardless of our trading performance. In the past, stockholders often have brought securities class action litigation against a company following periods of volatility in the market price of their securities. We may 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.

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ITEM 2. PROPERTIES

The Company's headquarters is located in an owned facility located in Pittsfield, Massachusetts. At year-end 2006, the Company entered into a long term lease for new corporate headquarters to be occupied in 2007 in Pittsfield. The current headquarters will be used for the expansion of operations. At year-end 2006, the Company occupied a total of 47 facilities, of which 17 were owned by the Company and 30 were leased, within its primary market areas of Berkshire County, Massachusetts; Pioneer Valley, Massachusetts; and Capital Region, Northeastern New York. In 2006, the Company opened 3 new branches in New York, bringing the total full service branch count to 27, of which 14 operate in premises owned by the Company. The Company also announced 4 new branch locations for 2007, all of which will operate in facilities leased by the Company. Additionally, with the acquisition of the five insurance agencies in October of 2006, the Company now leases 10 buildings throughout the Pioneer Valley and Berkshire County in relation to these insurance agencies. Also at year-end 2006, the Company occupied 6 additional office properties, of which 3 were leased and 3 were owned. The Company is increasing its workspace capacity in proportion with its current expansion and growth plans to adequately fill its needs.

ITEM 3. LEGAL PROCEEDINGS

At December 31, 2006, neither the Company nor the Bank were 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. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of security holders during the fourth quarter of 2006.

Index**PART II****ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED SHAREHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES**

Market Information

The common shares of Berkshire Hills trade on the NASDAQ Global Select Market under the symbol "BHLB". Since its initial public offering, the Company's shares had traded on the American Stock Exchange under the symbol "BHL". The Company's shares began trading on the NASDAQ Global Select Market on October 25, 2005.

The following table sets forth the quarterly high and low sales price information and dividends declared per share of common stock in 2006 and 2005. On March 7, 2007, the closing market price of Berkshire Hills common stock was \$33.52. Berkshire Hills increased its quarterly dividend to \$0.14 per share in the third quarter of 2005.

	High	Low	Dividends Declared
2006			
First quarter	\$ 36.08	\$ 32.37	\$ 0.14
Second quarter	36.39	32.77	0.14
Third quarter	38.44	33.46	0.14
Fourth quarter	39.67	33.08	0.14
2005			
First quarter	\$ 37.64	\$ 33.40	\$ 0.12
Second quarter	34.90	30.97	0.12
Third quarter	35.20	31.90	0.14
Fourth quarter	35.57	31.75	0.14

Holders

The Company had approximately 2,029 holders of record of common stock at March 8, 2007.

Dividends

The principal source of the Company's cash reserves is dividends received from the Bank and, in the future from Berkshire Insurance Group, together with proceeds from stock option exercises. In addition, the Company has issued subordinated debt to its wholly owned subsidiary grantor trust. The banking regulators may prohibit banks and holding companies from paying dividends that would constitute an unsafe or unsound banking practice, or which would reduce the amount of its capital below that necessary to minimum applicable regulatory capital requirements. The Company is subject to the requirements of Delaware law, which generally limits dividends to an amount equal to the excess of the net assets of the Company (the amount by which total assets exceed total liabilities) over its statutory capital or, if there is no excess, to its net profits for the current and/or immediately preceding fiscal year. See also the Stockholders' Equity note in the financial statements in Item 8 of this Form 10-K.

Securities Authorized for Issuance under Equity Compensation Plans

Information regarding securities authorized for issuance under equity compensation plans appears in Part III, Item 12 of this report.

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

No unregistered securities were sold by the Company within the last three years. Registered securities were exchanged as part of the consideration for the acquisition of Woronoco Bancorp.

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The following table provides information with respect to any purchase 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 during the fourth quarter of 2006.

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, 2006	-	\$ -	-	300,000
November 1-30, 2006	-	-	-	300,000
December 1-31, 2006	15,000	34.66	15,000	285,000
Total	15,000	\$ 34.66	15,000	285,000

On February 23, 2006, the Company authorized the purchase of up to 300,000 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. As of December 31, 2006, there were 15,000 shares repurchased under this plan and 285,000 shares remained available to be repurchased. The Company has no plans that it has elected to terminate prior to expiration or under which it does not intend to make further purchases.

Index**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 NASDAQ Composite Index, the SNL \$1 Billion - \$5 Billion Thrift Index, and the SNL All Bank and Thrift Index. Total stockholder return is measured by dividing total dividends (assuming dividend reinvestment) for the measurement period plus share price change for a period by the share price at the beginning of the measurement period. The Company's cumulative stockholder return over a five-year period is based on an initial investment of \$100 on December 31, 2001.

The Company has previously used the SNL \$1 Billion - \$5 Billion Thrift Index to compare its stock performance to a peer index. Due to the Company's growth and transformation into a more diversified regional financial institution with a more bank-like balance sheet, the Company has determined that a more appropriate index to compare to its stock performance is the SNL Bank and Thrift Index. Both of these indices are shown in the performance graph, and in the future the SNL Bank and Thrift Index will be shown as the banking industry comparative index.

Comparison of Five Year Cumulative Total Return Among Berkshire Hills Bancorp, NASDAQ Composite Index, SNL \$1B - \$5B Thrift Index, and SNL Bank and Thrift Index

<i>Index</i>	<i>Period Ending</i>					
	12/31/01	12/31/02	12/31/03	12/31/04	12/31/05	12/31/06
Berkshire Hills Bancorp, Inc.	100.00	118.72	185.60	193.04	176.77	179.44
NASDAQ Composite	100.00	68.76	103.67	113.16	115.57	127.58
SNL \$1B-\$5B Thrift Index	100.00	128.06	192.07	217.67	215.77	248.17
SNL Bank and Thrift Index	100.00	93.96	127.39	142.66	144.89	169.30

Index**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. Financial data includes the impact of the acquisition of Woronoco Bancorp, Inc. in 2005 and five affiliated insurance agencies in 2006.

	At or For the Years Ended December 31,				
<i>(Dollars in thousands, except per share data)</i>	2006	2005	2004	2003	2002
Selected Financial Data:					
Total assets	\$ 2,149,642	\$ 2,035,553	\$ 1,310,115	\$ 1,218,548	\$ 1,045,947
Securities	234,174	420,320	414,363	359,294	226,919
Loans, net	1,679,617	1,407,229	818,842	783,258	712,714
Goodwill and intangibles	121,341	99,616	7,254	10,233	10,436
Deposits	1,521,938	1,371,218	845,789	830,244	782,360
Borrowings and subordinated debentures	360,469	412,917	327,926	251,465	133,702
Total stockholders' equity	258,161	246,066	131,736	123,175	120,569
Selected Operating Data:					
Total interest and dividend income	\$ 118,051	\$ 87,732	\$ 61,081	\$ 56,308	\$ 64,128
Total interest expense	57,811	36,115	20,724	18,742	23,428
Net interest income	60,240	51,617	40,357	37,566	40,700
Provision for loan losses	7,860	1,313	1,565	1,460	6,180
Service charge and fee income	13,539	9,373	5,493	5,023	4,659
All other non-interest income	(1,491)	5,550	2,271	1,425	1,768
Total non-interest expense	48,868	48,998	28,977	28,243	37,279
Provision for income taxes	4,668	8,003	5,639	5,161	885
Net income (loss) from discontinued operations	371	-	(431)	(185)	(686)
Net income	\$ 11,263	\$ 8,226	\$ 11,509	\$ 8,965	\$ 2,097
Dividends per share	\$ 0.56	\$ 0.52	\$ 0.48	\$ 0.48	\$ 0.48
Basic earnings per share:					
Continuing operations	\$ 1.28	\$ 1.16	\$ 2.26	\$ 1.74	\$ 0.52
Discontinued operations	0.04	-	(0.08)	(0.04)	(0.13)
Total	\$ 1.32	\$ 1.16	\$ 2.18	\$ 1.70	\$ 0.39
Diluted earnings per share:					
Continuing operations	\$ 1.25	\$ 1.10	\$ 2.08	\$ 1.60	\$ 0.47
Discontinued operations	0.04	-	(0.07)	(0.03)	(0.11)
Total	\$ 1.29	\$ 1.10	\$ 2.01	\$ 1.57	\$ 0.36
Average shares outstanding:					
Basic	8,538	7,122	5,284	5,266	5,435

Diluted	8,730	7,503	5,731	5,703	5,867
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At or For the Years Ended December 31,

(Dollars in thousands, except per share data)

2006 2005 2004 2003 2002

Selected Operating Ratios and Other Data:**Performance Ratios:**

Return on average assets	0.53%	0.47%	0.89%	0.80%	0.20%
Return on average equity	4.40	4.19	9.06	7.28	1.54
Interest rate spread	2.81	3.00	3.10	3.29	3.70
Net interest margin	3.24	3.33	3.37	3.61	4.18
Non-interest income/total net revenue	16.67	22.43	16.13	14.65	13.64
Non-interest expense/average assets	2.31	2.81	2.25	2.53	3.54
Dividend payout ratio	42.92	45.06	22.02	28.24	123.08

Bank Capital Ratios:

Tier 1 capital to average assets	7.69	7.79	8.08	7.87	8.60
Total capital to risk-weighted assets	10.27	11.12	12.69	12.55	13.48
Shareholders' equity/total assets	12.01	12.09	10.06	10.11	11.53

Asset Quality Ratios:

Nonperforming loans/total loans	0.45	0.08	0.14	0.40	0.52
Nonperforming assets/total assets	0.35	0.06	0.09	0.26	0.36
Net loans charged-off/average total loans	0.07	0.08	0.15	0.35	0.87
Allowance for loan losses/total loans	1.14	0.92	1.13	1.13	1.43
Allowance for loan losses/nonperforming loans	2.55 x	10.96 x	8.11 x	2.80 x	2.76 x

Share Data:

Book value per share	\$ 29.63	\$ 28.81	\$ 22.43	\$ 20.87	\$ 19.71
Market price at year end	\$ 33.46	\$ 33.50	\$ 37.15	\$ 36.20	\$ 23.55

Note: All performance ratios are based on average balance sheet amounts where applicable.

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

GENERAL

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

CRITICAL ACCOUNTING POLICIES

The Company's significant accounting policies are described in Note 1 to the consolidated financial statements. Please see those policies in conjunction with this discussion.

Critical accounting policies are those that are reflective of significant judgments and uncertainties, and could potentially result in materially different results under different assumptions and conditions. Management believes that our most critical accounting policies, which involve the most complex or subjective decisions or assessments, are as follows:

Allowance for Loan Losses. Arriving at an appropriate level of allowance for loan losses involves a high degree of judgment. The allowance for loan losses provides for probable estimable losses based upon evaluations of known and inherent risks in the loan portfolio. Management uses historical information, as well as current economic data, to assess the adequacy of the allowance for loan losses as it is affected by changing economic conditions and various external factors, which may impact the portfolio in ways currently unforeseen. Although we believe that we use the appropriate information available to establish the allowance for loan losses, future additions to the allowance may be necessary if certain future events occur that cause actual results to differ from the assumptions used in making the evaluation. For

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example, a downturn in the local economy could cause an increase in non-performing loans. Additionally, a decline in real estate values could cause some of our loans to become inadequately collateralized. In either case, this may require us to increase our provisions for loan losses, which would negatively impact earnings. The allowance for loan losses discussion in Item 1 provides additional information about the allowance.

Income Taxes. Management considers accounting for income taxes as a critical accounting policy due to the subjective nature of certain estimates that are involved in the calculation and evaluation of the timing and recognition of resulting tax liabilities and assets. Management uses the asset liability method of accounting for income taxes in which deferred tax assets and liabilities are established for the temporary differences between the financial reporting basis and the tax basis of the Company's assets and liabilities. Management must assess the realizability of the deferred tax asset, including the carry forward of a portion of the charitable contribution, and to the extent that management believes that recovery is not likely, a valuation allowance is established. Adjustments to increase or decrease the valuation allowance are generally charged or credited, respectively, to income tax expense.

Goodwill and Identifiable Intangible Assets. In conjunction with the acquisition of Woronoco Bancorp in 2005, goodwill was recorded as an intangible asset equal to the excess of the purchase price over the estimated fair value of the net assets acquired. Other intangible assets were recorded for the fair value of core deposits and non-compete agreements. Goodwill and intangible assets were recorded for the purchase of insurance agencies in 2006. The valuation techniques used by management to determine the carrying value of assets acquired in the acquisition and the estimated lives of identifiable intangible assets involve estimates for discount rates, projected future cash flows and time period calculations, all of which are susceptible to change based on changes in economic conditions and other factors. Future events or changes in the estimates which were used to determine the carrying value of goodwill and identifiable intangible assets or which otherwise adversely affects their value or estimated lives could have a material adverse impact on future results of operations.

SUMMARY - 2006

Net income increased by 37% to \$11.3 million in 2006, compared to \$8.2 million in the prior year. Net income per diluted share increased by 17% to \$1.29 in 2006 from \$1.10 in 2005. Earnings growth included the benefit of organic growth and expansion, along with the acquisition of Woronoco Bancorp in June 2005. All earnings per share references are to diluted shares, and also reflect the additional shares issued for the Woronoco acquisition.

Financial highlights in 2006 included:

·	44% growth in fee income
·	20% growth in total loans
·	33% growth in total commercial loans
·	11% growth in total deposits

Other highlights in 2006 included: