

BERKSHIRE HILLS BANCORP INC

Form 10-Q

August 09, 2018

Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended: June 30, 2018

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

For the transition period from _____ to _____

Commission File Number: 001-15781

BERKSHIRE HILLS BANCORP, INC.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

04-3510455

(I.R.S. Employer Identification No.)

60 State Street, Boston, Massachusetts

(Address of principal executive offices)

02109

(Zip Code)

Registrant's telephone number, including area code: (800) 773-5601, ext. 133773

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

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

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

Large accelerated filer Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

Emerging growth company

Table of Contents

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act)

Yes No

The Registrant had 45,423,719 shares of common stock, par value \$0.01 per share, outstanding as of August 7, 2018.

Table of Contents

BERKSHIRE HILLS BANCORP, INC.
FORM 10-Q

INDEX

| | Page |
|---|-----------|
| <u>PART I. FINANCIAL INFORMATION</u> | |
| <u>Item 1. Consolidated Financial Statements (unaudited)</u> | |
| <u>Consolidated Balance Sheets as of June 30, 2018 and December 31, 2017</u> | <u>4</u> |
| <u>Consolidated Statements of Income for the Three and Six Months Ended June 30, 2018 and 2017</u> | <u>5</u> |
| <u>Consolidated Statements of Comprehensive Income for the Three and Six Months Ended June 30, 2018 and 2017</u> | <u>6</u> |
| <u>Consolidated Statements of Changes in Shareholders' Equity for the Six Months Ended June 30, 2018 and 2017</u> | <u>7</u> |
| <u>Consolidated Statements of Cash Flows for the Six Months Ended June 30, 2018 and 2017</u> | <u>8</u> |
| Notes to Consolidated Financial Statements | |
| <u>Note 1 Basis of Presentation</u> | <u>10</u> |
| <u>Note 2 Trading Security</u> | <u>13</u> |
| <u>Note 3 Securities Available for Sale, Held to Maturity, and Marketable Equity Securities</u> | <u>14</u> |
| <u>Note 4 Loans</u> | <u>19</u> |
| <u>Note 5 Loan Loss Allowance</u> | <u>34</u> |
| <u>Note 6 Deposits</u> | <u>41</u> |
| <u>Note 7 Borrowed Funds</u> | <u>41</u> |
| <u>Note 8 Capital Ratios and Shareholders' Equity</u> | <u>43</u> |
| <u>Note 9 Earnings per Share</u> | <u>48</u> |
| <u>Note 10 Stock-Based Compensation Plans</u> | <u>49</u> |
| <u>Note 11 Derivative Financial Instruments and Hedging Activities</u> | <u>50</u> |
| <u>Note 12 Fair Value Measurements</u> | <u>57</u> |
| <u>Note 13 Net Interest Income after Provision for Loan Losses</u> | <u>66</u> |
| <u>Note 14 Revenue</u> | <u>67</u> |
| <u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u> | <u>69</u> |
| <u>Selected Financial Data</u> | <u>69</u> |
| <u>Average Balances and Average Yields/Rates</u> | <u>71</u> |
| <u>Non-GAAP Financial Measures</u> | <u>73</u> |
| <u>Item 3. Quantitative and Qualitative Disclosures about Market Risk</u> | <u>84</u> |

Item 4. Controls and Procedures

85

2

Table of Contents

PART II. OTHER INFORMATION

| | | |
|-----------------|--|-----------|
| <u>Item 1.</u> | <u>Legal Proceedings</u> | <u>86</u> |
| <u>Item 1A.</u> | <u>Risk Factors</u> | <u>87</u> |
| <u>Item 2.</u> | <u>Unregistered Sales of Equity Securities and Use of Proceeds</u> | <u>88</u> |
| <u>Item 3.</u> | <u>Defaults Upon Senior Securities</u> | <u>88</u> |
| <u>Item 4.</u> | <u>Mine Safety Disclosures</u> | <u>88</u> |
| <u>Item 5.</u> | <u>Other Information</u> | <u>88</u> |
| <u>Item 6.</u> | <u>Exhibits</u> | <u>89</u> |
| | <u>Signatures</u> | <u>90</u> |

Table of Contents

PART I

ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

BERKSHIRE HILLS BANCORP, INC.
CONSOLIDATED BALANCE SHEETS

| (In thousands, except share data) | June 30, 2018 | December 31, 2017 |
|--|------------------|----------------------|
| Assets | | |
| Cash and due from banks | \$90,964 | \$91,122 |
| Short-term investments | 48,093 | 157,641 |
| Total cash and cash equivalents | 139,057 | 248,763 |
| Trading security, at fair value | 11,483 | 12,277 |
| Marketable equity securities, at fair value | 59,726 | 45,185 |
| Securities available for sale, at fair value | 1,393,250 | 1,380,914 |
| Securities held to maturity (fair values of \$377,486 and \$405,276) | 379,905 | 397,103 |
| Federal Home Loan Bank stock and other restricted securities | 75,530 | 63,085 |
| Total securities | 1,919,894 | 1,898,564 |
| Loans held for sale, at fair value | 149,182 | 153,620 |
| Commercial real estate loans | 3,319,323 | 3,264,742 |
| Commercial and industrial loans | 1,875,118 | 1,803,939 |
| Residential mortgages | 2,397,192 | 2,102,807 |
| Consumer loans | 1,118,333 | 1,127,850 |
| Total loans | 8,709,966 | 8,299,338 |
| Less: Allowance for loan losses | (55,925) | (51,834) |
| Net loans | 8,654,041 | 8,247,504 |
| Premises and equipment, net | 112,217 | 109,352 |
| Goodwill | 519,128 | 519,287 |
| Other intangible assets | 35,838 | 38,296 |
| Cash surrender value of bank-owned life insurance policies | 193,121 | 191,221 |
| Deferred tax assets, net | 53,679 | 47,061 |
| Other assets | 125,806 | 117,083 |
| Total assets | \$11,901,963 | \$11,570,751 |
| Liabilities | | |
| Demand deposits | \$1,553,039 | \$1,606,656 |
| NOW and other deposits | 858,014 | 734,558 |
| Money market deposits | 2,619,943 | 2,776,157 |
| Savings deposits | 747,722 | 741,954 |
| Time deposits | 3,060,034 | 2,890,205 |
| Total deposits | 8,838,752 | 8,749,530 |
| Short-term debt | 1,002,000 | 667,300 |
| Long-term Federal Home Loan Bank advances | 272,342 | 380,436 |
| Subordinated borrowings | 89,429 | 89,339 |
| Total borrowings | 1,363,771 | 1,137,075 |
| Other liabilities | 183,199 | 187,882 |
| Total liabilities | \$10,385,722 | \$10,074,487 |
| (continued) | | |

Edgar Filing: BERKSHIRE HILLS BANCORP INC - Form 10-Q

| | June 30, 2018 | December 31, 2017 |
|--|------------------|----------------------|
| Shareholders' equity | | |
| Preferred Stock (Series B non-voting convertible preferred stock - \$0.01 par value; 2,000,000 shares authorized, 521,607 shares issued and outstanding in 2018; 1,000,000 shares authorized, 521,607 shares issued and outstanding in 2017) | 40,633 | 40,633 |
| Common stock (\$.01 par value; 100,000,000 shares authorized and 46,211,894 shares issued and 45,420,276 shares outstanding in 2018; 50,000,000 shares authorized, 46,211,894 shares issued and 45,290,433 shares outstanding in 2017) | 460 | 460 |
| Additional paid-in capital - common stock | 1,244,691 | 1,242,487 |
| Unearned compensation | (10,096 |) (6,531) |
| Retained earnings | 283,256 | 239,179 |
| Accumulated other comprehensive (loss) income | (21,266 |) 4,161 |
| Treasury stock, at cost (791,618 shares in 2018 and 921,461 shares in 2017) | (21,437 |) (24,125) |
| Total shareholders' equity | 1,516,241 | 1,496,264 |
| Total liabilities and shareholders' equity | \$11,901,963 | \$11,570,751 |
| The accompanying notes are an integral part of these consolidated financial statements. | | |

Table of ContentsBERKSHIRE HILLS BANCORP, INC.
CONSOLIDATED STATEMENTS OF INCOME

| (In thousands, except per share data) | Three Months Ended | | Six Months Ended | |
|--|--------------------|----------|------------------|-----------|
| | June 30, 2018 | 2017 | June 30, 2018 | 2017 |
| Interest and dividend income | | | | |
| Loans | \$101,649 | \$71,983 | \$194,484 | \$140,926 |
| Securities and other | 15,230 | 12,683 | 29,635 | 24,449 |
| Total interest and dividend income | 116,879 | 84,666 | 224,119 | 165,375 |
| Interest expense | | | | |
| Deposits | 17,768 | 9,971 | 33,093 | 19,069 |
| Borrowings | 7,990 | 5,150 | 14,435 | 9,875 |
| Total interest expense | 25,758 | 15,121 | 47,528 | 28,944 |
| Net interest income | 91,121 | 69,545 | 176,591 | 136,431 |
| Non-interest income | | | | |
| Mortgage banking originations | 10,195 | 16,281 | 20,342 | 28,959 |
| Loan related income | 6,549 | 5,275 | 11,987 | 9,454 |
| Deposit related fees | 7,605 | 6,645 | 15,671 | 12,849 |
| Insurance commissions and fees | 2,549 | 2,588 | 5,574 | 5,724 |
| Wealth management fees | 2,280 | 2,286 | 4,877 | 4,812 |
| Total fee income | 29,178 | 33,075 | 58,451 | 61,798 |
| Other, net | 155 | (276) | 1,423 | (183) |
| (Loss)/gain on securities, net | 718 | (1) | (784) | 12,569 |
| (Loss)/gain on sale of business operations and other assets, net | (21) | — | 460 | — |
| Loss on termination of hedges | — | — | — | (6,629) |
| Total non-interest income | 30,030 | 32,798 | 59,550 | 67,555 |
| Total net revenue | 121,151 | 102,343 | 236,141 | 203,986 |
| Provision for loan losses | 6,532 | 4,889 | 12,107 | 9,984 |
| Non-interest expense | | | | |
| Compensation and benefits | 41,134 | 36,997 | 83,318 | 73,116 |
| Occupancy and equipment | 10,230 | 8,678 | 20,312 | 17,704 |
| Technology and communications | 7,359 | 6,883 | 14,189 | 12,970 |
| Marketing and promotion | 2,369 | 3,177 | 4,981 | 5,176 |
| Professional services | 1,139 | 2,190 | 3,192 | 4,641 |
| FDIC premiums and assessments | 1,411 | 1,588 | 2,606 | 2,886 |
| Other real estate owned and foreclosures | 1 | 30 | 68 | 58 |
| Amortization of intangible assets | 1,246 | 770 | 2,514 | 1,571 |
| Acquisition, restructuring, and other expenses | 847 | 2,903 | 5,940 | 14,585 |
| Other | 6,601 | 6,307 | 12,086 | 11,142 |
| Total non-interest expense | 72,337 | 69,523 | 149,206 | 143,849 |
| Income before income taxes | 42,282 | 27,931 | 74,828 | 50,153 |
| Income tax expense | 8,251 | 8,237 | 15,549 | 14,999 |
| Net income | \$34,031 | \$19,694 | \$59,279 | \$35,154 |
| Preferred stock dividend | 229 | — | 459 | — |
| Income available to common shareholders | 33,802 | 19,694 | 58,820 | 35,154 |
| Earnings per common share: | | | | |
| Basic | \$0.74 | \$0.53 | \$1.29 | \$0.97 |

Edgar Filing: BERKSHIRE HILLS BANCORP INC - Form 10-Q

| | | | | |
|--------------------------------------|--------|--------|--------|--------|
| Diluted | \$0.74 | \$0.53 | \$1.28 | \$0.96 |
| Weighted average shares outstanding: | | | | |
| Basic | 46,032 | 37,324 | 45,999 | 36,305 |
| Diluted | 46,215 | 37,474 | 46,206 | 36,466 |

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

5

Table of ContentsBERKSHIRE HILLS BANCORP, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

| (In thousands) | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|-----------------------------------|----------|------------------------------|----------|
| | 2018 | 2017 | 2018 | 2017 |
| Net income | \$34,031 | \$19,694 | \$59,279 | \$35,154 |
| Other comprehensive income, before tax: | | | | |
| Changes in unrealized loss on debt securities available-for-sale | (7,840) | 3,927 | (27,002) | (5,505) |
| Changes in unrealized loss on derivative hedges | — | — | — | 6,573 |
| Income taxes related to other comprehensive income: | | | | |
| Changes in unrealized loss on debt securities available-for-sale | 2,001 | (1,455) | 6,932 | 2,086 |
| Changes in unrealized gains on derivative hedges | — | — | — | (2,589) |
| Total other comprehensive (loss)/income | (5,839) | 2,472 | (20,070) | 565 |
| Total comprehensive income | \$28,192 | \$22,166 | \$39,209 | \$35,719 |

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

Table of Contents

BERKSHIRE HILLS BANCORP, INC.

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

| | Preferred stock | Common stock | Additional | Unearned | Retained | Accumulated | Treasury | | | |
|--|-----------------|--------------|------------|--------------|-------------|---------------|-----------|------------|-------------|-------------|
| (In thousands) | Shares | Shares | paid-in | compensation | earnings | other | stock | Total | | |
| | Amount | Amount | capital | | | comprehensive | | | | |
| | Share | Share | capital | | | income/(loss) | | | | |
| Balance at December 31, 2016 | — | 35,673 | \$366 | \$898,989 | \$(6,374) | \$217,494 | \$9,766 | \$(26,943) | \$1,093,298 | |
| Comprehensive income: | | | | | | | | | | |
| Net income | — | — | — | — | — | 35,154 | — | — | 35,154 | |
| Other comprehensive loss | — | — | — | — | — | — | 565 | — | 565 | |
| Total comprehensive income | — | — | — | — | — | 35,154 | 565 | — | 35,719 | |
| Common stock issued | — | 4,638 | 46 | 152,879 | — | — | — | — | 152,925 | |
| Cash dividends declared (\$0.42 per share) | — | — | — | — | — | (15,024) | — | — | (15,024) | |
| Forfeited shares | — | (10) | — | 63 | 304 | — | — | (367) | — | |
| Exercise of stock options | — | 7 | — | — | — | (85) | — | 196 | 111 | |
| Restricted stock grants | — | 154 | — | 1,566 | (5,505) | — | — | 3,939 | — | |
| Stock-based compensation | — | — | — | — | 2,524 | — | — | — | 2,524 | |
| Other, net | — | (34) | — | (4) | — | (69) | — | (1,286) | (1,359) | |
| Balance at June 30, 2017 | — | 40,428 | \$412 | \$1,053,493 | \$(9,051) | \$237,470 | \$10,331 | \$(24,461) | \$1,268,194 | |
| Balance at December 31, 2017 | 522 | \$40,633 | 45,290 | \$460 | \$1,242,487 | \$(6,531) | \$239,179 | \$4,161 | \$(24,125) | \$1,496,264 |
| Comprehensive income: | | | | | | | | | | |
| Net income | — | — | — | — | — | 59,279 | — | — | 59,279 | |
| Other comprehensive loss | — | — | — | — | — | — | (20,070) | — | (20,070) | |
| Total comprehensive income | — | — | — | — | — | 59,279 | (20,070) | — | 39,209 | |

| | | | | | | | | | | |
|---|-----|----------|--------|-------|-------------|------------|-----------|------------|------------|-------------|
| Adoption of ASU No 2016-01, Financial Instruments - Overall (Subtopic 825-10) - Recognition and Measurement of Financial Assets and Liabilities | — | — | — | — | — | — | 6,253 | (6,253) | — | — |
| Adoption of ASU No 2018-02, Income Statement - Reporting Comprehensive Income (Topic 220) - Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income | — | — | — | — | — | — | (896) | 896 | — | — |
| Cash dividends declared on common shares (\$0.44 per share) | — | — | — | — | — | — | (19,977) | — | — | (19,977) |
| Cash dividends declared on preferred shares (\$0.88 per share) | — | — | — | — | — | — | (459) | — | — | (459) |
| Forfeited shares | — | — | (15) | — | 88 | 478 | — | — | (566) | — |
| Exercise of stock options | — | — | 8 | — | — | — | (123) | — | 224 | 101 |
| Restricted stock grants | — | — | 181 | — | 2,100 | (6,841) | — | — | 4,741 | — |
| Stock-based compensation | — | — | — | — | — | 2,798 | — | — | — | 2,798 |
| Other, net | — | — | (44) | — | 16 | — | — | — | (1,711) | (1,695) |
| Balance at June 30, 2018 | 522 | \$40,633 | 45,420 | \$460 | \$1,244,691 | \$(10,096) | \$283,256 | \$(21,266) | \$(21,437) | \$1,516,241 |

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

Table of ContentsBERKSHIRE HILLS BANCORP, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS

| (In thousands) | Six Months Ended June 30, 2018 | 2017 |
|---|--------------------------------------|--------------|
| Cash flows from operating activities: | | |
| Net income | \$ 59,279 | \$ 35,154 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Provision for loan losses | 12,107 | 9,984 |
| Net amortization of securities | 1,460 | 1,332 |
| Change in unamortized net loan costs and premiums | (1,520) | (158) |
| Premises and equipment depreciation and amortization expense | 5,215 | 4,961 |
| Stock-based compensation expense | 2,798 | 2,524 |
| Accretion of purchase accounting entries, net | (11,114) | (7,971) |
| Amortization of other intangibles | 2,514 | 1,571 |
| Income from cash surrender value of bank-owned life insurance policies | (2,359) | (1,188) |
| Securities losses (gains), net | 784 | (12,571) |
| Originations of loans held for sale | (1,106,100) | (1,105,114) |
| Proceeds from sale of loans held for sale | 1,130,880 | 1,108,264 |
| Net gain on sale of loans and other mortgage banking income | (20,342) | (28,959) |
| Loss on disposition of assets | — | 912 |
| Loss on sale of real estate | — | (12) |
| | 2,100 | 2,782 |

| | | | |
|---|----------|---|----------|
| Amortization of interest in tax-advantaged projects | | | |
| Net change in other | (9,748 |) | 4,374 |
| Net cash provided by operating activities | 65,954 | | 15,885 |
| Cash flows from investing activities: | | | |
| Net decrease in trading security | 329 | | 311 |
| Proceeds from sales of securities available for sale | — | | 3,444 |
| Proceeds from maturities, calls, and prepayments of securities available for sale | 93,049 | | 88,821 |
| Purchases of securities available for sale | (165,312 |) | (227,484 |
| Proceeds from sales of marketable equity securities | 26,096 | | 38,575 |
| Purchases of marketable equity securities | (12,688 |) | (14,230 |
| Proceeds from maturities, calls, and prepayments of securities held to maturity | 23,981 | | 6,076 |
| Purchases of securities held to maturity | (7,781 |) | (23,582 |
| Net change in loans | (413,717 |) | (279,723 |
| Proceeds from surrender of bank-owned life insurance | 459 | | 310 |
| Proceeds from sale of Federal Home Loan Bank stock | 28,673 | | 68,672 |
| Purchase of Federal Home Loan Bank stock | (41,118 |) | (76,433 |
| Net investment in limited partnership tax credits | 2,464 | | (756 |
| Purchase of premises and equipment, net | (7,958 |) | (6,921 |

| | | |
|---|------------|------------|
| Payment to terminate cash flow hedges | — | 6,573 |
| Proceeds from sale of other real estate | 1,600 | 274 |
| Net cash (used) by investing activities (continued) | (471,923) | (416,073) |

8

Table of Contents

| (In thousands) | Six Months Ended | |
|--|------------------|-------------|
| | June 30, 2018 | 2017 |
| Cash flows from financing activities: | | |
| Net increase in deposits | 90,009 | 94,324 |
| Proceeds from Federal Home Loan Bank advances and other borrowings | 2,287,896 | 3,841,600 |
| Repayments of Federal Home Loan Bank advances and other borrowings | (2,061,307) | (3,683,292) |
| Exercise of stock options | 101 | 111 |
| Common and preferred stock cash dividends paid | (20,436) | (15,023) |
| Common stock issued, net | — | 152,925 |
| Acquisition contingent consideration paid | — | (1,700) |
| Net cash provided by financing activities | 296,263 | 388,945 |
| | | |
| Net change in cash and cash equivalents | (109,706) | (11,243) |
| | | |
| Cash and cash equivalents at beginning of period | 248,763 | 113,075 |
| | | |
| Cash and cash equivalents at end of period | \$ 139,057 | \$ 101,832 |
| | | |
| Supplemental cash flow information: | | |
| Interest paid on deposits | \$32,160 | \$19,398 |
| Interest paid on borrowed funds | 14,202 | 10,021 |
| Income taxes paid (refund), net | (2,446) | 6,339 |
| | | |
| Other non-cash changes: | | |
| Other net comprehensive income | (20,070) | 565 |
| Real estate owned acquired in settlement of loans | (1,600) | 390 |

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1. BASIS OF PRESENTATION

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

The Company has evaluated subsequent events for potential recognition and/or disclosure through the date these consolidated financial statements were issued.

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

The results for any interim period are not necessarily indicative of results for the full year. These consolidated financial statements should be read in conjunction with the audited financial statements and note disclosures Berkshire Hills Bancorp, Inc. previously filed with the Securities and Exchange Commission in the Company’s Annual Report on Form 10-K for the year ended December 31, 2017. In management’s opinion, all adjustments necessary for a fair statement are reflected in the interim periods presented.

Reclassifications

Certain items in prior financial statements have been reclassified to conform to the current presentation.

Prior Period Acquisition

The Company completed the acquisition of Commerce Bancshares Corp. (“Commerce”), the parent company of Commerce Bank & Trust Company (“Commerce Bank”), at the close of business on October 13, 2017. With this acquisition, the Company established a market position in Worcester, New England’s second largest city. Additionally, this acquisition was a catalyst for the Company’s decision to relocate its corporate headquarters to Boston and to expand its Greater Boston market initiatives. This acquisition also increased the Company’s total assets over the \$10 billion Dodd Frank Act threshold for additional regulatory requirements.

The acquisition was accounted for under the acquisition method of accounting in accordance with ASC Topic 805, Business Combinations. Due to the complexity in valuing the acquired loans and the significant amount of data inputs required, the valuation of the loans is not yet final. Fair value estimates are based on the information available, and are subject to change up to one year after the closing date of the acquisition as additional information relative to the closing date fair values become available. In the second quarter of 2018 the Company did not recognize a material measurement period adjustment. Management continues to review initial estimates on certain areas such as loan valuations and the deferred tax asset and the review will be completed in the third quarter of 2018.

Recently Adopted Accounting Principles

Effective January 1, 2018, the following new accounting guidance was adopted by the Company:

ASU No. 2014-09, Revenue from Contracts with Customers (additional information is disclosed in Note 14 - Revenue of the Consolidated Financial Statements);

ASU No. 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

In February 2018, the FASB issued ASU No. 2018-02, "Income statement - Reporting Comprehensive Income (Topic 220) Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income" which will allow a reclassification from accumulated other comprehensive income ("AOCI") to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act of 2017. These amendments are effective for all entities for fiscal years beginning after December 15, 2018. For interim periods within those fiscal years, early adoption of the amendment is permitted including public business entities for reporting periods for which financial statements have not yet been issued. The Company elected to early adopt ASU 2018-02 during the first quarter of 2018, and elected to reclassify the income tax effects of the Tax Cuts and Jobs Act of 2017 from AOCI to retained earnings. The immaterial reclassification increased AOCI and decreased retained earnings by \$896 thousand, with no net effect on total shareholders' equity.

Future Application of Accounting Pronouncements

In February 2016, the FASB issued ASU No. 2016-02, "Leases". The new pronouncement improves the transparency and comparability of financial reporting around leasing transactions and more closely aligns accounting for leases with the recently issued International Financial Reporting Standard. The pronouncement affects all entities that are participants to leasing agreements. From a lessee accounting perspective, the ASU requires a lessee to recognize assets and liabilities on the balance sheet for operating leases and changes many key definitions, including the definition of a lease. The ASU includes a short-term lease exception for leases with a term of twelve months or less, in which a lessee can make an accounting policy election not to recognize lease assets and lease liabilities. Lessees will continue to differentiate between finance leases (previously referred to as capital leases) and operating leases, using classification criteria that are substantially similar to the previous guidance. For lessees, the recognition, measurement, and presentation of expenses and cash flows arising from a lease have not significantly changed from previous GAAP. From a lessor accounting perspective, the guidance is largely unchanged, except for targeted improvements to align with new terminology under lessee accounting and with the updated revenue recognition guidance in Topic 606. For sale-leaseback transactions, for a sale to occur the transfer must meet the sale criteria under the new revenue standard, ASC 606. Entities will not be required to reassess transactions previously accounted under then existing guidance.

Additionally, the ASU includes additional quantitative and qualitative disclosures required by lessees and lessors to help users better understand the amount, timing, and uncertainty of cash flows arising from leases. ASU No. 2016-02 is effective for fiscal years beginning after December 31, 2018, and interim periods within those fiscal years. Lessees and lessors are required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach. The modified retrospective approach includes a number of optional practical expedients that entities may elect to apply as well as transition guidance specific to nonstandard leasing transactions. The Company is currently evaluating the provisions of ASU No. 2016-02 to determine the potential impact the new standard will have on the Company's consolidated financial statements. It is expected that assets and liabilities will increase based on the present value of remaining lease payments for leases in place at the adoption date; however, this is not expected to be material to the Company's results of operations or financial position. The Company continues to identify a complete inventory of arrangements containing a lease and accumulating the lease data necessary to apply the guidance. We will continue to review contracts up through the effective date and may identify additional leases or leases embedded in arrangements that will be within the scope of the new guidance.

In June 2016, the FASB issued ASU No. 2016-13, "Measurement of Credit Losses on Financial Instruments." This ASU improves financial reporting by requiring timelier recording of credit losses on loans and other financial instruments. The ASU requires companies to measure all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Forward-looking information will now be used in credit loss estimates. The ASU requires enhanced disclosures to provide better understanding surrounding significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of a company's portfolio. These disclosures include qualitative and quantitative requirements

that provide additional information about the amounts recorded in the financial statements. Additionally, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. Most debt instruments will require a cumulative-effect adjustment to retained earnings on the statement of financial position as of the beginning of the first reporting

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

period in which the guidance is adopted (modified retrospective approach). However, there is instrument-specific transition guidance. ASU No. 2016-13 is effective for interim and annual periods beginning after December 15, 2019. Early application will be permitted for interim and annual periods beginning after December 15, 2018. The Company is evaluating the provisions of ASU No. 2016-13, and will closely monitor developments and additional guidance to determine the potential impact on the Company's consolidated financial statements. The Company expects the primary changes to be the application of the expected credit loss model to the financial statements. In addition, the Company expects the guidance to change the presentation of credit losses within the available-for-sale fixed maturities portfolio through an allowance method rather than as a direct write-down. The expected credit loss model will require a financial asset to be presented at the net amount expected to be collected. The allowance method for available-for-sale debt securities will allow the Company to record reversals of credit losses if the estimate of credit losses declines. The Company is in the process of identifying and implementing required changes to loan loss estimation models and processes and evaluating the impact of this new accounting guidance, which at the date of adoption is expected to increase the allowance for credit losses with a resulting negative adjustment to retained earnings.

In January 2017, the FASB issued ASU No. 2017-04, "Intangibles: Goodwill and Other: Simplifying the Test for Goodwill Impairment." The ASU simplifies the test for goodwill impairment by eliminating the second step of the current two-step method. Under the new accounting guidance, entities will compare the fair value of a reporting unit with its carrying amount. If the carrying amount exceeds the reporting unit's fair value, the entity is required to recognize an impairment charge for this amount. Current guidance requires an entity to proceed to a second step, whereby the entity would determine the fair value of its assets and liabilities. The new method applies to all reporting units. The performance of a qualitative assessment is still allowable. This accounting guidance is effective prospectively for interim and annual reporting periods beginning after December 15, 2019. Early adoption is permitted. The Company does not expect adoption to have a material effect on our consolidated financial statements.

In August 2017, the FASB issued ASU No. 2017-12, "Derivatives and Hedging: Targeted Improvements to Accounting for Hedging Activities." The purpose of this updated guidance is to better align a company's financial reporting for hedging activities with the economic objectives of those activities. ASU No. 2017-12 is effective for public business entities for fiscal years beginning after December 15, 2018, with early adoption, including adoption in an interim period, permitted. ASU 2017-12 requires a modified retrospective transition method in which the Company will recognize the cumulative effect of the change on the opening balance of each affected component of equity in the consolidated balance sheet as of the date of adoption. While the Company continues to assess all potential impacts of the standard, we currently do not expect adoption to have a material impact on our consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 2. TRADING SECURITY

The Company holds a tax advantaged economic development bond accounted for at fair value. The security had an amortized cost of \$10.4 million and \$10.8 million, and a fair value of \$11.5 million and \$12.3 million, at June 30, 2018 and December 31, 2017, respectively. As discussed further in Note 11 - Derivative Financial Instruments and Hedging Activities, the Company entered into a swap contract to swap-out the fixed rate of the security in exchange for a variable rate. The Company does not purchase securities with the intent of selling them in the near term, and there were no other securities in the trading portfolio at June 30, 2018.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 3. SECURITIES AVAILABLE FOR SALE, HELD TO MATURITY, AND MARKETABLE EQUITY SECURITIES

The Company adopted ASU-2016-01 "Recognition and Measurement of Financial Assets and Financial Liabilities" in the first quarter of 2018. All changes in the fair value of marketable equity securities, including other-than-temporary impairment, are immediately recognized in earnings.

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

| (In thousands) | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
|--|-------------------|------------------------------|-------------------------------|--------------|
| June 30, 2018 | | | | |
| Securities available for sale | | | | |
| Debt securities: | | | | |
| Municipal bonds and obligations | \$ 110,381 | \$ 2,475 | \$(719) | \$ 112,137 |
| Agency collateralized mortgage obligations | 940,130 | 10 | (24,923) | 915,217 |
| Agency mortgage-backed securities | 190,872 | 45 | (6,247) | 184,670 |
| Agency commercial mortgage-backed securities | 62,930 | — | (3,417) | 59,513 |
| Corporate bonds | 100,985 | 534 | (457) | 101,062 |
| Trust preferred securities | 11,266 | 348 | — | 11,614 |
| Other bonds and obligations | 9,042 | 44 | (49) | 9,037 |
| Total securities available for sale | 1,425,606 | 3,456 | (35,812) | 1,393,250 |
| Securities held to maturity | | | | |
| Municipal bonds and obligations | 268,529 | 3,928 | (3,066) | 269,391 |
| Agency collateralized mortgage obligations | 72,754 | 169 | (1,392) | 71,531 |
| Agency mortgage-backed securities | 7,457 | — | (351) | 7,106 |
| Agency commercial mortgage-backed securities | 10,449 | — | (532) | 9,917 |
| Tax advantaged economic development bonds | 20,395 | 19 | (1,194) | 19,220 |
| Other bonds and obligations | 321 | — | — | 321 |
| Total securities held to maturity | 379,905 | 4,116 | (6,535) | 377,486 |
| Marketable equity securities | 55,618 | 6,024 | (1,916) | 59,726 |
| Total | \$ 1,861,129 | \$ 13,596 | \$(44,263) | \$ 1,830,462 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

| (In thousands) | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
|--|-------------------|------------------------------|-------------------------------|--------------|
| December 31, 2017 | | | | |
| Securities available for sale | | | | |
| Debt securities: | | | | |
| Municipal bonds and obligations | \$ 113,427 | \$ 5,012 | \$(206) | \$ 118,233 |
| Agency collateralized mortgage obligations | 859,705 | 397 | (8,944) | 851,158 |
| Agency mortgage-backed securities | 218,926 | 279 | (2,265) | 216,940 |
| Agency commercial mortgage-backed securities | 64,025 | 41 | (1,761) | 62,305 |
| Corporate bonds | 110,076 | 882 | (237) | 110,721 |
| Trust preferred securities | 11,334 | 343 | — | 11,677 |
| Other bonds and obligations | 9,757 | 154 | (31) | 9,880 |
| Total securities available for sale | 1,387,250 | 7,108 | (13,444) | 1,380,914 |
| Securities held to maturity | | | | |
| Municipal bonds and obligations | 270,310 | 8,675 | (90) | 278,895 |
| Agency collateralized mortgage obligations | 73,742 | 1,045 | (486) | 74,301 |
| Agency mortgage-backed securities | 7,892 | — | (164) | 7,728 |
| Agency commercial mortgage-backed securities | 10,481 | — | (268) | 10,213 |
| Tax advantaged economic development bonds | 34,357 | 596 | (1,135) | 33,818 |
| Other bonds and obligations | 321 | — | — | 321 |
| Total securities held to maturity | 397,103 | 10,316 | (2,143) | 405,276 |
| Marketable equity securities | 36,483 | 9,211 | (509) | 45,185 |
| Total | \$ 1,820,836 | \$ 26,635 | \$(16,096) | \$ 1,831,375 |

The amortized cost and estimated fair value of available for sale (“AFS”) and held to maturity (“HTM”) securities segregated by contractual maturity at June 30, 2018 are presented below. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations. Mortgage-backed securities are shown in total, as their maturities are highly variable.

| (In thousands) | Available for sale | | Held to maturity | |
|-----------------------------|--------------------|---------------|-------------------|---------------|
| | Amortized Cost | Fair Value | Amortized Cost | Fair Value |
| Within 1 year | \$265 | \$266 | \$2,251 | \$2,251 |
| Over 1 year to 5 years | 32,662 | 32,794 | 14,496 | 14,425 |
| Over 5 years to 10 years | 76,018 | 76,647 | 6,701 | 6,780 |
| Over 10 years | 122,729 | 124,143 | 265,797 | 265,476 |
| Total bonds and obligations | 231,674 | 233,850 | 289,245 | 288,932 |
| Mortgage-backed securities | 1,193,932 | 1,159,400 | 90,660 | 88,554 |
| Total | \$1,425,606 | \$1,393,250 | \$379,905 | \$377,486 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

| (In thousands) | Less Than Twelve Months | | Over Twelve Months | | Total | |
|--|-------------------------|--------------|-------------------------|------------|-------------------------|--------------|
| | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses | Fair Value |
| June 30, 2018 | | | | | | |
| Securities available for sale | | | | | | |
| Debt securities: | | | | | | |
| Municipal bonds and obligations | \$ 162 | \$ 5,805 | \$ 557 | \$ 8,600 | \$ 719 | \$ 14,405 |
| Agency collateralized mortgage obligations | 20,590 | 800,936 | 4,333 | 97,803 | 24,923 | 898,739 |
| Agency mortgage-backed securities | 3,074 | 119,032 | 3,173 | 62,416 | 6,247 | 181,448 |
| Agency commercial mortgage-backed securities | 351 | 13,421 | 3,066 | 46,092 | 3,417 | 59,513 |
| Corporate bonds | 457 | 61,521 | — | — | 457 | 61,521 |
| Other bonds and obligations | 20 | 987 | 29 | 2,085 | 49 | 3,072 |
| Total securities available for sale | 24,654 | 1,001,702 | 11,158 | 216,996 | 35,812 | 1,218,698 |
| Securities held to maturity | | | | | | |
| Municipal bonds and obligations | 2,885 | 117,250 | 181 | 1,936 | 3,066 | 119,186 |
| Agency collateralized mortgage obligations | 720 | 31,773 | 672 | 11,882 | 1,392 | 43,655 |
| Agency mortgage-backed securities | — | — | 351 | 7,106 | 351 | 7,106 |
| Agency commercial mortgage-backed securities | — | — | 532 | 9,917 | 532 | 9,917 |
| Tax advantaged economic development bonds | 1,194 | 15,514 | — | — | 1,194 | 15,514 |
| Total securities held to maturity | 4,799 | 164,537 | 1,736 | 30,841 | 6,535 | 195,378 |
| Total | \$ 29,453 | \$ 1,166,239 | \$ 12,894 | \$ 247,837 | \$ 42,347 | \$ 1,414,076 |
| December 31, 2017 | | | | | | |
| Securities available for sale | | | | | | |
| Debt securities: | | | | | | |
| Municipal bonds and obligations | \$ — | \$ — | \$ 206 | \$ 8,985 | \$ 206 | \$ 8,985 |
| Agency collateralized mortgage obligations | 6,849 | 655,479 | 2,095 | 80,401 | 8,944 | 735,880 |
| Agency mortgage-backed securities | 765 | 95,800 | 1,500 | 65,323 | 2,265 | 161,123 |
| Agency commercial mortgage-backed securities | 334 | 17,379 | 1,427 | 39,268 | 1,761 | 56,647 |
| Corporate bonds | 1 | 328 | 236 | 15,769 | 237 | 16,097 |
| Other bonds and obligations | 11 | 1,096 | 20 | 2,004 | 31 | 3,100 |
| Total securities available for sale | 7,960 | 770,082 | 5,484 | 211,750 | 13,444 | 981,832 |
| Securities held to maturity | | | | | | |
| Municipal bonds and obligations | 35 | 10,213 | 55 | 2,059 | 90 | 12,272 |
| Agency collateralized mortgage obligations | — | — | 486 | 12,946 | 486 | 12,946 |
| Agency mortgage-backed securities | — | — | 164 | 7,728 | 164 | 7,728 |
| Agency commercial mortgage-backed securities | — | — | 268 | 10,213 | 268 | 10,213 |
| Tax advantaged economic development bonds | 1,135 | 7,305 | — | — | 1,135 | 7,305 |
| Total securities held to maturity | 1,170 | 17,518 | 973 | 32,946 | 2,143 | 50,464 |

Edgar Filing: BERKSHIRE HILLS BANCORP INC - Form 10-Q

| | | | | | | |
|-------|----------|------------|----------|------------|-----------|--------------|
| Total | \$ 9,130 | \$ 787,600 | \$ 6,457 | \$ 244,696 | \$ 15,587 | \$ 1,032,296 |
|-------|----------|------------|----------|------------|-----------|--------------|

16

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Debt Securities

The Company expects to recover its amortized cost basis on all debt securities in its AFS and HTM portfolios. Furthermore, the Company does not intend to sell nor does it anticipate that it will be required to sell any of its securities in an unrealized loss position as of June 30, 2018, prior to this recovery. The Company's ability and intent to hold these securities until recovery is supported by the Company's strong capital and liquidity positions as well as its historically low portfolio turnover.

The following summarizes, by investment security type, the basis for the conclusion that the debt securities in an unrealized loss position within the Company's AFS and HTM portfolios were not other-than-temporarily impaired at June 30, 2018:

AFS municipal bonds and obligations

At June 30, 2018, 17 of the total 251 securities in the Company's portfolio of AFS municipal bonds and obligations were in unrealized loss positions. Aggregate unrealized losses represented 4.8% of the amortized cost of securities in unrealized loss positions. The Company continually monitors the municipal bond sector of the market carefully and periodically evaluates the appropriate level of exposure to the market. At this time, the Company feels the bonds in this portfolio carry minimal risk of default and the Company is appropriately compensated for that risk. There were no material underlying credit downgrades during the quarter. All securities are performing.

AFS collateralized mortgage obligations

At June 30, 2018, 237 out of the total 245 securities in the Company's portfolio of AFS collateralized mortgage obligations were in unrealized loss positions. Aggregate unrealized losses represented 2.7% of the amortized cost of securities in unrealized loss positions. The Federal National Mortgage Association ("FNMA"), Federal Home Loan Mortgage Corporation ("FHLMC"), and Government National Mortgage Association ("GNMA") guarantee the contractual cash flows of all of the Company's collateralized mortgage obligations. The securities are investment grade rated and there were no material underlying credit downgrades during the quarter. All securities are performing.

AFS commercial and residential mortgage-backed securities

At June 30, 2018, 73 out of the total 100 securities in the Company's portfolio of AFS mortgage-backed securities were in unrealized loss positions. Aggregate unrealized losses represented 3.9% of the amortized cost of securities in unrealized loss positions. The FNMA, FHLMC, and GNMA guarantee the contractual cash flows of all of the Company's mortgage-backed securities. The securities are investment grade rated and there were no material underlying credit downgrades during the quarter. All securities are performing.

AFS corporate bonds

At June 30, 2018, 12 out of the total 20 securities in the Company's portfolio of AFS corporate bonds were in an unrealized loss position. The aggregate unrealized loss represents 0.7% of the amortized cost of bonds in unrealized loss positions. The Company reviews the financial strength of all of these bonds and has concluded that the amortized cost remains supported by the expected future cash flows of these securities.

AFS other bonds and obligations

At June 30, 2018, 6 out of the total 8 securities in the Company's portfolio of other bonds and obligations were in unrealized loss positions. Aggregate unrealized losses represented 1.6% of the amortized cost of securities in unrealized loss positions. The securities are all investment grade rated, and there were no material underlying credit downgrades during the quarter. All securities are performing.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

HTM Municipal bonds and obligations

At June 30, 2018, 78 of the 227 securities in the Company's portfolio of municipal bonds and obligations were in unrealized loss positions. Aggregate unrealized losses represented 2.5% of the amortized cost of securities in unrealized loss positions. The Company continually monitors the municipal bond sector of the market carefully and periodically evaluates the appropriate level of exposure to the market. At this time, the Company feels the bonds in this portfolio carry minimal risk of default and the Company is appropriately compensated for that risk. There were no material underlying credit downgrades during the quarter. All securities are performing.

HTM collateralized mortgage obligations

At June 30, 2018, 4 of the 9 securities in the Company's portfolio of HTM collateralized mortgage obligations were in unrealized loss positions. Aggregate unrealized losses represented 4.7% of the amortized cost of securities in unrealized loss positions. The FNMA, FHLMC, and GNMA guarantee the contractual cash flows of all of the Company's collateralized residential mortgage obligations. The securities are investment grade rated, and there were no material underlying credit downgrades during the quarter. All securities are performing.

HTM commercial and residential mortgage-backed securities

At June 30, 2018, 2 out of a total of 2 securities in the Company's portfolio of HTM mortgage-backed securities were in unrealized loss positions. Aggregate unrealized losses represented 4.9% of the amortized cost of securities in unrealized loss positions. The FNMA, FHLMC, and GNMA guarantee the contractual cash flows of the Company's residential mortgage-backed securities. The securities are investment grade rated and there were no material underlying credit downgrades during the quarter. All securities are performing.

HTM tax-advantaged economic development bonds

At June 30, 2018, 3 out of the total 6 securities in the Company's portfolio of tax advantaged economic development bonds were in unrealized loss positions. Aggregate unrealized losses represented 7.2% of the amortized cost of the securities in unrealized loss positions. One of the above mentioned tax advantaged economic bonds was downgraded to special mention during 2017. The Company believes that more likely than not all the principal outstanding will be collected. All securities are performing.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 4. LOANS

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

Total loans include business activity loans and acquired loans. Acquired loans are those loans acquired from Commerce Bank and Trust Company, First Choice Bank, Parke Bank, Firestone Financial Corp., Hampden Bancorp, Inc., the New York branch acquisition, Beacon Federal Bancorp, Inc., The Connecticut Bank and Trust Company, Legacy Bancorp, Inc., and Rome Bancorp, Inc. Acquired loans that are refinanced are transferred to business activity loans. Business activity and acquired loans are serviced, managed, and accounted for under the Company's same control environment. The following is a summary of total loans:

| (In thousands) | June 30, 2018 | | | December 31, 2017 | | |
|----------------------------------|---------------------|----------------|-------------|---------------------|----------------|-------------|
| | Business Activities | Acquired Loans | Total | Business Activities | Acquired Loans | Total |
| Commercial real estate: | | | | | | |
| Construction | \$345,896 | \$59,268 | \$405,164 | \$269,206 | \$84,965 | \$354,171 |
| Single and multi-family | 378,434 | 195,865 | 574,299 | 217,083 | 206,082 | 423,165 |
| Other commercial real estate | 1,644,666 | 695,194 | 2,339,860 | 1,731,418 | 755,988 | 2,487,406 |
| Total commercial real estate | 2,368,996 | 950,327 | 3,319,323 | 2,217,707 | 1,047,035 | 3,264,742 |
| Commercial and industrial loans: | 1,355,864 | 519,254 | 1,875,118 | 1,182,569 | 621,370 | 1,803,939 |
| Total commercial loans | 3,724,860 | 1,469,581 | 5,194,441 | 3,400,276 | 1,668,405 | 5,068,681 |
| Residential mortgages: | | | | | | |
| 1-4 family | 2,129,976 | 259,734 | 2,389,710 | 1,808,024 | 289,373 | 2,097,397 |
| Construction | 7,289 | 193 | 7,482 | 5,177 | 233 | 5,410 |
| Total residential mortgages | 2,137,265 | 259,927 | 2,397,192 | 1,813,201 | 289,606 | 2,102,807 |
| Consumer loans: | | | | | | |
| Home equity | 293,450 | 99,380 | 392,830 | 294,954 | 115,227 | 410,181 |
| Auto and other | 634,804 | 90,699 | 725,503 | 603,767 | 113,902 | 717,669 |
| Total consumer loans | 928,254 | 190,079 | 1,118,333 | 898,721 | 229,129 | 1,127,850 |
| Total loans | \$6,790,379 | \$1,919,587 | \$8,709,966 | \$6,112,198 | \$2,187,140 | \$8,299,338 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The carrying amount of the acquired loans at June 30, 2018 totaled \$1.9 billion. A subset of these loans was determined to have evidence of credit deterioration at acquisition date, which is accounted for in accordance with ASC 310-30. These purchased credit-impaired loans presently maintain a carrying value of \$70.8 million (and a note balance of \$171.7 million). These loans are evaluated for impairment through the periodic reforecasting of expected cash flows. Loans considered not credit-impaired at acquisition date had a carrying amount of \$1.8 billion.

At December 31, 2017, acquired loans maintained a carrying value of \$2.2 billion and purchased credit-impaired loans totaled \$97.3 million (note balance of \$208.7 million). Loans considered not credit-impaired at acquisition date had a carrying amount of \$2.1 billion.

The following table summarizes activity in the accretable yield for the acquired loan portfolio that falls under the purview of ASC 310-30, Loans and Debt Securities Acquired with Deteriorated Credit Quality:

| | Three Months Ended June 30, | |
|--|--------------------------------|----------|
| (In thousands) | 2018 | 2017 |
| Balance at beginning of period | \$ 10,392 | \$ 7,363 |
| Accretion | (2,195) | (1,005) |
| Net reclassifications from (to) nonaccretable difference | (169) | (85) |
| Payments received, net | (1,724) | (506) |
| Disposals | — | — |
| Balance at end of period | \$ 6,304 | \$ 5,767 |

| | Six Months Ended June 30, | |
|--|------------------------------|----------|
| (In thousands) | 2018 | 2017 |
| Balance at beginning of period | \$ 11,561 | \$ 8,738 |
| Accretion | (4,918) | (2,051) |
| Net reclassifications from (to) nonaccretable difference | 1,654 | 333 |
| Payments received, net | (1,912) | (1,253) |
| Disposals | (81) | — |
| Balance at end of period | \$ 6,304 | \$ 5,767 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following is a summary of past due loans at June 30, 2018 and December 31, 2017:

Business Activities Loans

| (In thousands) | 30-59 Days Past Due | 60-89 Days Past Due | 90 Days or Greater Past Due | Total Past Due | Current | Total Loans | Past Due > 90 days and Accruing |
|----------------------------------|------------------------|------------------------|---|-------------------|-------------|-------------|---------------------------------------|
| June 30, 2018 | | | | | | | |
| Commercial real estate: | | | | | | | |
| Construction | \$ — | \$ — | \$— | \$ — | \$345,896 | \$345,896 | \$ — |
| Single and multi-family | 314 | — | 433 | 747 | 377,687 | 378,434 | 9 |
| Other commercial real estate | 1,163 | 262 | 21,993 | 23,418 | 1,621,248 | 1,644,666 | 16,706 |
| Total | 1,477 | 262 | 22,426 | 24,165 | 2,344,831 | 2,368,996 | 16,715 |
| Commercial and industrial loans: | | | | | | | |
| Total | 2,272 | 114 | 2,528 | 4,914 | 1,350,950 | 1,355,864 | 42 |
| Residential mortgages: | | | | | | | |
| 1-4 family | 817 | 445 | 2,798 | 4,060 | 2,125,916 | 2,129,976 | 879 |
| Construction | — | — | — | — | 7,289 | 7,289 | — |
| Total | 817 | 445 | 2,798 | 4,060 | 2,133,205 | 2,137,265 | 879 |
| Consumer loans: | | | | | | | |
| Home equity | 72 | — | 2,462 | 2,534 | 290,916 | 293,450 | — |
| Auto and other | 2,766 | 478 | 1,667 | 4,911 | 629,893 | 634,804 | 49 |
| Total | 2,838 | 478 | 4,129 | 7,445 | 920,809 | 928,254 | 49 |
| Total | \$ 7,404 | \$ 1,299 | \$31,881 | \$ 40,584 | \$6,749,795 | \$6,790,379 | \$ 17,685 |

Business Activities Loans

| (In thousands) | 30-59 Days Past Due | 60-89 Days Past Due | 90 Days or Greater Past Due | Total Past Due | Current | Total Loans | Past Due > 90 days and Accruing |
|----------------------------------|------------------------|------------------------|---|-------------------|-----------|-------------|---------------------------------------|
| December 31, 2017 | | | | | | | |
| Commercial real estate: | | | | | | | |
| Construction | \$ — | \$ — | \$— | \$ — | \$269,206 | \$269,206 | \$ — |
| Single and multi-family | — | — | 451 | 451 | 216,632 | 217,083 | — |
| Other commercial real estate | 1,925 | 48 | 5,023 | 6,996 | 1,724,422 | 1,731,418 | 457 |
| Total | 1,925 | 48 | 5,474 | 7,447 | 2,210,260 | 2,217,707 | 457 |
| Commercial and industrial loans: | | | | | | | |
| Total | 4,031 | 1,912 | 6,023 | 11,966 | 1,170,603 | 1,182,569 | 128 |
| Residential mortgages: | | | | | | | |
| 1-4 family | 2,412 | 242 | 2,186 | 4,840 | 1,803,184 | 1,808,024 | 520 |
| Construction | — | — | — | — | 5,177 | 5,177 | — |
| Total | 2,412 | 242 | 2,186 | 4,840 | 1,808,361 | 1,813,201 | 520 |
| Consumer loans: | | | | | | | |
| Home equity | 444 | 1,235 | 1,747 | 3,426 | 291,528 | 294,954 | 120 |
| Auto and other | 3,389 | 599 | 1,597 | 5,585 | 598,182 | 603,767 | 143 |
| Total | 3,833 | 1,834 | 3,344 | 9,011 | 889,710 | 898,721 | 263 |

Edgar Filing: BERKSHIRE HILLS BANCORP INC - Form 10-Q

| | | | | | | | |
|-------|-----------|----------|-----------|-----------|--------------|--------------|----------|
| Total | \$ 12,201 | \$ 4,036 | \$ 17,027 | \$ 33,264 | \$ 6,078,934 | \$ 6,112,198 | \$ 1,368 |
|-------|-----------|----------|-----------|-----------|--------------|--------------|----------|

21

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Acquired Loans

| (In thousands) | 30-59 Days Past Due | 60-89 Days Past Due | 90 Days or Greater Past Due | Total Past Due | Acquired Credit Impaired | Total Loans | Past Due > 90 days and Accruing |
|----------------------------------|------------------------|------------------------|---|-------------------|--------------------------------|--------------|---------------------------------------|
| June 30, 2018 | | | | | | | |
| Commercial real estate: | | | | | | | |
| Construction | \$ — | \$ — | \$ — | \$ — | \$ 7,633 | \$ 59,268 | \$ — |
| Single and multi-family | 337 | 100 | 270 | 707 | 2,074 | 195,865 | — |
| Other commercial real estate | 417 | 1,248 | 4,680 | 6,345 | 21,308 | 695,194 | 323 |
| Total | 754 | 1,348 | 4,950 | 7,052 | 31,015 | 950,327 | 323 |
| Commercial and industrial loans: | | | | | | | |
| Total | 446 | 260 | 1,543 | 2,249 | 32,297 | 519,254 | — |
| Residential mortgages: | | | | | | | |
| 1-4 family | 1,318 | 241 | 1,494 | 3,053 | 5,054 | 259,734 | 216 |
| Construction | — | — | — | — | — | 193 | — |
| Total | 1,318 | 241 | 1,494 | 3,053 | 5,054 | 259,927 | 216 |
| Consumer loans: | | | | | | | |
| Home equity | 183 | 119 | 998 | 1,300 | 2,004 | 99,380 | 81 |
| Auto and other | 150 | 8 | 483 | 641 | 396 | 90,699 | 14 |
| Total | 333 | 127 | 1,481 | 1,941 | 2,400 | 190,079 | 95 |
| Total | \$ 2,851 | \$ 1,976 | \$ 9,468 | \$ 14,295 | \$ 70,766 | \$ 1,919,587 | \$ 634 |

Acquired Loans

| (In thousands) | 30-59 Days Past Due | 60-89 Days Past Due | 90 Days or Greater Past Due | Total Past Due | Acquired Credit Impaired | Total Loans | Past Due > 90 days and Accruing |
|----------------------------------|------------------------|------------------------|---|-------------------|--------------------------------|--------------|---------------------------------------|
| December 31, 2017 | | | | | | | |
| Commercial real estate: | | | | | | | |
| Construction | \$ — | \$ — | \$ — | \$ — | \$ 7,655 | \$ 84,965 | \$ — |
| Single and multi-family | 671 | — | 203 | 874 | 2,846 | 206,082 | — |
| Other commercial real estate | 816 | 1,875 | 2,156 | 4,847 | 42,801 | 755,988 | 109 |
| Total | 1,487 | 1,875 | 2,359 | 5,721 | 53,302 | 1,047,035 | 109 |
| Commercial and industrial loans: | | | | | | | |
| Total | 1,252 | 268 | 1,439 | 2,959 | 34,629 | 621,370 | 23 |
| Residential mortgages: | | | | | | | |
| 1-4 family | 957 | 2,581 | 1,247 | 4,785 | 6,974 | 289,373 | 30 |
| Construction | — | — | — | — | — | 233 | — |
| Total | 957 | 2,581 | 1,247 | 4,785 | 6,974 | 289,606 | 30 |
| Consumer loans: | | | | | | | |
| Home equity | 286 | 40 | 1,965 | 2,291 | 1,956 | 115,227 | — |
| Auto and other | 346 | 135 | 430 | 911 | 483 | 113,902 | 38 |
| Total | 632 | 175 | 2,395 | 3,202 | 2,439 | 229,129 | 38 |
| Total | \$ 4,328 | \$ 4,899 | \$ 7,440 | \$ 16,667 | \$ 97,344 | \$ 2,187,140 | \$ 200 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following is summary information pertaining to non-accrual loans at June 30, 2018 and December 31, 2017:

| (In thousands) | June 30, 2018 | | | December 31, 2017 | | |
|----------------------------------|--|----------|----------|--|----------|----------|
| | Business Acquired Activities Loans (1) | Loans(1) | Total | Business Acquired Activities Loans (2) | Loans(2) | Total |
| Commercial real estate: | | | | | | |
| Construction | \$— | \$— | \$— | \$— | \$— | \$— |
| Single and multi-family | 424 | 206 | 630 | 451 | 203 | 654 |
| Other commercial real estate | 5,287 | 3,493 | 8,780 | 4,566 | 2,047 | 6,613 |
| Total | 5,711 | 3,699 | 9,410 | 5,017 | 2,250 | 7,267 |
| Commercial and industrial loans: | | | | | | |
| Total | 2,486 | 1,543 | 4,029 | 5,895 | 1,333 | 7,228 |
| Residential mortgages: | | | | | | |
| 1-4 family | 1,919 | 1,278 | 3,197 | 1,666 | 1,217 | 2,883 |
| Construction | — | — | — | — | — | — |
| Total | 1,919 | 1,278 | 3,197 | 1,666 | 1,217 | 2,883 |
| Consumer loans: | | | | | | |
| Home equity | 2,462 | 917 | 3,379 | 1,627 | 1,965 | 3,592 |
| Auto and other | 1,618 | 469 | 2,087 | 1,454 | 392 | 1,846 |
| Total | 4,080 | 1,386 | 5,466 | 3,081 | 2,357 | 5,438 |
| Total non-accrual loans | \$14,196 | \$ 7,906 | \$22,102 | \$15,659 | \$ 7,157 | \$22,816 |

(1) At quarter end June 30, 2018, acquired credit impaired loans accounted for \$927 thousand of loans greater than 90 days past due that are not presented in the above table.

(2) At December 31, 2017, acquired credit impaired loans accounted for \$83 thousand of loans greater than 90 days past due that are not presented in the above table.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Loans evaluated for impairment as of June 30, 2018 and December 31, 2017 were as follows:

Business Activities Loans

| (In thousands) | Commercial real estate | Commercial and industrial loans | Residential mortgages | Consumer | Total |
|---------------------------------------|---------------------------|------------------------------------|--------------------------|------------|--------------|
| June 30, 2018 | | | | | |
| Loans receivable: | | | | | |
| Balance at end of period | | | | | |
| Individually evaluated for impairment | \$ 27,806 | \$ 2,340 | \$ 2,280 | \$ 1,835 | \$ 34,261 |
| Collectively evaluated for impairment | 2,341,190 | 1,353,524 | 2,134,985 | 926,419 | 6,756,118 |
| Total | \$ 2,368,996 | \$ 1,355,864 | \$ 2,137,265 | \$ 928,254 | \$ 6,790,379 |

Business Activities Loans

| (In thousands) | Commercial real estate | Commercial and industrial loans | Residential mortgages | Consumer | Total |
|---------------------------------------|---------------------------|------------------------------------|--------------------------|------------|--------------|
| December 31, 2017 | | | | | |
| Loans receivable: | | | | | |
| Balance at end of year | | | | | |
| Individually evaluated for impairment | \$ 33,732 | \$ 5,761 | \$ 3,872 | \$ — | \$ 43,365 |
| Collectively evaluated for impairment | 2,183,975 | 1,176,808 | 1,809,329 | 898,721 | 6,068,833 |
| Total | \$ 2,217,707 | \$ 1,182,569 | \$ 1,813,201 | \$ 898,721 | \$ 6,112,198 |

Acquired Loans

| (In thousands) | Commercial real estate | Commercial and industrial loans | Residential mortgages | Consumer | Total |
|---------------------------------------|---------------------------|------------------------------------|--------------------------|------------|--------------|
| June 30, 2018 | | | | | |
| Loans receivable: | | | | | |
| Balance at end of Period | | | | | |
| Individually evaluated for impairment | \$ 5,601 | \$ 864 | \$ 765 | \$ 815 | \$ 8,045 |
| Purchased credit-impaired loans | 31,015 | 32,297 | 5,054 | 2,400 | 70,766 |
| Collectively evaluated for impairment | 913,711 | 486,093 | 254,108 | 186,864 | 1,840,776 |
| Total | \$ 950,327 | \$ 519,254 | \$ 259,927 | \$ 190,079 | \$ 1,919,587 |

Acquired Loans

| (In thousands) | Commercial real estate | Commercial and industrial loans | Residential mortgages | Consumer | Total |
|---------------------------------------|---------------------------|------------------------------------|--------------------------|------------|--------------|
| December 31, 2017 | | | | | |
| Loans receivable: | | | | | |
| Balance at end of year | | | | | |
| Individually evaluated for impairment | \$ 4,244 | \$ 421 | \$ 2,617 | \$ 27 | \$ 7,309 |
| Purchased credit-impaired loans | 53,302 | 34,629 | 6,974 | 2,439 | 97,344 |
| Collectively evaluated for impairment | 989,489 | 586,320 | 280,015 | 226,663 | 2,082,487 |
| Total | \$ 1,047,035 | \$ 621,370 | \$ 289,606 | \$ 229,129 | \$ 2,187,140 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following is a summary of impaired loans at June 30, 2018 and December 31, 2017:

Business Activities Loans

| (In thousands) | June 30, 2018 | | Related Allowance |
|---|-------------------------|------------------------------|-------------------|
| | Recorded Investment (1) | Unpaid Principal Balance (2) | |
| With no related allowance: | | | |
| Commercial real estate - single and multifamily | \$— | \$ — | \$ — |
| Other commercial real estate loans | 26,609 | 32,123 | — |
| Commercial and industrial loans | 908 | 2,180 | — |
| Residential mortgages - 1-4 family | 904 | 1,541 | — |
| Consumer - home equity | 1,776 | 2,410 | — |
| Consumer - other | — | — | — |
| With an allowance recorded: | | | |
| Commercial real estate - single and multifamily | \$306 | \$ 323 | \$ 1 |
| Other commercial real estate loans | 1,430 | 1,423 | 14 |
| Commercial and industrial loans | 1,453 | 1,434 | 70 |
| Residential mortgages - 1-4 family | 1,395 | 1,440 | 109 |
| Consumer - home equity | 43 | 52 | — |
| Consumer - other | 15 | 15 | 1 |
| Total | | | |
| Commercial real estate | \$28,345 | \$ 33,869 | \$ 15 |
| Commercial and industrial loans | 2,361 | 3,614 | 70 |
| Residential mortgages | 2,299 | 2,981 | 109 |
| Consumer | 1,834 | 2,477 | 1 |
| Total impaired loans | \$34,839 | \$ 42,941 | \$ 195 |

(1) The Recorded Investment represents the face amount of the loan increased or decreased by applicable accrued interest, net deferred loan fees and costs, and unamortized premium or discount, and reflects direct charge-offs. These amounts are components of total loans and other assets on the Consolidated Balance Sheet.

(2) The Unpaid Principal Balance represents the customer's legal obligation to the Company.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Business Activities Loans

| (In thousands) | December 31, 2017 | | Related Allowance |
|---|----------------------------|---------------------------------|-------------------|
| | Recorded Investment (1) | Unpaid Principal Balance (2) | |
| With no related allowance: | | | |
| Commercial real estate - single and multifamily | \$1,077 | \$ 3,607 | \$ — |
| Other commercial real estate loans | 18,285 | 18,611 | — |
| Commercial and industrial loans | 2,060 | 2,629 | — |
| Residential mortgages - 1-4 family | 660 | 1,075 | — |
| Consumer - home equity | 867 | 1,504 | — |
| With an allowance recorded: | | | |
| Commercial real estate - construction | \$159 | \$ 159 | \$ 1 |
| Commercial real estate - single and multifamily | 159 | 171 | 1 |
| Other commercial real estate loans | 14,321 | 15,235 | 227 |
| Commercial and industrial loans | 3,716 | 4,249 | 66 |
| Residential mortgages - 1-4 family | 1,344 | 1,446 | 130 |
| Consumer - home equity | 1,014 | 999 | 34 |
| Consumer - other | 17 | 17 | 1 |
| Total | | | |
| Commercial real estate | \$34,001 | \$ 37,783 | \$ 229 |
| Commercial and industrial loans | 5,776 | 6,878 | 66 |
| Residential mortgages | 2,004 | 2,521 | 130 |
| Consumer | 1,898 | 2,520 | 35 |
| Total impaired loans | \$43,679 | \$ 49,702 | \$ 460 |

(1) The Recorded Investment represents the face amount of the loan increased or decreased by applicable accrued interest, net deferred loan fees and costs, and unamortized premium or discount, and reflects direct charge-offs. This amount is a component of total loans on the Consolidated Balance Sheet.

(2) The Unpaid Principal Balance represents the customer's legal obligation to the Company.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Acquired Loans

| (In thousands) | June 30, 2018 | | Related Allowance |
|---|-------------------------|------------------------------|-------------------|
| | Recorded Investment (1) | Unpaid Principal Balance (2) | |
| With no related allowance: | | | |
| Commercial real estate - single and multifamily | \$ 167 | \$ 261 | \$ — |
| Other commercial real estate loans | 2,501 | 5,556 | — |
| Commercial and industrial loans | 521 | 597 | — |
| Residential mortgages - 1-4 family | 696 | 707 | — |
| Consumer - home equity | 501 | 959 | — |
| Consumer - other | 13 | 15 | — |
| With an allowance recorded: | | | |
| Commercial real estate - single and multifamily | \$ 759 | \$ 756 | \$ 10 |
| Other commercial real estate loans | 2,201 | 2,211 | 22 |
| Commercial and industrial loans | 348 | 347 | 9 |
| Residential mortgages - 1-4 family | 76 | 76 | 6 |
| Consumer - home equity | 301 | 360 | 11 |
| Total | | | |
| Commercial real estate | \$ 5,628 | \$ 8,784 | \$ 32 |
| Commercial and industrial loans | 869 | 944 | 9 |
| Residential mortgages | 772 | 783 | 6 |
| Consumer | 815 | 1,334 | 11 |
| Total impaired loans | \$ 8,084 | \$ 11,845 | \$ 58 |

(1) The Recorded Investment represents the face amount of the loan increased or decreased by applicable accrued interest, net deferred loan fees and costs, and unamortized premium or discount, and reflects direct charge-offs. This amount is a component of total loans on the Consolidated Balance Sheet.

(2) The Unpaid Principal Balance represents the customer's legal obligation to the Company.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Acquired Loans

| (In thousands) | December 31, 2017 | | Related Allowance |
|---|-------------------------|------------------------------|-------------------|
| | Recorded Investment (1) | Unpaid Principal Balance (2) | |
| With no related allowance: | | | |
| Commercial real estate - single and multifamily | \$204 | \$ 290 | \$ — |
| Other commercial real estate loans | 1,123 | 2,794 | — |
| Other commercial and industrial loans | 255 | 310 | — |
| Residential mortgages - 1-4 family | 658 | 671 | — |
| Consumer - home equity | 1,374 | 1,654 | — |
| Consumer - other | 27 | 27 | — |
| With an allowance recorded: | | | |
| Commercial real estate - single and multifamily | \$887 | \$ 880 | \$ 18 |
| Other commercial real estate loans | 2,043 | 1,661 | 38 |
| Commercial and industrial loans | 165 | 166 | 1 |
| Residential mortgages - 1-4 family | 166 | 185 | 9 |
| Consumer - home equity | 433 | 540 | 45 |
| Total | | | |
| Commercial real estate | \$4,257 | \$ 5,625 | \$ 56 |
| Commercial and industrial loans | 420 | 476 | 1 |
| Residential mortgages | 824 | 856 | 9 |
| Consumer | 1,834 | 2,221 | 45 |
| Total impaired loans | \$7,335 | \$ 9,178 | \$ 111 |

(1) The Recorded Investment represents the face amount of the loan increased or decreased by applicable accrued interest, net deferred loan fees and costs, and unamortized premium or discount, and reflects direct charge-offs. This amount is a component of total loans on the Consolidated Balance Sheet.

(2) The Unpaid Principal Balance represents the customer's legal obligation to the Company.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following is a summary of the average recorded investment and interest income recognized on impaired loans as of June 30, 2018 and 2017:

Business Activities Loans

| (In thousands) | Six Months Ended June 30, 2018 | | Six Months Ended June 30, 2017 | |
|---|-----------------------------------|--|-----------------------------------|--|
| | Average Recorded Investment | Cash Basis Interest Income Recognized | Average Recorded Investment | Cash Basis Interest Income Recognized |
| With no related allowance: | | | | |
| Commercial real estate - single and multifamily | \$— | \$ — | \$99 | \$ — |
| Other commercial real estate loans | 29,092 | 326 | 22,362 | 473 |
| Commercial and industrial loans | 4,467 | 201 | 1,251 | 16 |
| Residential mortgages - 1-4 family | 942 | 26 | 1,870 | 11 |
| Consumer - home equity | 1,754 | 4 | 90 | — |
| Consumer - other | — | — | — | — |
| With an allowance recorded: | | | | |
| Commercial real estate - single and multifamily | \$310 | \$ 8 | \$171 | \$ 8 |
| Other commercial real estate loans | 1,476 | 39 | 10,056 | 119 |
| Commercial and industrial loans | 1,279 | 83 | 6,902 | 131 |
| Residential mortgages - 1-4 family | 1,409 | 32 | 636 | 7 |
| Consumer - home equity | 45 | 1 | 2,371 | 17 |
| Consumer - other | 16 | — | — | — |
| Total | | | | |
| Commercial real estate | \$30,878 | \$ 373 | \$32,688 | \$ 600 |
| Commercial and industrial loans | 5,746 | 284 | 8,153 | 147 |
| Residential mortgages | 2,351 | 58 | 2,506 | 18 |
| Consumer loans | 1,815 | 5 | 2,461 | 17 |
| Total impaired loans | \$40,790 | \$ 720 | \$45,808 | \$ 782 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Acquired Loans

| (In thousands) | Six Months Ended June 30, 2018 | | Six Months Ended June 30, 2017 | |
|---|-----------------------------------|--|-----------------------------------|--|
| | Average Recorded Investment | Cash Basis Interest Income Recognized | Average Recorded Investment | Cash Basis Interest Income Recognized |
| With no related allowance: | | | | |
| Commercial real estate - single and multifamily | \$ 182 | \$ 9 | \$ 396 | \$ 43 |
| Other commercial real estate loans | 2,124 | 102 | 269 | 49 |
| Commercial and industrial loans | 349 | 27 | 298 | 1 |
| Residential mortgages - 1-4 family | 1,505 | 6 | 393 | 6 |
| Consumer - home equity | 760 | — | 771 | — |
| Consumer - other | 17 | 1 | — | — |
| With an allowance recorded: | | | | |
| Commercial real estate - single and multifamily | \$ 765 | \$ 20 | \$ 905 | \$ 12 |
| Other commercial real estate loans | 2,255 | 69 | 1,482 | 19 |
| Commercial and industrial loans | 287 | 17 | 328 | 8 |
| Residential mortgages - 1-4 family | 77 | 2 | 94 | 1 |
| Consumer - home equity | 320 | 5 | 390 | 5 |
| Consumer - other | — | — | — | — |
| Total | | | | |
| Other commercial real estate loans | \$ 5,326 | \$ 200 | \$ 3,052 | \$ 123 |
| Commercial and industrial loans | 636 | 44 | 626 | 9 |
| Residential mortgages | 1,582 | 8 | 487 | 7 |
| Consumer loans | 1,097 | 6 | 1,161 | 5 |
| Total impaired loans | \$ 8,641 | \$ 258 | \$ 5,326 | \$ 144 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Troubled Debt Restructuring Loans

The Company's loan portfolio also includes certain loans that have been modified in a Troubled Debt Restructuring (TDR), where economic concessions have been granted to borrowers who have experienced or are expected to experience financial difficulties. These concessions typically result from the Company's loss mitigation activities and could include reductions in the interest rate, payment extensions, forgiveness of principal, forbearance, or other actions. Certain TDRs are classified as nonperforming at the time of restructure and may only be returned to performing status after considering the borrower's sustained repayment performance for a reasonable period, generally six months. TDRs are evaluated individually for impairment and may result in a specific allowance amount allocated to an individual loan.

The following tables include the recorded investment and number of modifications identified during the three and six months ended June 30, 2018 and June 30, 2017. The table includes the recorded investment in the loans prior to a modification and also the recorded investment in the loans after the loans were restructured. There were no modifications made during the three months ended June 30, 2018. The modifications for the six months ended June 30, 2018 were attributable to interest rate concessions, principal concessions, maturity date extensions, modified payment terms, reamortization, and accelerated maturity. The modifications for the three and six months ended June 30, 2017 were attributable to interest rate concessions, principal concessions, maturity date extensions, modified payment terms, reamortization, and accelerated maturity.

| (Dollars in thousands) | Three Months Ended June 30, 2018 | | | |
|-----------------------------------|----------------------------------|----------------------|----------------------|------------|
| | Pre-Modification | | Post-Modification | |
| | Number of | Outstanding Recorded | Outstanding Recorded | Investment |
| | Modifications | Investment | Investment | |
| Troubled Debt Restructurings | | | | |
| Commercial and industrial | — | \$ — | \$ — | — |
| Residential - 1-4 Family | — | — | — | — |
| Total | — | \$ — | \$ — | — |
| (Dollars in thousands) | Six Months Ended June 30, 2018 | | | |
| | Pre-Modification | | Post-Modification | |
| | Number of | Outstanding Recorded | Outstanding Recorded | Investment |
| | Modifications | Investment | Investment | |
| Troubled Debt Restructurings | | | | |
| Commercial and industrial | 4 | \$ 1,995 | \$ 1,924 | |
| Residential - 1-4 Family | 1 | 118 | 118 | |
| Total | 5 | \$ 2,113 | \$ 2,042 | |
| (Dollars in thousands) | Three Months Ended June 30, 2017 | | | |
| | Pre-Modification | | Post-Modification | |
| | Number of | Outstanding Recorded | Outstanding Recorded | Investment |
| | Modifications | Investment | Investment | |
| Troubled Debt Restructurings | | | | |
| Commercial - Other | 9 | \$ 10,613 | \$ 9,385 | |
| Commercial and industrial - Other | 4 | 1,793 | 1,793 | |
| Residential - 1-4 Family | — | — | — | |
| Consumer Home Equity | — | — | — | |
| Total | 13 | \$ 12,406 | \$ 11,178 | |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

| (Dollars in thousands) | Six Months Ended June 30, 2017 | |
|-----------------------------------|---|---|
| | Pre-Modification Number of Outstanding Modifications Investment | Post-Modification Outstanding Recorded Investment |
| Troubled Debt Restructurings | | |
| Commercial - Other | 15 \$ 13,445 | \$ 11,718 |
| Commercial and industrial - Other | 5 1,817 | 1,817 |
| Residential - 1-4 Family | 2 205 | 188 |
| Consumer Home Equity | 1 53 | 53 |
| Total | 23 \$ 15,520 | \$ 13,776 |

The following table discloses the recorded investments and numbers of modifications for TDRs where a concession has been made within the previous 12 months, that then defaulted in the respective reporting period. For the three and six months ended June 30, 2018, there were two loans that were restructured that had subsequently defaulted during the period.

| (Dollars in thousands) | Modifications that Subsequently Defaulted Three Months Ended June 30, 2018 | |
|-----------------------------------|---|------------|
| | Number of Contracts | Investment |
| Troubled Debt Restructurings | | |
| Commercial - Other | 1 \$ 5,992 | |
| Commercial and industrial - Other | 1 \$ 1,065 | |

| (Dollars in thousands) | Modifications that Subsequently Defaulted Six Months Ended June 30, 2018 | |
|-----------------------------------|---|------------|
| | Number of Contracts | Investment |
| Troubled Debt Restructurings | | |
| Commercial - Other | 1 \$ 5,992 | |
| Commercial and industrial - Other | 1 \$ 1,065 | |

| (Dollars in thousands) | Modifications that Subsequently Defaulted Three Months Ended June 30, 2017 | |
|-----------------------------------|---|------------|
| | Number of Contracts | Investment |
| Troubled Debt Restructurings | | |
| Commercial - Other | — \$ — | — |
| Commercial and industrial - Other | — \$ — | — |

| (Dollars in thousands) | Modifications that Subsequently Defaulted Six Months Ended June 30, 2017 | |
|-----------------------------------|---|------------|
| | Number of Contracts | Investment |
| Troubled Debt Restructurings | | |
| Commercial - Other | 1 \$ 113 | |
| Commercial and industrial - Other | 1 \$ 101 | |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table presents the Company's TDR activity for the three and six months ended June 30, 2018 and 2017:

| | Three Months Ended June 30, | |
|------------------------------------|--------------------------------|----------|
| (In thousands) | 2018 | 2017 |
| Balance at beginning of the period | \$43,105 | \$34,699 |
| Principal payments | (2,511) | (266) |
| TDR status change (1) | — | — |
| Other reductions/increases (2) | (7,088) | (1,055) |
| Newly identified TDRs | — | 11,178 |
| Balance at end of the period | \$33,506 | \$44,556 |
| | Six Months Ended June 30, | |
| (In thousands) | 2018 | 2017 |
| Balance at beginning of the period | \$41,990 | \$33,829 |
| Principal payments | (3,150) | (1,154) |
| TDR status change (1) | — | — |
| Other reductions/increases (2) | (7,376) | (1,895) |
| Newly identified TDRs | 2,042 | 13,776 |
| Balance at end of the period | \$33,506 | \$44,556 |

- (1) TDR status change classification represents TDR loans with a specified interest rate equal to or greater than the rate that the Company was willing to accept at the time of the restructuring for a new loan with comparable risk and the loan was on current payment status and not impaired based on the terms specified by the restructuring agreement.
- (2) Other reductions classification consists of transfer to other real estate owned and charge-offs and advances to loans.

The evaluation of certain loans individually for specific impairment includes loans that were previously classified as TDRs or continue to be classified as TDRs.

As of June 30, 2018, the Company maintained no foreclosed residential real estate property. Additionally, residential mortgage loans collateralized by real estate property that are in the process of foreclosure as of June 30, 2018 and December 31, 2017 totaled \$3.8 million and \$4.9 million, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 5. LOAN LOSS ALLOWANCE

Activity in the allowance for loan losses for the three and six months ended June 30, 2018 and 2017 was as follows:

| Business Activities Loans (In thousands) | At or for the three months ended June 30, 2018 | | | | |
|---|--|--|--------------------------|----------|----------|
| | Commercial real estate | Commercial and industrial loans | Residential mortgages | Consumer | Total |
| Balance at beginning of period | \$17,841 | \$ 13,229 | \$ 8,598 | \$ 7,609 | \$47,277 |
| Charged-off loans | 1,392 | 1,706 | 27 | 837 | 3,962 |
| Recoveries on charged-off loans | 26 | 447 | 6 | 135 | 614 |
| Provision/(releases) for loan losses | 2,676 | 2,685 | 853 | 171 | 6,385 |
| Balance at end of period | \$19,151 | \$ 14,655 | \$ 9,430 | \$ 7,078 | \$50,314 |

| Business Activities Loans (In thousands) | At or for the six months ended June 30, 2018 | | | | |
|---|--|--|--------------------------|----------|----------|
| | Commercial real estate | Commercial and industrial loans | Residential mortgages | Consumer | Total |
| Balance at beginning of period | \$16,843 | \$ 13,850 | \$ 9,420 | \$ 5,807 | \$45,920 |
| Charged-off loans | 1,498 | 2,596 | 27 | 1,777 | 5,898 |
| Recoveries on charged-off loans | 49 | 491 | 6 | 209 | 755 |
| Provision/(releases) for loan losses | 3,757 | 2,910 | 31 | 2,839 | 9,537 |
| Balance at end of period | \$19,151 | \$ 14,655 | \$ 9,430 | \$ 7,078 | \$50,314 |

| Business Activities Loans (In thousands) | At or for the three months ended June 30, 2017 | | | | |
|---|--|--|--------------------------|----------|----------|
| | Commercial real estate | Commercial and industrial loans | Residential mortgages | Consumer | Total |
| Balance at beginning of period | \$16,280 | \$ 11,850 | \$ 7,863 | \$ 5,470 | \$41,463 |
| Charged-off loans | 1,393 | 581 | 278 | 631 | 2,883 |
| Recoveries on charged-off loans | — | 55 | 14 | 87 | 156 |
| Provision/(releases) for loan losses | 1,046 | 1,306 | 512 | 1,295 | 4,159 |
| Balance at end of period | \$15,933 | \$ 12,630 | \$ 8,111 | \$ 6,221 | \$42,895 |

| Business Activities Loans (In thousands) | At or for the six months ended June 30, 2017 | | | | |
|---|--|--|--------------------------|----------|----------|
| | Commercial real estate | Commercial and industrial loans | Residential mortgages | Consumer | Total |
| Balance at beginning of period | \$16,498 | \$ 9,447 | \$ 7,805 | \$ 5,479 | \$39,229 |
| Charged-off loans | 1,516 | 1,851 | 513 | 1,317 | 5,197 |
| Recoveries on charged-off loans | 57 | 71 | 29 | 172 | 329 |
| Provision/(releases) for loan losses | 894 | 4,963 | 790 | 1,887 | 8,534 |
| Balance at end of period | \$15,933 | \$ 12,630 | \$ 8,111 | \$ 6,221 | \$42,895 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

| | At or for the three months ended June 30, 2018 | | | | |
|--------------------------------------|--|--|--------------------------|----------|---------|
| Acquired Loans (In thousands) | Commercial real estate | Commercial and industrial loans | Residential mortgages | Consumer | Total |
| Balance at beginning of period | \$3,995 | \$ 1,243 | \$ 1,046 | \$ 298 | \$6,582 |
| Charged-off loans | 972 | — | 622 | 164 | 1,758 |
| Recoveries on charged-off loans | 259 | 66 | 11 | 304 | 640 |
| Provision/(releases) for loan losses | 100 | (182) | 183 | 46 | 147 |
| Balance at end of period | \$3,382 | \$ 1,127 | \$ 618 | \$ 484 | \$5,611 |
| | At or for the six months ended June 30, 2018 | | | | |
| Acquired Loans (In thousands) | Commercial real estate | Commercial and industrial loans | Residential mortgages | Consumer | Total |
| Balance at beginning of period | \$3,856 | \$ 1,125 | \$ 598 | \$ 335 | \$5,914 |
| Charged-off loans | 1,712 | 155 | 1,053 | 693 | 3,613 |
| Recoveries on charged-off loans | 265 | 95 | 36 | 344 | 740 |
| Provision/(releases) for loan losses | 973 | 62 | 1,037 | 498 | 2,570 |
| Balance at end of period | \$3,382 | \$ 1,127 | \$ 618 | \$ 484 | \$5,611 |
| | At or for the three months ended June 30, 2017 | | | | |
| Acquired Loans (In thousands) | Commercial real estate | Commercial and industrial loans | Residential mortgages | Consumer | Total |
| Balance at beginning of period | \$2,128 | \$ 1,054 | \$ 706 | \$ 453 | \$4,341 |
| Charged-off loans | 94 | 43 | 71 | 340 | 548 |
| Recoveries on charged-off loans | 13 | (56) | (2) | (14) | (59) |
| Provision/(releases) for loan losses | 309 | 59 | 57 | 305 | 730 |
| Balance at end of period | \$2,356 | \$ 1,014 | \$ 690 | \$ 404 | \$4,464 |
| | At or for the six months ended June 30, 2017 | | | | |
| Acquired Loans (In thousands) | Commercial real estate | Commercial and industrial loans | Residential mortgages | Consumer | Total |
| Balance at beginning of period | \$2,303 | \$ 1,164 | \$ 766 | \$ 536 | \$4,769 |
| Charged-off loans | 670 | 481 | 215 | 491 | 1,857 |
| Recoveries on charged-off loans | 22 | 1 | 38 | 41 | 102 |
| Provision/(releases) for loan losses | 701 | 330 | 101 | 318 | 1,450 |
| Balance at end of period | \$2,356 | \$ 1,014 | \$ 690 | \$ 404 | \$4,464 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following tables present a summary of the allowance for loan losses as of June 30, 2018 and December 31, 2017:

| Business Activities Loans (In thousands) | At June 30, 2018 | | | | |
|---|---------------------------|------------------------------------|--------------------------|----------|-----------|
| | Commercial real estate | Commercial and industrial loans | Residential mortgages | Consumer | Total |
| Individually evaluated for impairment | 15 | 70 | 109 | 1 | 195 |
| Collectively evaluated for impairment | 19,136 | 14,585 | 9,321 | 7,077 | 50,119 |
| Total | \$ 19,151 | \$ 14,655 | \$ 9,430 | \$ 7,078 | \$ 50,314 |

| Business Activities Loans (In thousands) | At December 31, 2017 | | | | |
|---|---------------------------|------------------------------------|--------------------------|----------|--------|
| | Commercial real estate | Commercial and industrial loans | Residential mortgages | Consumer | Total |
| Individually evaluated for impairment | 229 | 66 | 130 | 35 | 460 |
| Collectively evaluated for impairment | 16,614 | 13,784 | 9,290 | 5,772 | 45,460 |
| Total | 16,843 | 13,850 | 9,420 | 5,807 | 45,920 |

| Acquired Loans (In thousands) | At June 30, 2018 | | | | |
|---------------------------------------|---------------------------|--|--------------------------|----------|----------|
| | Commercial real estate | Commercial and industrial loans | Residential mortgages | Consumer | Total |
| Individually evaluated for impairment | 32 | 9 | 6 | 11 | 58 |
| Purchased credit-impaired loans | — | — | — | — | — |
| Collectively evaluated for impairment | 3,350 | 1,118 | 612 | 473 | 5,553 |
| Total | \$ 3,382 | \$ 1,127 | \$ 618 | \$ 484 | \$ 5,611 |

| Acquired Loans (In thousands) | At December 31, 2017 | | | | |
|---------------------------------------|---------------------------|--|--------------------------|----------|-------|
| | Commercial real estate | Commercial and industrial loans | Residential mortgages | Consumer | Total |
| Individually evaluated for impairment | 56 | 1 | 9 | 45 | 111 |
| Collectively evaluated for impairment | 3,800 | 1,124 | 589 | 290 | 5,803 |
| Total | 3,856 | 1,125 | 598 | 335 | 5,914 |

Credit Quality Information

Business Activities Loans Credit Quality Analysis

The Company monitors the credit quality of its portfolio by using internal risk ratings that are based on regulatory guidance. Loans that are given a Pass rating are not considered a problem credit. Loans that are classified as Special Mention loans are considered to have potential credit problems and are evaluated closely by management.

Substandard and non-accruing loans are loans for which a definitive weakness has been identified and which may make full collection of contractual cash flows questionable. Doubtful loans are those with identified weaknesses that make full collection of contractual cash flows, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

For commercial credits, the Company assigns an internal risk rating at origination and reviews the rating annually, semiannually or quarterly depending on the risk rating. The rating is also reassessed at any point in time when management becomes aware of information that may affect the borrower's ability to fulfill their obligations.

The Company risk rates its residential mortgages, including 1-4 family and residential construction loans, based on a three rating system: Pass, Special Mention and Substandard. Loans that are current within 59 days are rated Pass. Residential mortgages that are 60-89 days delinquent are rated Special Mention. Loans delinquent for 90 days

36

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

or greater are rated Substandard and generally placed on non-accrual status. Home equity loans are risk rated based on the same rating system as the Company's residential mortgages.

Ratings for other consumer loans, including auto loans, are based on a two rating system. Loans that are current within 119 days are rated Performing while loans delinquent for 120 days or more are rated Non-performing. Other consumer loans are placed on non-accrual at such time as they become Non-performing.

Acquired Loans Credit Quality Analysis

Upon acquiring a loan portfolio, the Company's internal loan review function assigns risk ratings to the acquired loans, utilizing the same methodology as it does with business activities loans. This may differ from the risk rating policy of the predecessor bank. Loans which are rated Substandard or worse according to the rating process outlined below are deemed to be credit impaired loans accounted for under ASC 310-30, regardless of whether they are classified as performing or non-performing.

The Bank utilizes an eleven grade internal loan rating system for each of its acquired commercial real estate, construction and commercial loans as outlined in the Credit Quality Information section of this Note. The ratings system is similar to loans originated through business activities.

The Company subjects loans that do not meet the ASC 310-30 criteria to ASC 450-20 (Loss Contingencies) by collectively evaluating these loans for an allowance for loan loss. The Company applies a methodology similar to the methodology prescribed for business activities loans, which includes the application of environmental factors to each category of loans. The methodology to collectively evaluate the acquired loans outside the scope of ASC 310-30 includes the application of a number of environmental factors that reflect management's best estimate of the level of incremental credit losses that might be recognized given current conditions. This is reviewed as part of the allowance for loan loss adequacy analysis. As the loan portfolio matures and environmental factors change, the loan portfolio will be reassessed each quarter to determine an appropriate reserve allowance.

Additionally, the Company considers the need for a reserve for acquired loans accounted for outside of the scope of ASC 310-30 under ASC 310-20. At acquisition date, the Bank determined a fair value mark with credit and interest rate components. Under the Company's model, the impairment evaluation process involves comparing the carrying value of acquired loans, including the entire unamortized premium or discount, to the calculated reserve allowance. If necessary, the Company books a reserve to account for shortfalls identified through this calculation. Fair value marks are not bifurcated when evaluating for impairment.

A decrease in the expected cash flows in subsequent periods requires the establishment of an allowance for loan losses at that time for ASC 310-30 loans. At June 30, 2018, the allowance for loan losses related to acquired loans under ASC 310-30 and ASC 310-20 was \$5.6 million using the above mentioned criteria.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following tables present the Company's loans by risk rating at June 30, 2018 and December 31, 2017:

Business Activities Loans

Commercial Real Estate

Credit Risk Profile by Creditworthiness Category

| (In thousands) | Construction | | Single and multi-family Real Estate | | Total commercial real estate | | | |
|-----------------|---------------|-------------------|-------------------------------------|-------------------|------------------------------|-------------------|---------------|-------------------|
| | June 30, 2018 | December 31, 2017 | June 30, 2018 | December 31, 2017 | June 30, 2018 | December 31, 2017 | June 30, 2018 | December 31, 2017 |
| Grade: | | | | | | | | |
| Pass | \$345,896 | \$269,206 | \$375,907 | \$214,289 | \$1,566,673 | \$1,687,256 | \$2,288,476 | \$2,170,751 |
| Special mention | — | — | 459 | 504 | 33,235 | 12,999 | 33,694 | 13,503 |
| Substandard | — | — | 2,068 | 2,290 | 44,758 | 31,163 | 46,826 | 33,453 |
| Total | \$345,896 | \$269,206 | \$378,434 | \$217,083 | \$1,644,666 | \$1,731,418 | \$2,368,996 | \$2,217,707 |

Commercial and Industrial Loans

Credit Risk Profile by Creditworthiness Category

| (In thousands) | Total comm. and industrial loans | |
|-----------------|----------------------------------|-------------------|
| | June 30, 2018 | December 31, 2017 |
| Grade: | | |
| Pass | \$1,325,226 | \$1,156,240 |
| Special mention | 14,697 | 12,806 |
| Substandard | 15,941 | 11,123 |
| Doubtful | — | 2,400 |
| Total | \$1,355,864 | \$1,182,569 |

Residential Mortgages

Credit Risk Profile by Internally Assigned Grade

| (In thousands) | 1-4 family | | Construction | | Total residential mortgages | |
|-----------------|---------------|-------------------|---------------|-------------------|-----------------------------|-------------------|
| | June 30, 2018 | December 31, 2017 | June 30, 2018 | December 31, 2017 | June 30, 2018 | December 31, 2017 |
| Grade: | | | | | | |
| Pass | \$2,126,733 | \$1,805,596 | \$7,289 | \$5,177 | \$2,134,022 | \$1,810,773 |
| Special mention | 445 | 242 | — | — | 445 | 242 |
| Substandard | 2,798 | 2,186 | — | — | 2,798 | 2,186 |
| Total | \$2,129,976 | \$1,808,024 | \$7,289 | \$5,177 | \$2,137,265 | \$1,813,201 |

Consumer Loans

Credit Risk Profile Based on Payment Activity

| (In thousands) | Home equity | | Auto and other | | Total consumer loans | |
|----------------|---------------|-------------------|----------------|-------------------|----------------------|-------------------|
| | June 31, 2018 | December 31, 2017 | June 31, 2018 | December 31, 2017 | June 30, 2018 | December 31, 2017 |
| Performing | \$290,988 | \$293,327 | \$633,185 | \$602,313 | \$924,173 | \$895,640 |
| Nonperforming | 2,462 | 1,627 | 1,619 | 1,454 | 4,081 | 3,081 |
| Total | \$293,450 | \$294,954 | \$634,804 | \$603,767 | \$928,254 | \$898,721 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Acquired Loans

Commercial Real Estate

Credit Risk Profile by Creditworthiness Category

| (In thousands) | Construction | | Single and multi-family | | Real Estate | | Total commercial real estate | |
|-----------------|---------------|-------------------|-------------------------|-------------------|---------------|-------------------|------------------------------|-------------------|
| | June 30, 2018 | December 31, 2017 | June 30, 2018 | December 31, 2017 | June 30, 2018 | December 31, 2017 | June 30, 2018 | December 31, 2017 |
| Grade: | | | | | | | | |
| Pass | \$50,934 | \$76,611 | \$191,132 | \$203,624 | \$641,490 | \$684,846 | \$883,556 | \$965,081 |
| Special mention | — | — | — | 603 | 9,734 | 22,070 | 9,734 | 22,673 |
| Substandard | 8,334 | 8,354 | 4,733 | 1,855 | 43,970 | 49,072 | 57,037 | 59,281 |
| Total | \$59,268 | \$84,965 | \$195,865 | \$206,082 | \$695,194 | \$755,988 | \$950,327 | \$1,047,035 |

Commercial and Industrial Loans

Credit Risk Profile by Creditworthiness Category

| (In thousands) | Total comm. and industrial loans | |
|-----------------|----------------------------------|-------------------|
| | June 30, 2018 | December 31, 2017 |
| Grade: | | |
| Pass | \$ 500,636 | \$ 606,922 |
| Special mention | 1,128 | 1,241 |
| Substandard | 17,490 | 13,207 |
| Total | \$ 519,254 | \$ 621,370 |

Residential Mortgages

Credit Risk Profile by Internally Assigned Grade

| (In thousands) | 1-4 family | | Construction | | Total residential mortgages | |
|-----------------|---------------|-------------------|---------------|-------------------|-----------------------------|-------------------|
| | June 30, 2018 | December 31, 2017 | June 30, 2018 | December 31, 2017 | June 30, 2018 | December 31, 2017 |
| Grade: | | | | | | |
| Pass | \$255,272 | \$281,160 | \$193 | \$233 | \$255,465 | \$281,393 |
| Special mention | 268 | 2,704 | — | — | 268 | 2,704 |
| Substandard | 4,194 | 5,509 | — | — | 4,194 | 5,509 |
| Total | \$259,734 | \$289,373 | \$193 | \$233 | \$259,927 | \$289,606 |

Consumer Loans

Credit Risk Profile Based on Payment Activity

| (In thousands) | Home equity | | Auto and other | | Total consumer loans | |
|----------------|---------------|-------------------|----------------|-------------------|----------------------|-------------------|
| | June 30, 2018 | December 31, 2017 | June 30, 2018 | December 31, 2017 | June 30, 2018 | December 31, 2017 |
| Performing | \$98,464 | \$113,262 | \$90,230 | \$113,510 | \$188,694 | \$226,772 |
| Nonperforming | 916 | 1,965 | 469 | 392 | 1,385 | 2,357 |
| Total | \$99,380 | \$115,227 | \$90,699 | \$113,902 | \$190,079 | \$229,129 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table summarizes information about total loans rated Special Mention or lower as of June 30, 2018 and December 31, 2017. The table below includes consumer loans that are special mention and substandard accruing that are classified in the above table as performing based on payment activity.

| (In thousands) | June 30, 2018 | | | December 31, 2017 | | |
|----------------------|------------------------|----------------|-----------|------------------------|----------------|-----------|
| | Business Activities | Acquired Loans | Total | Business Activities | Acquired Loans | Total |
| Non-Accrual | \$14,196 | \$ 8,833 | \$23,029 | \$15,659 | \$ 7,240 | \$22,899 |
| Substandard Accruing | 55,498 | 71,527 | 127,025 | 36,846 | 73,412 | 110,258 |
| Total Classified | 69,694 | 80,360 | 150,054 | 52,505 | 80,652 | 133,157 |
| Special Mention | 49,314 | 11,380 | 60,694 | 28,387 | 26,802 | 55,189 |
| Total Criticized | \$119,008 | \$ 91,740 | \$210,748 | \$80,892 | \$ 107,454 | \$188,346 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 6. DEPOSITS

A summary of time deposits is as follows:

| (In thousands) | June 30, 2018 | December 31, 2017 |
|----------------------------------|------------------|----------------------|
| Time less than \$100,000 | \$707,398 | \$ 733,785 |
| Time \$100,000 through \$250,000 | 1,906,803 | 1,717,050 |
| Time more than \$250,000 | 445,833 | 439,370 |
| Total time deposits | \$3,060,034 | \$ 2,890,205 |

Included in total deposits are brokered deposits of \$1.3 billion and \$1.1 billion at June 30, 2018 and December 31, 2017, respectively. Included in total deposits are reciprocal deposits of \$94.0 million and \$99.8 million at June 30, 2018 and December 31, 2017, respectively.

NOTE 7. BORROWED FUNDS

Borrowed funds at June 30, 2018 and December 31, 2017 are summarized, as follows:

| (Dollars in thousands) | June 30, 2018 | | December 31, 2017 | |
|---|---------------|-----------------------------|-------------------|-----------------------------|
| | Principal | Weighted Average Rate | Principal | Weighted Average Rate |
| Short-term borrowings: | | | | |
| Advances from the FHLB | \$ 1,002,000 | 2.11 % | \$ 667,300 | 1.48 % |
| Total short-term borrowings: | 1,002,000 | 2.11 | 667,300 | 1.48 |
| Long-term borrowings: | | | | |
| Advances from the FHLB and other borrowings | 272,342 | 1.69 | 380,436 | 1.54 |
| Subordinated borrowings | 73,965 | 7.00 | 73,875 | 7.00 |
| Junior subordinated borrowings | 15,464 | 4.18 | 15,464 | 3.30 |
| Total long-term borrowings: | 361,771 | 2.88 | 469,775 | 2.46 |
| Total | \$ 1,363,771 | 2.32 % | \$ 1,137,075 | 1.88 % |

Short-term debt includes Federal Home Loan Bank ("FHLB") advances with an original maturity of less than one year and a short-term line-of-credit drawdown through a correspondent bank. The Bank also maintains a \$3.0 million secured line of credit with the FHLB that bears a daily adjustable rate calculated by the FHLB. There was no outstanding balance on the FHLB line of credit for the periods ended June 30, 2018 and December 31, 2017.

The Bank is approved to borrow on a short-term basis from the Federal Reserve Bank of Boston as a non-member bank. The Bank has pledged certain loans and securities to the Federal Reserve Bank to support this arrangement. No borrowings with the Federal Reserve Bank took place for the periods ended June 30, 2018 and December 31, 2017.

Long-term FHLB advances consist of advances with an original maturity of more than one year. The advances outstanding at June 30, 2018 include no callable advances and amortizing advances totaling \$1.3 million. The advances outstanding at December 31, 2017 include no callable advances and amortizing advances totaling \$1.4 million. All FHLB borrowings, including the line of credit, are secured by a blanket security agreement on certain qualified collateral, principally all residential first mortgage loans and certain securities.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

A summary of maturities of FHLB advances as of June 30, 2018 is as follows:

| (In thousands, except rates) | June 30, 2018 | |
|-------------------------------|---------------|-----------------------|
| | Principal | Weighted Average Rate |
| Fixed rate advances maturing: | | |
| 2018 | \$ 1,063,993 | 2.07 % |
| 2019 | 150,079 | 1.64 |
| 2020 | 53,371 | 2.04 |
| 2021 | 213 | 2.71 |
| 2022 and beyond | 6,686 | 2.64 |
| Total FHLB advances | \$ 1,274,342 | 2.02 % |

The Company did not have variable-rate FHLB advances for the periods ended June 30, 2018 and December 31, 2017.

In September 2012, the Company issued fifteen year subordinated notes in the amount of \$75.0 million at a discount of 1.15%. The interest rate is fixed at 6.875% for the first ten years. After ten years, the notes become callable and convert to an interest rate of three-month LIBOR rate plus 5.113%. The subordinated note includes reduction to the note principal balance of \$522 thousand and \$583 thousand for unamortized debt issuance costs as of June 30, 2018 and December 31 2017, respectively.

The Company holds 100% of the common stock of Berkshire Hills Capital Trust I ("Trust I") which is included in other assets with a cost of \$0.5 million. The sole asset of Trust I is \$15.5 million of the Company's junior subordinated debentures due in 2035. These debentures bear interest at a variable rate equal to LIBOR plus 1.85% and had a rate of 4.18% and 3.30% at June 30, 2018 and December 31, 2017, respectively. The Company has the right to defer payments of interest for up to five years on the debentures at any time, or from time to time, with certain limitations, including a restriction on the payment of dividends to shareholders while such interest payments on the debentures have been deferred. The Company has not exercised this right to defer payments. The Company has the right to redeem the debentures at par value. Trust I is considered a variable interest entity for which the Company is not the primary beneficiary. Accordingly, Trust I is not consolidated into the Company's financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 8. CAPITAL RATIOS AND SHAREHOLDERS' EQUITY

The actual and required capital ratios were as follows:

| | June 30, 2018 | Regulatory Minimum to be Well Capitalized | December 31, 2017 | Regulatory Minimum to be Well Capitalized |
|--|------------------|---|----------------------|---|
| Company (consolidated) | | | | |
| Total capital to risk weighted assets | 12.8 % | N/A | 12.4 % | N/A |
| Common equity tier 1 capital to risk weighted assets | 11.3 | N/A | 11.0 | N/A |
| Tier 1 capital to risk weighted assets | 11.5 | N/A | 11.2 | N/A |
| Tier 1 capital to average assets | 9.1 | N/A | 9.0 | N/A |
| Bank | | | | |
| Total capital to risk weighted assets | 12.0 % | 8.0 % | 11.2 % | 8.0 % |
| Common equity tier 1 capital to risk weighted assets | 11.1 | 4.5 | 10.3 | 4.5 |
| Tier 1 capital to risk weighted assets | 11.1 | 6.0 | 10.3 | 6.0 |
| Tier 1 capital to average assets | 8.8 | 4.0 | 8.3 | 4.0 |

At each date shown, the Bank met the conditions to be classified as “well capitalized” under the relevant regulatory framework. To be categorized as well capitalized, an institution must maintain minimum total risk-based, Tier 1 risk-based, and Tier 1 leverage ratios as set forth in the table above.

Effective January 1, 2015, the Company and the Bank became subject to the Basel III rule that requires the Company and the Bank to assess their Common equity Tier 1 capital to risk weighted assets. The Bank's Common equity Tier 1 capital to risk weighted assets exceeds the minimum to be well capitalized. In addition, the final capital rules added a requirement to maintain a minimum conservation buffer, composed of Common equity Tier 1 capital, of 2.5% of risk-weighted assets, to be phased in over three years and applied to the Common equity Tier 1 risk-based capital ratio, the Tier 1 risk-based capital ratio, and the Total risk-based capital ratio. Accordingly, banking organizations, on a fully phased in basis no later than January 1, 2019, must maintain a minimum Common equity Tier 1 risk-based capital ratio of 7.0%, a minimum Tier 1 risk-based capital ratio of 8.5%, and a minimum Total risk-based capital ratio of 10.5%.

The required minimum conservation buffer began to be phased in incrementally, starting at 0.625% on January 1, 2016, increased to 1.25% on January 1, 2017, increased to 1.875% on January 1, 2018 and will increase to 2.5% on January 1, 2019. The final capital rules impose restrictions on capital distributions and certain discretionary cash bonus payments if the minimum capital conservation buffer is not met.

At June 30, 2018, the capital levels of both the Company and the Bank exceeded all regulatory capital requirements and the Bank's regulatory capital ratios were above the minimum levels required to be considered well capitalized for regulatory purposes. The capital levels of both the Company and the Bank at June 30, 2018 also exceeded the minimum capital requirements including the currently applicable capital conservation buffer of 1.875%.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Accumulated other comprehensive income (loss)

Components of accumulated other comprehensive income is as follows:

| (In thousands) | June 30, 2018 | December 31, 2017 |
|--|------------------|----------------------|
| Other accumulated comprehensive income, before tax: | | |
| Net unrealized holding loss on AFS securities | \$(25,347) | \$ 10,034 |
| Net unrealized holding loss on pension plans | (3,048) | (3,048) |
| Income taxes related to items of accumulated other comprehensive income: | | |
| Net unrealized holding gain on AFS securities | 6,326 | (4,026) |
| Net unrealized holding loss on pension plans | 803 | 1,201 |
| Accumulated other comprehensive (loss)/income | \$(21,266) | \$ 4,161 |

The following table presents the components of other comprehensive income for the three and six months ended June 30, 2018 and 2017:

| (In thousands) | Before Tax | Tax Effect | Net of Tax |
|---|-------------|-------------|-------------|
| Three Months Ended June 30, 2018 | | | |
| Net unrealized holding (loss) on AFS securities: | x | | |
| Net unrealized (losses) arising during the period | \$ (7,839) | \$ 2,001 | \$ (5,838) |
| Less: reclassification adjustment for gains realized in net income | 1 | — | 1 |
| Net unrealized holding (loss) on AFS securities | (7,840) | 2,001 | (5,839) |
| Other comprehensive (loss) | \$ (7,840) | \$ 2,001 | \$ (5,839) |
| Three Months Ended June 30, 2017 | | | |
| Net unrealized holding gain on AFS securities: | | | |
| Net unrealized gains arising during the period | \$ 3,926 | \$ (1,455) | \$ 2,471 |
| Less: reclassification adjustment for losses realized in net income | (1) | — | (1) |
| Net unrealized holding gain on AFS securities | 3,927 | (1,455) | 2,472 |
| Other comprehensive income | \$ 3,927 | \$ (1,455) | \$ 2,472 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

| (In thousands) | Before Tax | Tax Effect | Net of Tax |
|---|-------------|------------|-------------|
| Six Months Ended June 30, 2018 | | | |
| Net unrealized holding (loss) on AFS securities: | x | | |
| Net unrealized (losses) arising during the period | \$(27,001) | \$ 6,932 | \$(20,069) |
| Less: reclassification adjustment for gains realized in net income | 1 | — | \$1 |
| Net unrealized holding (loss) on AFS securities | (27,002) | 6,932 | \$(20,070) |
| Other comprehensive (loss) | \$(27,002) | \$ 6,932 | \$(20,070) |
| Less: reclassification related to adoption of ASU 2016-01 | 8,379 | (2,126) | 6,253 |
| Less: reclassification related to adoption of ASU 2018-02 | — | (896) | (896) |
| Total change to accumulated other comprehensive (loss) | (35,381) | 9,954 | (25,427) |
| Six Months Ended June 30, 2017 | | | |
| Net unrealized holding gain on AFS securities: | | | |
| Net unrealized gains arising during the period | \$7,064 | \$(2,627) | \$4,437 |
| Less: reclassification adjustment for gains realized in net income | 12,569 | (4,713) | 7,856 |
| Net unrealized holding (loss) on AFS securities | (5,505) | 2,086 | (3,419) |
| Net unrealized loss on cash flow hedging derivatives: | | | |
| Net unrealized (loss) arising during the period | (449) | 180 | (269) |
| Less: reclassification adjustment for (losses) realized in net income | (7,022) | 2,769 | (4,253) |
| Net unrealized gain on cash flow hedging derivatives | 6,573 | (2,589) | 3,984 |
| Other comprehensive income | \$1,068 | \$(503) | \$565 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table presents the changes in each component of accumulated other comprehensive (loss) income, for the three and six months ended June 30, 2018 and 2017:

| (In thousands) | Net unrealized holding gain on AFS Securities | Net loss on effective cash flow hedging derivatives | Net unrealized holding loss on pension plans | Total |
|--|--|--|---|------------|
| Three Months Ended June 30, 2018 | | | | |
| Balance at Beginning of Period | \$ (13,182) | \$ — | \$ (2,245) | \$(15,427) |
| Other comprehensive loss before reclassifications | (5,838) | — | — | (5,838) |
| Less: amounts reclassified from accumulated other comprehensive income (loss) | 1 | — | — | 1 |
| Total other comprehensive (loss) | (5,839) | — | — | (5,839) |
| Balance at End of Period | \$ (19,021) | \$ — | \$ (2,245) | \$(21,266) |
| Three Months Ended June 30, 2017 | | | | |
| Balance at Beginning of Period | \$ 9,649 | \$ — | \$ (1,790) | \$7,859 |
| Other comprehensive gain before reclassifications | 2,471 | — | — | 2,471 |
| Less: amounts reclassified from accumulated other comprehensive income (loss) | (1) | — | — | (1) |
| Total other comprehensive income | 2,472 | — | — | 2,472 |
| Balance at End of Period | \$ 12,121 | \$ — | \$ (1,790) | \$10,331 |
| Six Months Ended June 30, 2018 | | | | |
| Balance at Beginning of Period | \$ 6,008 | \$ — | \$ (1,847) | \$4,161 |
| Other comprehensive (loss) before reclassifications | (20,069) | — | — | (20,069) |
| Less: amounts reclassified from accumulated other comprehensive income | 1 | — | — | 1 |
| Total other comprehensive (loss) | (20,070) | — | — | (20,070) |
| Less: amounts reclassified from accumulated other comprehensive income (loss) related to adoption of ASU 2016-01 and ASU 2018-02 | \$ 4,959 | \$ — | \$ 398 | \$5,357 |
| Balance at End of Period | \$ (19,021) | \$ — | \$ (2,245) | \$(21,266) |
| Six Months Ended June 30, 2017 | | | | |
| Balance at Beginning of Period | \$ 15,540 | \$ (3,984) | \$ (1,790) | \$9,766 |
| Other comprehensive gain (loss) before reclassifications | 4,437 | (269) | — | 4,168 |
| Less: amounts reclassified from accumulated other comprehensive income | 7,856 | (4,253) | — | 3,603 |
| Total other comprehensive (loss) income | (3,419) | 3,984 | — | 565 |
| Balance at End of Period | \$ 12,121 | \$ — | \$ (1,790) | \$10,331 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table presents the amounts reclassified out of each component of accumulated other comprehensive (loss) income for the three and six months ended June 30, 2018 and 2017:

| | Three Months Ended June 30, 2018 | Affected Line Item in the Statement where Net Income is Presented |
|---|--|---|
| (In thousands) | | |
| Realized gains on AFS securities: | \$1 | Non-interest income |
| | (1) | Tax expense |
| | | Net of tax |
| Realized (losses) on cash flow hedging derivatives: | | |
| | | Interest expense |
| | | Non-interest expense |
| | | Tax benefit |
| | | Net of tax |
| Total reclassifications for the period | \$1 | Net of tax |
| | | Affected Line Item in the |
| | Six Months Ended June 30, 2017 | Statement where Net Income is Presented |
| (In thousands) | | |
| Realized gains on AFS securities: | \$1 | Non-interest income |
| | (12,569) | Tax expense |
| | | Net of tax |
| Realized (losses) on cash flow hedging derivatives: | | |
| | (393) | Interest expense |
| | (6,629) | Non-interest expense |
| | 2,769 | Tax benefit |
| | | Net of tax |
| Total reclassifications for the period | \$1 | Net of tax |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 9. EARNINGS PER SHARE

Earnings per share have been computed based on the following (average diluted shares outstanding are calculated using the treasury stock method):

| (In thousands, except per share data) | Three Months | | Six Months | |
|--|----------------|----------|----------------|----------|
| | Ended June 30, | | Ended June 30, | |
| | 2018 | 2017 | 2018 | 2017 |
| Net income | \$34,031 | \$19,694 | \$59,279 | \$35,154 |
| Average number of common shares issued | 46,212 | 38,720 | 46,212 | 37,731 |
| Less: average number of treasury shares | 788 | 943 | 828 | 981 |
| Less: average number of unvested stock award shares | 435 | 453 | 428 | 445 |
| Plus: average participating preferred shares | 1,043 | — | 1,043 | — |
| Average number of basic shares outstanding | 46,032 | 37,324 | 45,999 | 36,305 |
| Plus: dilutive effect of unvested stock award shares | 152 | 106 | 176 | 116 |
| Plus: dilutive effect of stock options outstanding | 31 | 44 | 31 | 45 |
| Average number of diluted shares outstanding | 46,215 | 37,474 | 46,206 | 36,466 |
| Earnings per common share: | | | | |
| Basic | \$0.74 | \$0.53 | \$1.29 | \$0.97 |
| Diluted | \$0.74 | \$0.53 | \$1.28 | \$0.96 |

For the six months ended June 30, 2018, 252 thousand shares of restricted stock and 33 thousand options were anti-dilutive and therefore excluded from the earnings per share calculations. For the six months ended June 30, 2017, 327 thousand shares of restricted stock and 48 thousand options were anti-dilutive and therefore excluded from the earnings per share calculations.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 10. STOCK-BASED COMPENSATION PLANS

A combined summary of activity in the Company's stock award and stock option plans for the six months ended June 30, 2018 is presented in the following table:

| (Shares in thousands) | Non-Vested Stock Awards Outstanding | | Stock Options Outstanding | |
|--------------------------------------|-------------------------------------|--|---------------------------|---------------------------------|
| | Number of Shares | Weighted-Average Grant Date Fair Value | Number of Shares | Weighted-Average Exercise Price |
| December 31, 2017 | 418 | \$ 29.68 | 76 | \$ 13.59 |
| Granted | 181 | 37.81 | — | — |
| Stock options exercised | — | — | (8) | 12.46 |
| Stock awards vested | (150) | 28.65 | — | — |
| Forfeited | (15) | 32.93 | — | — |
| Expired | — | — | (11) | 22.61 |
| June 30, 2018 | 434 | \$ 33.18 | 57 | \$ 10.61 |
| Exercisable options at June 30, 2018 | | | 57 | \$ 10.61 |

During the six months ended June 30, 2018 and 2017, proceeds from stock option exercises totaled \$101 thousand and \$111 thousand, respectively. During the six months ended June 30, 2018, there were 150 thousand shares issued in connection with vested stock awards. During the six months ended June 30, 2017, there were 133 thousand shares issued in connection with vested stock awards. All of these shares were issued from available treasury stock. Stock-based compensation expense totaled \$2.8 million and \$2.5 million during the six months ended June 30, 2018 and 2017, respectively. Stock-based compensation expense is recognized over the requisite service period for all awards.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 11. DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES

As of June 30, 2018, the Company held derivatives with a total notional amount of \$3.0 billion. The Company had economic hedges and non-hedging derivatives totaling \$2.7 billion and \$0.3 billion, respectively, which are not designated as hedges for accounting purposes with changes in fair value recorded directly through earnings. Economic hedges included interest rate swaps totaling \$2.2 billion, risk participation agreements with dealer banks of \$0.2 billion, and \$0.3 billion in forward commitment contracts.

As part of the Company's risk management strategy, the Company enters into interest rate swap agreements to mitigate the interest rate risk inherent in certain of the Company's assets and liabilities. Interest rate swap agreements involve the risk of dealing with both Bank customers and institutional derivative counterparties and their ability to meet contractual terms. The agreements are entered into with counterparties that meet established credit standards and contain master netting and collateral provisions protecting the at-risk party. The derivatives program is overseen by the Risk Management/Capital Committee of the Company's Board of Directors. Based on adherence to the Company's credit standards and the presence of the netting and collateral provisions, the Company believes that the credit risk inherent in these contracts was not significant at June 30, 2018.

The Company pledged collateral to derivative counterparties in the form of cash totaling \$6.9 million and securities with an amortized cost of \$14.3 million and a fair value of \$13.9 million as of June 30, 2018. The Company does not typically require its commercial customers to post cash or securities as collateral on its program of back-to-back economic hedges. However certain language is written into the International Swaps Dealers Association, Inc. ("ISDA") and loan documents where, in default situations, the Bank is allowed to access collateral supporting the loan relationship to recover any losses suffered on the derivative asset or liability. The Company may need to post additional collateral in the future in proportion to potential increases in unrealized loss positions.

Information about derivative assets and liabilities at June 30, 2018, follows:

| | Notional Amount (In thousands) | Weighted Average Maturity (In years) | Weighted Received | Weighted Average Rate Contract pay rate | Estimated Fair Value Asset (Liability) (In thousands) |
|---|--------------------------------------|---|----------------------|---|--|
| Cash flow hedges: | | | | | |
| Interest rate swaps on FHLB borrowings | \$ — | 0 | — | % | \$ — |
| Total cash flow hedges | — | | | | — |
| Economic hedges: | | | | | |
| Interest rate swap on tax advantaged economic development bond | 10,426 | 11.4 | 2.35 | % | 5.09 % (1,175) |
| Interest rate swaps on loans with commercial loan customers | 1,094,198 | 6.3 | 3.90 | % | 4.40 % 16,744 |
| Reverse interest rate swaps on loans with commercial loan customers | 1,094,198 | 6.3 | 4.40 | % | 3.90 % (16,403) |
| Risk participation agreements with dealer banks | 183,986 | 6.2 | | | (3) |
| Forward sale commitments | 338,884 | 0.2 | | | (658) |
| Total economic hedges | 2,721,692 | | | | (1,495) |
| Non-hedging derivatives: | | | | | |
| Commitments to lend | 289,750 | 0.2 | | | 7,285 |
| Total non-hedging derivatives | 289,750 | | | | 7,285 |

| | | |
|-------|--------------|----------|
| Total | \$ 3,011,442 | \$ 5,790 |
|-------|--------------|----------|

50

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Information about derivative assets and liabilities at December 31, 2017, follows:

| | Notional Amount (In thousands) | Weighted Average Maturity (In years) | Weighted Received | Average Rate Contract pay rate | Estimated Fair Value Asset (Liability) (In thousands) |
|---|--------------------------------------|---|----------------------|--------------------------------------|--|
| Cash flow hedges: | | | | | |
| Interest rate swaps on FHLB borrowings | \$ — | 0 | — % | — % | \$ — |
| Total cash flow hedges | — | | | | — |
| Economic hedges: | | | | | |
| Interest rate swap on tax advantaged economic development bond | 10,755 | 11.9 | 1.73 % | 5.09 % | (1,649) |
| Interest rate swaps on loans with commercial loan customers | 943,795 | 5.9 | 3.26 % | 4.25 % | (3,195) |
| Reverse interest rate swaps on loans with commercial loan customers | 943,795 | 5.9 | 4.25 % | 3.26 % | 3,204 |
| Risk participation agreements with dealer banks | 142,054 | 8.4 | | | (26) |
| Forward sale commitments | 276,572 | 0.2 | | | (123) |
| Total economic hedges | 2,316,971 | | | | (1,789) |
| Non-hedging derivatives: | | | | | |
| Commitments to lend | 193,966 | 0.2 | | | 5,259 |
| Total non-hedging derivatives | 193,966 | | | | 5,259 |
| Total | \$ 2,510,937 | | | | \$ 3,470 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Cash flow hedges

In the first quarter of 2017, the Company maintained six interest rate swap contracts with an aggregate notional value of \$300 million with original durations of three years. This hedge strategy converted one month rolling FHLB borrowings based on the FHLB's one month fixed interest rate to fixed interest rates, thereby protecting the Company from floating interest rate variability.

On February 7, 2017, the Company initiated and subsequently terminated all of its interest rate swaps associated with FHLB advances with 1-month LIBOR based floating interest rates of an aggregate notional amount of \$300 million. As of March 31, 2017, the Company no longer held the FHLB advances associated with the interest rate swaps. As a result, the Company reclassified \$6.6 million of losses from the effective portion of the unrealized changes in the fair value of the terminated derivatives from other comprehensive income to non-interest income as the forecasted transactions to the related FHLB advances will not occur.

For the periods presented prior to the termination, the effective portion of unrealized changes in the fair value of derivatives accounted for as cash flow hedges was reported in other comprehensive income. Each quarter, the Company assessed the effectiveness of each hedging relationship by comparing the changes in cash flows of the derivative hedging instrument with the changes in cash flows of the designated hedged item or transaction. Hedge ineffectiveness on interest rate swaps designated as cash flow hedges was immaterial to the Company's financial statements during the three and six months ended June 30, 2017.

Amounts included in the Consolidated Statements of Income and in the other comprehensive income section of the Consolidated Statements of Comprehensive Income (related to interest rate derivatives designated as hedges of cash flows), were as follows:

| | Three Months Ended June 30, 2018 | Six Months Ended June 30, 2017 |
|---|--|--|
| (In thousands) | | |
| Interest rate swaps on FHLB borrowings: | | |
| Unrealized (loss) recognized in accumulated other comprehensive loss | \$ — | \$ (449) |
| Less: reclassification of unrealized (loss) from accumulated other comprehensive income to interest expense | — | (393) |
| Less: reclassification of unrealized (loss) from accumulated other comprehensive income to other non-interest expense | — | (6,629) |
| Net tax (expense) benefit on items recognized in accumulated other comprehensive income | — | (2,589) |
| Other comprehensive gain (loss) recorded in accumulated other comprehensive income, net of reclassification adjustments and tax effects | \$ — | \$ 3,984 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Economic hedges

As of June 30, 2018, the Company has an interest rate swap with a \$10.4 million notional amount to swap out the fixed rate of interest on an economic development bond bearing a fixed rate of 5.09%, currently within the Company's trading portfolio under the fair value option, in exchange for a LIBOR-based floating rate. The intent of the economic hedge is to improve the Company's asset sensitivity to changing interest rates in anticipation of favorable average floating rates of interest over the 21-year life of the bond. The fair value changes of the economic development bond are mostly offset by fair value changes of the related interest rate swap.

The Company also offers certain derivative products directly to qualified commercial borrowers. The Company economically hedges derivative transactions executed with commercial borrowers by entering into mirror-image, offsetting derivatives with third-party financial institutions. The transaction allows the Company's customer to convert a variable-rate loan to a fixed rate loan. Because the Company acts as an intermediary for its customer, changes in the fair value of the underlying derivative contracts mostly offset each other in earnings. Credit valuation adjustments arising from the difference in credit worthiness of the commercial loan and financial institution counterparties totaled \$332 thousand as of June 30, 2018. The interest income and expense on these mirror image swaps exactly offset each other.

The Company has risk participation agreements with dealer banks. Risk participation agreements occur when the Company participates on a loan and a swap where another bank is the lead. The Company gets paid a fee to take on the risk associated with having to make the lead bank whole on Berkshire's portion of the pro-rated swap should the borrower default. Changes in fair value are recorded in current period earnings.

The Company utilizes forward sale commitments to hedge interest rate risk and the associated effects on the fair value of interest rate lock commitments and loans originated for sale. The forward sale commitments are accounted for as derivatives with changes in fair value recorded in current period earnings.

The Company uses the following types of forward sale commitments contracts:

- Best efforts loan sales,
- Mandatory delivery loan sales, and
- To Be Announced ("TBA") mortgage-backed securities sales.

A best efforts contract refers to a loan sale agreement where the Company commits to deliver an individual mortgage loan of a specified principal amount and quality to an investor if the loan to the underlying borrower closes. The Company may enter into a best efforts contract once the price is known, which is shortly after the potential borrower's interest rate is locked.

A mandatory delivery contract is a loan sale agreement where the Company commits to deliver a certain principal amount of mortgage loans to an investor at a specified price on or before a specified date. Generally, the Company may enter into mandatory delivery contracts shortly after the loan closes with a customer.

The Company may sell TBA mortgage-backed securities to hedge the changes in fair value of interest rate lock commitments and held for sale loans, which do not have corresponding best efforts or mandatory delivery contracts. These security sales transactions are closed once mandatory contracts are written. On the closing date the price of the security is locked-in, and the sale is paired-off with a purchase of the same security. Settlement of the security purchase/sale transaction is done with cash on a net-basis.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Non-hedging derivatives

The Company enters into interest rate lock commitments (“IRLCs”) for residential mortgage loans, which commit the Company to lend funds to a potential borrower at a specific interest rate and within a specified period of time. IRLCs that relate to the origination of mortgage loans that will be held for sale are considered derivative financial instruments under applicable accounting guidance. Outstanding IRLCs expose the Company to the risk that the price of the mortgage loans underlying the commitments may decline due to increases in mortgage interest rates from inception of the rate lock to the funding of the loan. The IRLCs are free-standing derivatives which are carried at fair value with changes recorded in noninterest income in the Company’s consolidated statements of income. Changes in the fair value of IRLCs subsequent to inception are based on changes in the fair value of the underlying loan resulting from the fulfillment of the commitment and changes in the probability that the loan will fund within the terms of the commitment, which is affected primarily by changes in interest rates and the passage of time.

Amounts included in the Consolidated Statements of Income related to economic hedges and non-hedging derivatives were as follows:

| (In thousands) | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|--------------------------------|---------|------------------------------|----------|
| | 2018 | 2017 | 2018 | 2017 |
| Economic hedges | | | | |
| Interest rate swap on industrial revenue bond: | | | | |
| Unrealized gain recognized in other non-interest income | \$163 | \$2 | \$474 | \$124 |
| Interest rate swaps on loans with commercial loan customers: | | | | |
| Unrealized gain/(loss) recognized in other non-interest income | 5,270 | (3,810) | 19,939 | (1,682) |
| Reverse interest rate swaps on loans with commercial loan customers: | | | | |
| Unrealized gain/(loss) recognized in other non-interest income | (5,270) | 3,810 | (19,939) | 1,682 |
| Favorable (Unfavorable) change in credit valuation adjustment recognized in other non-interest income | 95 | (114) | 332 | (276) |
| Risk participation agreements: | | | | |
| Unrealized gain recognized in other non-interest income | 7 | 23 | 23 | 5 |
| Forward commitments: | | | | |
| Unrealized (loss) gain recognized in other non-interest income | (658) | 975 | (1,567) | (276) |
| Realized gain (loss) in other non-interest income | 1,077 | 238 | 4,999 | (2,668) |
| Non-hedging derivatives | | | | |
| Commitments to lend | | | | |
| Unrealized gain recognized in other non-interest income | \$7,285 | \$7,375 | \$13,816 | \$15,436 |
| Realized gain in other non-interest income | 2,491 | 7,693 | 3,094 | 16,467 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Assets and Liabilities Subject to Enforceable Master Netting Arrangements

Interest Rate Swap Agreements ("Swap Agreements")

The Company enters into swap agreements to facilitate the risk management strategies for commercial banking customers. The Company mitigates this risk by entering into equal and offsetting swap agreements with highly rated third party financial institutions. The swap agreements are free-standing derivatives and are recorded at fair value in the Company's consolidated statements of condition. The Company is party to master netting arrangements with its financial institution counterparties; however, the Company does not offset assets and liabilities under these arrangements for financial statement presentation purposes. The master netting arrangements provide for a single net settlement of all swap agreements, as well as collateral, in the event of default on, or termination of, any one contract. Collateral generally in the form of marketable securities is received or posted by the counterparty with net liability positions, respectively, in accordance with contract thresholds.

The Company had net asset positions with its financial institution counterparties totaling \$18.6 million and \$1.1 million as of June 30, 2018 and December 31, 2017, respectively. The Company had net asset positions with its commercial banking counterparties totaling \$4.5 million and \$8.6 million as of June 30, 2018 and December 31, 2017, respectively. The Company had net liability positions with its financial institution counterparties totaling \$3.1 million and \$5.9 million as of June 30, 2018 and December 31, 2017, respectively. The Company had net liability positions with its commercial banking counterparties totaling \$20.9 million and \$5.4 million as of June 30, 2018 and December 31, 2017. The collateral posted by the Company that covered liability positions was \$6.9 million and \$5.9 million as of June 30, 2018 and December 31, 2017, respectively.

The following table presents the assets and liabilities subject to an enforceable master netting arrangement as of June 30, 2018 and December 31, 2017:

Offsetting of Financial Assets and Derivative Assets

| (In thousands) | Gross Amounts of Assets Recognized | Gross Amounts of Offset in the Statements of Condition | Net Amounts of Assets Presented in the Statements of Condition | Gross Amounts Not Offset in the Statements of Condition | | Net Amount |
|--------------------------------|------------------------------------|--|--|---|--------------------------|------------|
| | | | | Financial Instruments | Cash Collateral Received | |
| June 30, 2018 | | | | | | |
| Interest Rate Swap Agreements: | | | | | | |
| Institutional counterparties | \$ 20,015 | \$ (1,386) | \$ 18,629 | \$ — | \$ — | \$ 18,629 |
| Commercial counterparties | 4,546 | — | 4,546 | — | — | 4,546 |
| Total | \$ 24,561 | \$ (1,386) | \$ 23,175 | \$ — | \$ — | \$ 23,175 |

Offsetting of Financial Liabilities and Derivative Liabilities

| (In thousands) | Gross Amounts of Liabilities Recognized | Gross Amounts of Offset in the Statements of Condition | Net Amounts of Liabilities Presented in the Statements of Condition | Gross Amounts Not Offset in the Statements of Condition | | Net Amount |
|--------------------------------|---|--|---|---|-------------------------|------------|
| | | | | Financial Instruments | Cash Collateral Pledged | |
| June 30, 2018 | | | | | | |
| Interest Rate Swap Agreements: | | | | | | |
| Institutional counterparties | \$ (4,468) | \$ 1,404 | \$ (3,064) | \$ — | \$ 6,853 | \$ 3,789 |
| Commercial counterparties | (21,058) | 109 | (20,949) | — | — | (20,949) |

Total \$ (25,526) \$ 1,513 \$ (24,013) \$ — \$ 6,853 \$ (17,160)

55

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Offsetting of Financial Assets and Derivative Assets

| (In thousands) | Gross Amounts of Recognized Assets | Gross Amounts of Offset in the Statements of Condition | Net Amounts of Assets Presented in the Statements of Condition | Gross Amounts Not Offset in the Statements of Condition | | Net Amount |
|-----------------------------------|---|---|--|--|-----------------------------|------------|
| | | | | Financial Instruments | Cash Collateral Received | |
| December 31, 2017 | | | | | | |
| Interest Rate Swap Agreements: | | | | | | |
| Institutional counterparties | \$ 2,692 | \$ (1,622) | \$ 1,070 | \$ — | \$ — | \$ 1,070 |
| Commercial counterparties | 8,577 | — | 8,577 | — | — | 8,577 |
| Total | \$ 11,269 | \$ (1,622) | \$ 9,647 | \$ — | \$ — | \$ 9,647 |

Offsetting of Financial Liabilities and Derivative Liabilities

| (In thousands) | Gross Amounts of Recognized Liabilities | Gross Amounts of Offset in the Statements of Condition | Net Amounts of Liabilities Presented in the Statements of Condition | Gross Amounts Not Offset in the Statements of Condition | | Net Amount |
|-----------------------------------|--|---|---|--|----------------------------|-------------|
| | | | | Financial Instruments | Cash Collateral Pledged | |
| December 31, 2017 | | | | | | |
| Interest Rate Swap Agreements: | | | | | | |
| Institutional counterparties | \$(8,777) | \$ 2,835 | \$(5,942) | \$ 3,982 | \$ 1,960 | \$ — |
| Commercial counterparties | (5,375) | 2 | (5,373) | — | — | (5,373) |
| Total | \$(14,152) | \$ 2,837 | \$(11,315) | \$ 3,982 | \$ 1,960 | \$ (5,373) |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 12. FAIR VALUE MEASUREMENTS

A description of the valuation methodologies used for assets and liabilities measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below. These valuation methodologies were applied to all of the Company's financial assets and financial liabilities that are carried at fair value.

Recurring Fair Value Measurements

The following table summarizes financial assets and financial liabilities measured at fair value on a recurring basis as of June 30, 2018 and December 31, 2017, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value.

| (In thousands) | June 30, 2018 | | | |
|---|-------------------|-------------------|-------------------|---------------------|
| | Level 1 Inputs | Level 2 Inputs | Level 3 Inputs | Total Fair Value |
| Trading security | \$— | \$— | —\$11,483 | \$ 11,483 |
| Securities available for sale: | | | | |
| Municipal bonds and obligations | — | 112,137 | — | 112,137 |
| Agency collateralized mortgage obligations | — | 915,217 | — | 915,217 |
| Agency residential mortgage-backed securities | — | 184,670 | — | 184,670 |
| Agency commercial mortgage-backed securities | — | 59,513 | — | 59,513 |
| Corporate bonds | — | 101,062 | — | 101,062 |
| Trust preferred securities | — | 11,614 | — | 11,614 |
| Other bonds and obligations | — | 9,037 | — | 9,037 |
| Marketable equity securities | 59,726 | — | — | 59,726 |
| Loans held for sale | — | 149,182 | — | 149,182 |
| Derivative assets | — | 26,031 | 7,285 | 33,316 |
| Capitalized servicing rights | — | — | 7,839 | 7,839 |
| Derivative liabilities | — | 27,527 | — | 27,527 |
| | December 31, 2017 | | | |
| (In thousands) | Level 1 Inputs | Level 2 Inputs | Level 3 Inputs | Total Fair Value |
| Trading security | \$— | \$— | —\$12,277 | \$ 12,277 |
| Securities available for sale: | | | | |
| Municipal bonds and obligations | — | 118,233 | — | 118,233 |
| Agency collateralized mortgage obligations | — | 851,158 | — | 851,158 |
| Agency residential mortgage-backed securities | — | 216,940 | — | 216,940 |
| Agency commercial mortgage-backed securities | — | 62,305 | — | 62,305 |
| Corporate bonds | — | 110,721 | — | 110,721 |
| Trust preferred securities | — | 11,677 | — | 11,677 |
| Other bonds and obligations | — | 9,880 | — | 9,880 |
| Marketable equity securities | 45,185 | — | — | 45,185 |
| Loans held for sale | — | 153,620 | — | 153,620 |
| Derivative assets | — | 14,049 | 5,259 | 19,308 |
| Capitalized servicing rights | — | — | 3,834 | 3,834 |
| Derivative liabilities | — | 15,838 | 19 | 15,838 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

There were no transfers between levels during the six months ended June 30, 2018 or June 30, 2017.

Trading Security at Fair Value. The Company holds one security designated as a trading security. It is a tax advantaged economic development bond issued to the Company by a local nonprofit which provides wellness and health programs. The determination of the fair value for this security is determined based on a discounted cash flow methodology. Certain inputs to the fair value calculation are unobservable and there is little to no market activity in the security; therefore, the security meets the definition of a Level 3 security. The discount rate used in the valuation of the security is sensitive to movements in the 3-month LIBOR rate.

Securities Available for Sale and Marketable Equity Securities. Marketable equity securities classified as Level 1 consist of publicly-traded equity securities for which the fair values can be obtained through quoted market prices in active exchange markets. AFS and marketable equity securities classified as Level 2 include most of the Company's debt securities. The pricing on Level 2 was primarily sourced from third party pricing services, overseen by management, and is based on models that consider standard input factors such as dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond's terms and condition, among other things.

June 30, 2018

| (In thousands) | Fair Value | Amortized Cost | Gains |
|------------------------------|------------|----------------|---------|
| Marketable equity securities | \$ 59,726 | \$ 55,618 | \$4,108 |

December 31, 2017

| (In thousands) | Fair Value | Amortized Cost | Gains |
|------------------------------|------------|----------------|---------|
| Marketable equity securities | \$ 45,185 | \$ 36,483 | \$8,702 |

Loans Held for Sale. The Company elected the fair value option for all loans held for sale (HFS) originated for sale on or after May 1, 2012. Loans HFS are classified as Level 2 as the fair value is based on input factors such as quoted prices for similar loans in active markets.

| June 30, 2018 | Aggregate Fair Value | Aggregate Unpaid Principal | Aggregate Fair Value Less Aggregate Unpaid Principal |
|---------------------|----------------------|----------------------------|--|
| (In thousands) | Fair Value | Unpaid Principal | Unpaid Principal |
| Loans Held for Sale | \$ 149,182 | \$ 145,723 | \$ 3,459 |

| December 31, 2017 | Aggregate Fair Value | Aggregate Unpaid Principal | Aggregate Fair Value Less Aggregate Unpaid Principal |
|---------------------|----------------------|----------------------------|--|
| (In thousands) | Fair Value | Unpaid Principal | Unpaid Principal |
| Loans Held for Sale | \$ 153,620 | \$ 149,022 | \$ 4,598 |

The changes in fair value of loans held for sale for the three and six months ended June 30, 2018, were gains of \$1.3 million and losses of \$1.1 million, respectively. The changes in fair value of loans held for sale for the three and six months ended June 30, 2017, were gains of \$1.7 million and \$2.3 million, respectively. The changes in fair value are included in mortgage banking originations in the Consolidated Statements of Income.

Interest Rate Swaps. The valuation of the Company's interest rate swaps is obtained from a third-party pricing service and is determined using a discounted cash flow analysis on the expected cash flows of each derivative. The pricing analysis is based on observable inputs for the contractual terms of the derivatives, including the period to maturity and

interest rate curves.

The Company incorporates credit valuation adjustments to appropriately reflect both its own nonperformance risk and the respective counterparty's nonperformance risk in the fair value measurements. In adjusting the fair value of

58

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

its derivative contracts for the effect of nonperformance risk, the Company has considered the impact of netting and any applicable credit enhancements, such as collateral postings.

Although the Company has determined that the majority of the inputs used to value its interest rate derivatives fall within Level 2 of the fair value hierarchy, the credit valuation adjustments associated with its derivatives utilize Level 3 inputs, such as estimates of current credit spreads to evaluate the likelihood of default by itself and its counterparties. However, as of June 30, 2018, the Company assessed the significance of the impact of the credit valuation adjustments on the overall valuation of its derivative positions and determined that the credit valuation adjustments are not significant to the overall valuation of its derivatives. As a result, the Company determined that its derivative valuations in their entirety are classified in Level 2 of the fair value hierarchy.

Commitments to Lend. The Company enters into commitments to lend for residential mortgage loans intended for sale, which commit the Company to lend funds to a potential borrower at a specific interest rate and within a specified period of time. The estimated fair value of commitments to originate residential mortgage loans for sale is based on quoted prices for similar loans in active markets. However, this value is adjusted by a factor which considers the likelihood that the loan in a lock position will ultimately close, and by the non-refundable costs of originating the loan. The closing ratio is derived from the Bank's internal data and is adjusted using significant management judgment. The costs to originate are primarily based on the Company's internal commission rates that are not observable. As such, these commitments are classified as Level 3 measurements.

Forward Sale Commitments. The Company utilizes forward sale commitments as economic hedges against potential changes in the values of the commitments to lend and loans originated for sale. To Be Announced ("TBA") mortgage-backed securities forward commitment sales are used as the hedging instrument, are classified as Level 1, and consist of publicly-traded debt securities for which identical fair values can be obtained through quoted market prices in active exchange markets. The fair values of the Company's best efforts and mandatory delivery loan sale commitments are determined similarly to the commitments to lend using quoted prices in the market place that are observable. However, costs to originate and closing ratios included in the calculation are internally generated and are based on management's judgment and prior experience, which are considered factors that are not observable. As such, best efforts and mandatory forward commitments are classified as Level 3 measurements.

Capitalized Servicing Rights. The Company accounts for certain capitalized servicing rights at fair value in its Consolidated Financial Statements, as the Company is permitted to elect the fair value option for each specific instrument. A loan servicing right asset represents the amount by which the present value of the estimated future net cash flows to be received from servicing loans exceed adequate compensation for performing the servicing. The fair value of servicing rights is estimated using a present value cash flow model. The most important assumptions used in the valuation model are the anticipated rate of the loan prepayments and discount rates. Although some assumptions in determining fair value are based on standards used by market participants, some are based on unobservable inputs and therefore are classified in Level 3 of the valuation hierarchy. These capitalized servicing rights are included in other assets on the consolidated balance sheet.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The table below presents the changes in Level 3 assets and liabilities that were measured at fair value on a recurring basis for the three and six months ended June 30, 2018 and 2017.

| (In thousands) | Assets (Liabilities) | | | |
|---|----------------------|---------------------|---------------------|------------------------------|
| | Trading Security | Commitments to Lend | Forward Commitments | Capitalized Servicing Rights |
| Three Months Ended June 30, 2018 | | | | |
| March 31, 2018 | \$ 11,795 | \$ 6,531 | \$ — | \$ 5,705 |
| Unrealized (loss) gain, net recognized in other non-interest income | (148) | 12,787 | — | 339 |
| Paydown of trading security | (164) | — | — | — |
| Transfers to held for sale loans | — | (12,033) | — | — |
| Additions to servicing rights | — | — | — | 1,795 |
| June 30, 2018 | \$ 11,483 | \$ 7,285 | \$ — | \$ 7,839 |
| Six Months Ended June 30, 2018 | | | | |
| December 31, 2017 | \$ 12,277 | \$ 5,259 | \$ 19 | \$ 3,834 |
| Unrealized (loss) gain, net recognized in other non-interest income | (465) | 25,000 | (19) | 804 |
| Paydown of trading security | (329) | — | — | — |
| Transfers to held for sale loans | — | (22,974) | — | — |
| Additions to servicing rights | \$ — | \$ — | \$ — | \$ 3,201 |
| June 30, 2018 | \$ 11,483 | \$ 7,285 | \$ — | \$ 7,839 |
| Unrealized gains (losses) relating to instruments still held at June 30, 2018 | \$ 1,056 | \$ 7,285 | \$ — | \$ — |

| (In thousands) | Assets (Liabilities) | | | |
|---|----------------------|---------------------|---------------------|------------------------------|
| | Trading Security | Commitments to Lend | Forward Commitments | Capitalized Servicing Rights |
| Three Months Ended June 30, 2017 | | | | |
| March 31, 2017 | \$ 12,966 | \$ 8,061 | \$ (22) | \$ 976 |
| Unrealized gain (loss), net recognized in other non-interest income | 27 | 16,515 | 34 | (68) |
| Paydown of trading security | (156) | — | — | — |
| Transfers to held for sale loans | — | (17,202) | — | — |
| Additions to servicing rights | — | — | — | 660 |

Edgar Filing: BERKSHIRE HILLS BANCORP INC - Form 10-Q

| | | | | |
|---|----------|----------|-------|----------|
| June 30, 2017 | \$12,837 | \$ 7,374 | \$ 12 | \$ 1,568 |
| Six Months Ended June 30, 2017 | | | | |
| December 31, 2016 | \$13,229 | \$4,738 | \$100 | \$798 |
| Unrealized (loss) gain, net recognized in other non-interest income | (79) | 33,817 | (88) | (70) |
| Paydown of trading security | (313) | — | — | — |
| Transfers to held for sale loans | — | (31,181) | — | — |
| Additions to servicing rights | \$— | \$— | \$— | \$840 |
| June 30, 2017 | \$12,837 | \$7,374 | \$12 | \$1,568 |
| Unrealized gains (losses) relating to instruments still held at June 30, 2017 | \$1,736 | \$7,374 | \$12 | \$— |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Quantitative information about the significant unobservable inputs within Level 3 recurring assets and liabilities is as follows:

| (In thousands) | Fair Value | | Significant Unobservable Input | |
|------------------------------|-------------------|----------------------|--------------------------------|----------|
| | June 30, 2018 | Valuation Techniques | Unobservable Inputs | Value |
| Assets (Liabilities) | | | | |
| Trading security | \$ 11,483 | Discounted Cash Flow | Discount Rate | 3.32 % |
| Commitments to lend | 7,285 | Historical Trend | Closing Ratio | 83.54 % |
| | | Pricing Model | Origination Costs, per loan | \$ 3,063 |
| Forward commitments | — | Historical Trend | Closing Ratio | 83.54 % |
| | | Pricing Model | Origination Costs, per loan | \$ 3,063 |
| Capitalized servicing rights | 7,839 | Discounted cash flow | Constant Prepayment Rate (CPR) | 8.00 % |
| | | | Discount Rate | 9.96 % |
| Total | \$ 26,607 | | | |
| (In thousands) | Fair Value | | Significant Unobservable Input | |
| | December 31, 2017 | Valuation Techniques | Unobservable Inputs | Value |
| Assets (Liabilities) | | | | |
| Trading security | \$ 12,277 | Discounted Cash Flow | Discount Rate | 2.74 % |
| Commitments to lend | 5,259 | Historical Trend | Closing Ratio | 81.53 % |
| | | Pricing Model | Origination Costs, per loan | \$ 3,692 |
| Forward commitments | 19 | Historical Trend | Closing Ratio | 81.53 % |
| | | Pricing Model | Origination Costs, per loan | \$ 3,692 |
| Capitalized servicing rights | 3,834 | Discounted Cash Flow | Constant Prepayment Rate (CPR) | 10.00 % |
| | | | Discount Rate | 10.95 % |
| Total | \$ 21,389 | | | |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Non-Recurring Fair Value Measurements

The Company is required, on a non-recurring basis, to adjust the carrying value or provide valuation allowances for certain assets using fair value measurements in accordance with GAAP. The following is a summary of applicable non-recurring fair value measurements. There are no liabilities measured at fair value on a non-recurring basis.

| (In thousands) | June 30, December | | Fair Value Measurement Date as of June 30, 2018 |
|------------------------------|-------------------|----------|---|
| | 2018 | 31, 2017 | |
| | Level 3 | Level 3 | Level 3 |
| | Inputs | Inputs | Inputs |
| Assets | | | |
| Impaired loans | \$8,075 | \$23,853 | June 2018 |
| Capitalized servicing rights | 12,129 | 12,527 | June 2018 |
| Total | \$20,204 | \$36,380 | |

Quantitative information about the significant unobservable inputs within Level 3 non-recurring assets is as follows:

| (In thousands) | Fair Value | | Valuation Techniques | Unobservable Inputs | Range (Weighted Average) (a) |
|------------------------------|---------------|--|--------------------------|--------------------------------------|------------------------------|
| | June 30, 2018 | | | | |
| Assets | | | | | |
| Impaired Loans | \$8,075 | | Fair Value of Collateral | Discounted Cash Flow - Loss Severity | 38.39% to 0.02% (2.79%) |
| | | | | Appraised Value | \$2.80 to \$1,387 (\$603.90) |
| Capitalized servicing rights | 12,129 | | Discounted Cash Flow | Constant Prepayment Rate (CPR) | 7.27% to 10.90% (9.62%) |
| | | | | Discount Rate | 10.00% to 13.12% (11.64%) |
| Total | \$20,204 | | | | |

Where dollar amounts are disclosed, the amounts represent the lowest and highest fair value of the respective (a) assets in the population except for adjustments for market/property conditions, which represents the range of adjustments to individuals properties.

| (In thousands) | Fair Value | | Valuation Techniques | Unobservable Inputs | Range (Weighted Average) (a) |
|------------------------------|-------------------|--|--------------------------|--------------------------------------|------------------------------|
| | December 31, 2017 | | | | |
| Assets | | | | | |
| Impaired Loans | \$23,853 | | Fair Value of Collateral | Discounted Cash Flow - loss severity | 38.72% to 0.21% (3.40%) |
| | | | | Appraised Value | \$10.9 to \$5,967 (\$2,197) |
| Capitalized servicing rights | 12,527 | | Discounted Cash Flow | Constant Prepayment Rate (CPR) | 7.78% to 12.78% (10.38%) |
| | | | | Discount Rate | 10.00% to 13.28% (11.72%) |
| Total | \$36,380 | | | | |

Where dollar amounts are disclosed, the amounts represent the lowest and highest fair value of the respective (a) assets in the population except for adjustments for market/property conditions, which represents the range of adjustments to individuals properties.

There were no Level 1 or Level 2 nonrecurring fair value measurements for the periods ended June 30, 2018 and December 31, 2017.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Impaired loans. Loans are generally not recorded at fair value on a recurring basis. Periodically, the Company records non-recurring adjustments to the carrying value of loans based on fair value measurements for partial charge-offs of the uncollectible portions of those loans. Non-recurring adjustments can also include certain impairment amounts for collateral-dependent loans calculated when establishing the allowance for credit losses. Such amounts are generally based on the fair value of the underlying collateral supporting the loan and, as a result, the carrying value of the loan less the calculated valuation amount does not necessarily represent the fair value of the loan. Real estate collateral is typically valued using appraisals or other indications of value based on recent comparable sales of similar properties or assumptions generally observable in the marketplace. However, the choice of observable data is subject to significant judgment, and there are often adjustments based on judgment in order to make observable data comparable and to consider the impact of time, the condition of properties, interest rates, and other market factors on current values. Additionally, commercial real estate appraisals frequently involve discounting of projected cash flows, which relies inherently on unobservable data. Therefore, nonrecurring fair value measurement adjustments that relate to real estate collateral have generally been classified as Level 3. Estimates of fair value for other collateral that supports commercial loans are generally based on assumptions not observable in the marketplace and therefore such valuations have been classified as Level 3.

Capitalized loan servicing rights. A loan servicing right asset represents the amount by which the present value of the estimated future net cash flows to be received from servicing loans exceed adequate compensation for performing the servicing. The fair value of servicing rights is estimated using a present value cash flow model. The most important assumptions used in the valuation model are the anticipated rate of the loan prepayments and discount rates. Adjustments are only recorded when the discounted cash flows derived from the valuation model are less than the carrying value of the asset. Although some assumptions in determining fair value are based on standards used by market participants, some are based on unobservable inputs and therefore are classified in Level 3 of the valuation hierarchy.

Other real estate owned (“OREO”). OREO results from the foreclosure process on residential or commercial loans issued by the Bank. Upon assuming the real estate, the Company records the property at the fair value of the asset less the estimated sales costs. Thereafter, OREO properties are recorded at the lower of cost or fair value less the estimated sales costs. OREO fair values are primarily determined based on Level 3 data including comparable sales and appraisals.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Summary of Estimated Fair Values of Financial Instruments

The following tables summarize the estimated fair values, and related carrying amounts, of the Company's financial instruments. Certain financial instruments and all non-financial instruments are excluded. Accordingly, the aggregate fair value amounts presented may not necessarily represent the underlying fair value of the Company.

| (In thousands) | June 30, 2018 | | | | |
|--|-----------------|--------------|------------|--------------|-----------|
| | Carrying Amount | Fair Value | Level 1 | Level 2 | Level 3 |
| Financial Assets | | | | | |
| Cash and cash equivalents | \$ 139,057 | \$ 139,057 | \$ 139,057 | \$— | \$ — |
| Trading security | 11,483 | 11,483 | — | — | 11,483 |
| Marketable equity securities | 59,726 | 59,726 | 59,163 | 563 | — |
| Securities available for sale | 1,393,250 | 1,393,250 | — | 1,393,250 | — |
| Securities held to maturity | 379,905 | 377,486 | — | 358,265 | 19,221 |
| FHLB bank stock and restricted securities | 75,530 | N/A | N/A | N/A | N/A |
| Net loans | 8,654,041 | 8,796,933 | — | — | 8,796,933 |
| Loans held for sale | 149,182 | 149,182 | — | 149,182 | — |
| Accrued interest receivable | 36,017 | 36,017 | — | 36,017 | — |
| Cash surrender value of bank-owned life insurance policies | 193,121 | 193,121 | — | 193,121 | — |
| Derivative assets | 33,316 | 33,316 | — | 26,031 | 7,285 |
| Assets held for sale | 1,070 | 1,070 | — | 1,070 | — |
| Financial Liabilities | | | | | |
| Total deposits | \$ 8,838,752 | \$ 8,809,947 | \$— | \$ 8,809,947 | \$ — |
| Short-term debt | 1,002,000 | 1,001,944 | — | 1,001,944 | — |
| Long-term Federal Home Loan Bank advances | 272,342 | 270,112 | — | 270,112 | — |
| Subordinated borrowings | 89,429 | 97,006 | — | 97,006 | — |
| Derivative liabilities | 27,527 | 27,527 | 658 | 26,869 | — |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

| (In thousands) | December 31, 2017 | | | | |
|---|-------------------|-------------|-----------|-------------|-----------|
| | Carrying Amount | Fair Value | Level 1 | Level 2 | Level 3 |
| Financial Assets | | | | | |
| Cash and cash equivalents | \$248,763 | \$248,763 | \$248,763 | \$— | \$ — |
| Trading security | 12,277 | 12,277 | — | — | 12,277 |
| Marketable equity securities | 45,185 | 45,185 | 44,851 | 334 | — |
| Securities available for sale and other | 1,380,914 | 1,380,914 | — | 1,380,914 | — |
| Securities held to maturity | 397,103 | 405,276 | — | 371,458 | 33,818 |
| FHLB bank stock and restricted securities | 63,085 | N/A | N/A | N/A | N/A |
| Net loans | 8,247,504 | 8,422,034 | — | — | 8,422,034 |
| Loans held for sale | 153,620 | 153,620 | — | 153,620 | — |
| Accrued interest receivable | 33,739 | 33,739 | — | 33,739 | — |
| Derivative assets | 19,308 | 19,308 | — | 14,049 | 5,259 |
| Assets held for sale | 1,392 | 1,392 | — | 1,392 | — |
| Financial Liabilities | | | | | |
| Total deposits | \$8,749,530 | \$8,731,527 | \$— | \$8,731,527 | \$ — |
| Short-term debt | 667,300 | 667,246 | — | 667,246 | — |
| Long-term Federal Home Loan Bank advances | 380,436 | 378,766 | — | 378,766 | — |
| Subordinated borrowings | 89,339 | 97,414 | — | 97,414 | — |
| Derivative liabilities | 15,838 | 15,838 | 104 | 15,715 | 19 |

Other than as discussed above, the following methods and assumptions were used by management to estimate the fair value of significant classes of financial instruments for which it is practicable to estimate that value.

Cash and cash equivalents. Carrying value is assumed to represent fair value for cash and cash equivalents that have original maturities of ninety days or less.

FHLB bank stock and restricted securities. It is not practical to determine fair value due to the restricted nature of the securities.

Cash surrender value of life insurance policies. Carrying value approximates fair value.

Loans, net. In accordance with recent accounting guidance, the fair value of loans as of June 30, 2018 was measured using the exit price valuation method, determined primarily by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities or cash flows, while incorporating liquidity and credit assumptions.

Accrued interest receivable. Carrying value approximates fair value.

Deposits. The fair value of demand, non-interest bearing checking, savings and money market deposits is determined as the amount payable on demand at the reporting date. The fair value of time deposits is estimated by discounting the estimated future cash flows using market rates offered for deposits of similar remaining maturities.

Borrowed funds. The fair value of borrowed funds is estimated by discounting the future cash flows using market rates for similar borrowings. Such funds include all categories of debt and debentures in the table above.

Subordinated borrowings. The Company utilizes a pricing service along with internal models to estimate the valuation of its junior subordinated debentures. The junior subordinated debentures re-price every ninety days.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Off-balance-sheet financial instruments. Off-balance-sheet financial instruments include standby letters of credit and other financial guarantees and commitments considered immaterial to the Company's financial statements.

NOTE 13. NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES

Presented below is net interest income after provision for loan losses for the three and six months ended June 30, 2018 and 2017, respectively.

| (In thousands) | Three Months | | Six Months Ended | |
|---|----------------|----------|------------------|-----------|
| | Ended June 30, | | June 30, | |
| | 2018 | 2017 | 2018 | 2017 |
| Net interest income | \$91,121 | \$69,545 | \$176,591 | \$136,431 |
| Provision for loan losses | 6,532 | 4,889 | 12,107 | 9,984 |
| Net interest income after provision for loan losses | \$84,589 | \$64,656 | \$164,484 | \$126,447 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 14. REVENUE

The Company adopted ASU No. 2014-09, "Revenue from Contracts with Customers," and all subsequent ASU's that modified Topic 606 on January 1, 2018. A cumulative effect adjustment to opening retained earnings was not deemed necessary as the implementation of the new standard did not have a material impact on the measurement or recognition of revenue.

Topic 606 requires the Company to follow a five step process: (1) identify the contract(s) with a customer, (2) identify the performance obligations in the contract, (3) determine the transaction price, (4) allocate the transaction price to the performance obligations in the contract, and (5) recognize revenue when (or as) the entity satisfies a performance obligation. Revenue recognition under Topic 606 depicts the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for the goods or services. The Company does not have any material significant payment terms as payment is received at or shortly after the satisfaction of the performance obligation. The value of unsatisfied performance obligations for contracts with an original expected length of one year or less are not disclosed. The Company recognizes incremental costs of obtaining contracts as an expense when incurred for contracts with a term of one year or less.

Topic 606 does not apply to revenue associated with financial instruments, including revenue from loans and securities. In addition, certain non-interest income streams such as fees associated with mortgage servicing rights, financial guarantees, derivatives, and certain credit card fees are also not in scope of the new standard. Topic 606 is applicable to non-interest revenue streams such as wealth management fees, insurance commissions and fees, administrative services for customer deposit accounts, interchange fees, and sale of owned real estate properties.

Non-interest income streams in-scope of Topic 606 are discussed below.

Service Charges on Deposit Accounts. Service charges on deposit accounts consist of monthly service fees (i.e. business analysis fees and consumer service charges) and other deposit account related fees. The Company's performance obligation for monthly service fees is generally satisfied, and the related revenue recognized, over the period in which the service is provided. Other deposit account related fees are largely transactional based, and therefore, the Company's performance obligation is satisfied, and related revenue recognized, at a point in time. Payment for service charges on deposit accounts is primarily received immediately or in the following month through a direct charge to customers' accounts. The Company may, from time to time, waive certain fees (e.g., NSF fee) for customers but generally do not reduce the transaction price to reflect variability for future reversals due to the insignificance of the amounts. Waiver of fees reduces the revenue in the period the waiver is granted to the customer.

Insurance Commissions and Fees. Commission revenue is recognized as of the effective date of the insurance policy or the date the customer is billed, whichever is later, net of return commissions related to policy cancellations. Policy cancellation is a variable consideration that is not deemed significant and thus, does not impact the amount of revenue recognized.

In addition, the Company may receive additional performance commissions based on achieving certain sales and loss experience measures. Such commissions are recognized when determinable, which is generally when such commissions are received or when the Company receives data from the insurance companies that allows the reasonable estimation of these amounts.

Wealth Management Fees. Wealth management fees is primarily comprised of fees earned from consultative investment management, trust administration, tax return preparation, and financial planning. The Company's performance obligation is generally satisfied over time and the resulting fees are recognized monthly, based on the

daily accrual of the market value of the investment accounts and the applicable fee rate.

Interchange Fees. Interchange fees are transaction fees paid to the card-issuing bank to cover handling costs, fraud and bad debt costs, and the risk involved in approving the payment. Due to the day-to-day nature of these fees they are settled on a daily basis and are accounted for as they are received.

67

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Gains/Losses on Sales of OREO. The sale of OREO and other nonfinancial assets are accounted for with the derecognition of the asset in question once a contract exists and control of the asset has been transferred to the buyer. The gain or loss on the sale is calculated as the difference between the carrying value of the asset and the transaction price.

The following presents non-interest income, segregated by revenue streams in-scope and out-of-scope of Topic 606, for the three months ended June 30, 2018 and 2017.

| (In thousands) | Three months ended | | Six months ended | |
|---|--------------------|----------|------------------|----------|
| | June 30, 2018 | 2017 | June 30, 2018 | 2017 |
| Non-interest income | | | | |
| In-scope of Topic 606: | | | | |
| Service charges on deposit accounts | \$4,923 | \$4,156 | \$10,338 | \$8,196 |
| Insurance revenue | 2,549 | 2,588 | 5,574 | 5,724 |
| Wealth management fees | 2,280 | 2,286 | 4,877 | 4,812 |
| Interchange income | 2,391 | 1,920 | 4,281 | 3,668 |
| Non-interest income (in-scope of Topic 606) | 12,143 | 10,950 | 25,070 | 22,400 |
| Non-interest income (out-of-scope of Topic 606) | 17,887 | 21,848 | 34,480 | 45,155 |
| Total non-interest income | \$30,030 | \$32,798 | \$59,550 | \$67,555 |

Table of Contents

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

SELECTED FINANCIAL DATA

The following summary data is based in part on the consolidated financial statements and accompanying notes and other information appearing elsewhere in this or prior Forms 10-Q.

| | At or for the Three Months Ended June 30, 2018 | | At or for the Six Months Ended June 30, 2017 | | |
|--|---|---------|---|---------|---|
| PER SHARE DATA (1) | | | | | |
| Net earnings per common share, diluted | \$0.74 | \$0.53 | \$1.28 | \$0.96 | |
| Adjusted earnings per common share, diluted (1) | 0.74 | 0.58 | 1.38 | 1.12 | |
| Total book value per common share | 32.49 | 31.37 | 32.49 | 31.37 | |
| Tangible book value per common share (2) | 20.28 | 20.96 | 20.28 | 20.96 | |
| Dividend per common share | 0.22 | 0.21 | 0.44 | 0.42 | |
| Common stock price: | | | | | |
| High | 44.10 | 38.65 | 44.10 | 38.65 | |
| Low | 37.05 | 33.55 | 35.80 | 32.90 | |
| Close | 40.60 | 35.15 | 40.60 | 35.15 | |
| PERFORMANCE RATIOS (3) | | | | | |
| Return on assets | 1.17 | % 0.84 | % 1.03 | % 0.76 | % |
| Adjusted return on assets (1) | 1.17 | 0.92 | 1.11 | 0.89 | |
| Return on equity | 8.88 | 6.80 | 7.79 | 6.28 | |
| Adjusted return on equity (1) | 8.89 | 7.45 | 8.41 | 7.31 | |
| Adjusted return on tangible equity (1) | 14.82 | 11.96 | 14.13 | 12.01 | |
| Net interest margin, fully taxable equivalent (FTE) (4) | 3.50 | 3.36 | 3.43 | 3.35 | |
| Fee income/Net interest and fee income | 24.25 | 32.23 | 24.87 | 31.18 | |
| Efficiency ratio (2) | 56.37 | 61.72 | 57.91 | 61.83 | |
| GROWTH RATIOS | | | | | |
| Total commercial loans, (annualized) | 9 | % 10 | % 5 | % 13 | % |
| Total loans, (annualized) | 16 | 13 | 10 | 10 | |
| Total deposits, (annualized) | 7 | 4 | 2 | 3 | |
| Total net revenues, (compared to prior year period) | 18 | 42 | 16 | 40 | |
| Earnings per share, (compared to prior year period) | 40 | 2 | 33 | (8 |) |
| Adjusted earnings per share, (compared to prior year period) (2) | 28 | 7 | 24 | 5 | |
| FINANCIAL DATA: (In millions) | | | | | |
| Total assets | \$11,902 | \$9,627 | \$11,902 | \$9,627 | |
| Total earning assets | 10,827 | 8,807 | 10,827 | 8,807 | |
| Total securities | 1,920 | 1,773 | 1,920 | 1,773 | |
| Total borrowings | 1,364 | 1,472 | 1,364 | 1,472 | |
| Total loans | 8,710 | 6,864 | 8,710 | 6,864 | |
| Allowance for loan losses | 56 | 47 | 56 | 47 | |
| Total intangible assets | 555 | 421 | 555 | 421 | |
| Total deposits | 8,839 | 6,715 | 8,839 | 6,715 | |
| Total stockholders' equity | 1,516 | 1,268 | 1,516 | 1,268 | |

Table of Contents

| | At or for the Three Months Ended June 30, 2018 | | At or for the Six Months Ended June 30, 2017 | |
|--|---|----------|---|-----------|
| ASSET QUALITY AND CONDITION RATIOS (5) | | | | |
| Net charge-offs (annualized)/average loans | 0.21 | % 0.20 | % 0.19 | % 0.20 |
| Total non-performing assets/total assets | 0.20 | 0.25 | 0.20 | 0.25 |
| Allowance for loan losses/total loans | 0.64 | 0.69 | 0.64 | 0.69 |
| Loans/deposits | 99 | 102 | 99 | 102 |
| Shareholders' equity to total assets | 12.74 | 13.17 | 12.74 | 13.17 |
| Tangible shareholders' equity to tangible assets (2) | 8.47 | 9.20 | 8.47 | 9.20 |
| FOR THE PERIOD: (In thousands) | | | | |
| Net interest income | \$91,121 | \$69,545 | \$176,591 | \$136,431 |
| Non-interest income | 30,030 | 32,798 | 59,550 | 67,555 |
| Net revenue | 121,151 | 102,343 | 236,141 | 203,986 |
| Provision for loan losses | 6,532 | 4,889 | 12,107 | 9,984 |
| Non-interest expense | 72,337 | 69,523 | 149,206 | 143,849 |
| Net income | 34,031 | 19,694 | 59,279 | 35,154 |
| Adjusted Income (1) | 34,076 | 21,559 | 63,957 | 40,959 |

(1) Adjusted measurements are non-GAAP financial measures that are adjusted to exclude net non-operating charges primarily related to acquisitions and restructuring activities. Refer to the Reconciliation of Non-GAAP Financial Measures for additional information.

(2) Non-GAAP financial measure.

(3) All performance ratios are annualized and are based on average balance sheet amounts, where applicable.

(4) Fully taxable equivalent considers the impact of tax advantaged investment securities and loans.

(5) Generally accepted accounting principles require that loans acquired in a business combination be recorded at fair value, whereas loans from business activities are recorded at cost. The fair value of loans acquired in a business combination includes expected loan losses, and there is no loan loss allowance recorded for these loans at the time of acquisition. Accordingly, the ratio of the loan loss allowance to total loans is reduced as a result of the existence of such loans, and this measure is not directly comparable to prior periods. Similarly, net loan charge-offs are normally reduced for loans acquired in a business combination since these loans are recorded net of expected loan losses.

Therefore, the ratio of net loan charge-offs to average loans is reduced as a result of the existence of such loans, and this measure is not directly comparable to prior periods. Other institutions may have loans acquired in a business combination, and therefore there may be no direct comparability of these ratios between and among other institutions.

Table of Contents

AVERAGE BALANCES AND AVERAGE YIELDS/RATES

The following table presents average balances and an analysis of average rates and yields on an annualized fully taxable equivalent basis for the periods included:

| (\$ In millions) | Three Months Ended June 30, 2018 | | | 2017 | | | Six Months Ended June 30, 2018 | | | 2017 | | |
|--|-------------------------------------|------------|---|--------------------------------|------------|---|-----------------------------------|------------|---|--------------------------------|------------|---|
| | Average Balance (FTE basis) | Yield/Rate | | Average Balance (FTE basis) | Yield/Rate | | Average Balance (FTE basis) | Yield/Rate | | Average Balance (FTE basis) | Yield/Rate | |
| Assets | | | | | | | | | | | | |
| Loans: | | | | | | | | | | | | |
| Commercial real estate | \$3,316 | 5.08 | % | \$2,692 | 4.41 | % | \$3,283 | 4.92 | % | \$2,661 | 4.50 | % |
| Commercial and industrial loans | 1,774 | 5.73 | | 1,130 | 5.30 | | 1,806 | 5.46 | | 1,102 | 5.08 | |
| Residential mortgages | 2,269 | 3.72 | | 1,871 | 3.62 | | 2,204 | 3.64 | | 1,889 | 3.59 | |
| Consumer loans | 1,113 | 4.13 | | 997 | 3.81 | | 1,114 | 4.07 | | 988 | 3.72 | |
| Total loans (1) | 8,472 | 4.73 | | 6,690 | 4.25 | | 8,407 | 4.59 | | 6,640 | 4.22 | |
| Investment securities (2) | 1,931 | 3.47 | | 1,702 | 3.45 | | 1,932 | 3.37 | | 1,664 | 3.42 | |
| Short term investments & loans held for sale (3) | 146 | 3.86 | | 148 | 3.07 | | 143 | 3.64 | | 133 | 2.74 | |
| Total interest-earning assets | 10,549 | 4.48 | | 8,540 | 4.07 | | 10,482 | 4.34 | | 8,437 | 4.04 | |
| Intangible assets | 555 | | | 422 | | | 556 | | | 422 | | |
| Other non-interest earning assets | 507 | | | 369 | | | 529 | | | 378 | | |
| Total assets | \$11,611 | | | \$9,331 | | | \$11,567 | | | \$9,237 | | |
| Liabilities and shareholders' equity | | | | | | | | | | | | |
| Deposits: | | | | | | | | | | | | |
| NOW and other | \$819 | 0.44 | % | \$572 | 0.23 | % | \$766 | 0.36 | % | \$574 | 0.23 | % |
| Money market | 2,525 | 0.88 | | 1,795 | 0.54 | | 2,522 | 0.80 | | 1,800 | 0.53 | |
| Savings | 750 | 0.14 | | 668 | 0.14 | | 747 | 0.14 | | 658 | 0.14 | |
| Time | 2,879 | 1.54 | | 2,473 | 1.13 | | 2,896 | 1.47 | | 2,412 | 1.11 | |
| Total interest-bearing deposits | 6,973 | 1.02 | | 5,508 | 0.73 | | 6,931 | 0.96 | | 5,444 | 0.71 | |
| Borrowings and notes (4) | 1,394 | 2.29 | | 1,410 | 1.46 | | 1,341 | 2.16 | | 1,398 | 1.42 | |
| Total interest-bearing liabilities | 8,367 | 1.23 | | 6,918 | 0.88 | | 8,272 | 1.15 | | 6,842 | 0.86 | |
| Non-interest-bearing demand deposits | 1,619 | | | 1,156 | | | 1,666 | | | 1,167 | | |
| Other non-interest earning liabilities | 92 | | | 99 | | | 108 | | | 108 | | |
| Total liabilities | 10,078 | | | 8,173 | | | 10,046 | | | 8,117 | | |
| Total shareholders' equity (2) | 1,533 | | | 1,158 | | | 1,521 | | | 1,120 | | |
| Total liabilities and stockholders' equity | \$11,611 | | | \$9,331 | | | \$11,567 | | | \$9,237 | | |

Table of Contents

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|-----------------------------|---------------------------|---------------------------|---------------------------|
| | 2018 | 2017 | 2018 | 2017 |
| | Average Balance | Yield/Rate (FTE basis) | Average Balance | Yield/Rate (FTE basis) |
| Net interest spread | 3.25 | % | 3.19 | % |
| Net interest margin (5) | 3.50 | | 3.36 | |
| Cost of funds | 1.03 | | 0.75 | |
| Cost of deposits | 0.83 | | 0.60 | |
| Supplementary data | | | | |
| Total deposits (In millions) | \$8,592 | | \$6,664 | |
| Fully taxable equivalent income adj. (In thousands) (6) | 2,033 | | 2,644 | |

(1) The average balances of loans include nonaccrual loans and deferred fees and costs.

(2) The average balance for securities available for sale is based on amortized cost. The average balance of equity also reflects this adjustment.

(3) Interest income on loans held for sale is included in loan interest income on the income statement.

(4) The average balances of borrowings includes the capital lease obligation presented under other liabilities on the consolidated balance sheet.

Purchased loan accretion totaled \$6.9 million and \$2.6 million for the three months ended June 30, 2018 and 2017, respectively. Purchased loan accretion totaled \$10.3 million and \$6.2 million for the six months ended June 30, 2018 and 2017, respectively.

(6) Fully taxable equivalent considers the impact of tax advantaged investment securities and loans.

Table of Contents

NON-GAAP FINANCIAL MEASURES

This document contains certain non-GAAP financial measures in addition to results presented in accordance with Generally Accepted Accounting Principles (“GAAP”). These non-GAAP measures are intended to provide the reader with additional supplemental perspectives on operating results, performance trends, and financial condition. Non-GAAP financial measures are not a substitute for GAAP measures; they should be read and used in conjunction with the Company’s GAAP financial information. A reconciliation of non-GAAP financial measures to GAAP measures is provided below. In all cases, it should be understood that non-GAAP measures do not depict amounts that accrue directly to the benefit of shareholders. An item which management excludes when computing non-GAAP adjusted earnings can be of substantial importance to the Company’s results for any particular quarter or year. The Company’s non-GAAP adjusted earnings information set forth is not necessarily comparable to non-GAAP information which may be presented by other companies. Each non-GAAP measure used by the Company in this report as supplemental financial data should be considered in conjunction with the Company’s GAAP financial information.

The Company utilizes the non-GAAP measure of adjusted earnings in evaluating operating trends, including components for operating revenue and expense. These measures exclude amounts which the Company views as unrelated to its normalized operations, including securities gains/losses, gains on the sale of business operations and assets, losses recorded for hedge terminations, merger costs, restructuring costs, legal settlements, systems conversion costs, and out-of-period adjustments. Securities gains/losses include gains/losses on equity securities beginning in the first quarter of 2018. Non-GAAP adjustments are presented net of an adjustment for income tax expense.

The Company also calculates adjusted earnings per share based on its measure of adjusted earnings and based on diluted common shares. The Company views these amounts as important to understanding its operating trends, particularly due to the impact of accounting standards related to merger and acquisition activity. Analysts also rely on these measures in estimating and evaluating the Company’s performance. Management also believes that the computation of non-GAAP adjusted earnings and adjusted earnings per share may facilitate the comparison of the Company to other companies in the financial services industry.

Charges related to merger and acquisition activity consist primarily of severance/benefit related expenses, contract termination costs, system conversion costs, variable compensation expenses, and professional fees. Systems conversion costs relate primarily to the Company’s core systems conversion and related systems conversions costs. Restructuring costs primarily consist of the Company’s continued effort to create efficiencies in operations through calculated adjustments to the branch banking and office footprint. Expense adjustments include variable rate compensation related to non-operating items.

The Company also adjusts certain equity related measures to exclude intangible assets due to the importance of these measures to the investment community.

Table of Contents

RECONCILIATION OF NON-GAAP FINANCIAL MEASURES

The following table summarizes the reconciliation of non-GAAP items recorded for the periods indicated:

| | At or for the Three Months Ended June 30, | | At or for the Six Months Ended June 30, | | |
|---|---|-----------|---|------------|-----------|
| (in thousands) | 2018 | 2017 | 2018 | 2017 | |
| GAAP Net income | \$34,031 | \$19,694 | \$59,279 | \$35,154 | |
| Adj: (Gains)/losses on securities, net (1) | (718 |)1 | 784 | (12,569) | |
| Adj: Loss on termination of hedges | — | — | — | 6,629 | |
| Adj: Net losses/(gains) on sale of business operations and assets | 21 | — | (460 |)— | |
| Adj: Merger and acquisition expense | 847 | 2,266 | 5,940 | 8,213 | |
| Adj: Restructuring and other expense | — | 637 | — | 6,372 | |
| Adj: Income taxes | (105 |)(1,039) | (1,586 |)(2,840) | |
| Total adjusted income (non-GAAP) (2) | (A) | \$34,076 | \$21,559 | \$63,957 | \$40,959 |
| GAAP Total revenue | \$121,151 | \$102,343 | \$236,141 | \$203,986 | |
| Adj: (Gains)/losses on securities, net (1) | (718 |)1 | 784 | (12,569) | |
| Adj: Net (gains) on sale of business operations and assets | 21 | — | (460 |)— | |
| Adj: Loss on termination of hedges | — | — | — | 6,629 | |
| Total operating revenue (non-GAAP) (2) | (B) | \$120,454 | \$102,344 | \$236,465 | \$198,046 |
| GAAP Total non-interest expense | \$72,337 | \$69,523 | \$149,206 | \$143,849 | |
| Less: Total non-operating expense (see above) | (847 |)(2,903) | (5,940 |)(14,585) | |
| Operating non-interest expense (non-GAAP) (2) | (C) | \$71,490 | \$66,620 | \$143,266 | \$129,264 |
| (in millions, except per share data) | | | | | |
| Total average assets | (D) | \$11,611 | \$9,331 | \$11,567 | \$9,238 |
| Total average shareholders' equity | (E) | 1,533 | 1,158 | 1,521 | 1,120 |
| Total average tangible shareholders' equity (2) | (F) | 979 | 736 | 965 | 698 |
| Total average tangible common shareholders' equity (2) | (G) | 938 | 736 | 925 | 698 |
| Total tangible shareholders' equity, period-end (2)(3) | (H) | 961 | 847 | 961 | 847 |
| Total tangible common shareholders' equity, period-end (2)(3) | (I) | 921 | 847 | 921 | 847 |
| Total tangible assets, period-end (2)(3) | (J) | 11,347 | 9,206 | 11,347 | 9,206 |
| Total common shares outstanding, period-end (thousands) | (K) | 45,420 | 40,428 | 45,420 | 40,428 |
| Average diluted shares outstanding (thousands) | (L) | 46,215 | 37,474 | 46,206 | 36,466 |
| Earnings per common share, diluted | | \$0.74 | \$0.53 | \$1.28 | \$0.96 |
| Adjusted earnings per common share, diluted (2) | (A/L) | 0.74 | 0.58 | 1.38 | 1.12 |
| Book value per common share, period-end | | 32.49 | 31.37 | 32.49 | 31.37 |
| Tangible book value per common share, period-end (2) | (I/K) | 20.28 | 20.96 | 20.28 | 20.96 |
| Total shareholders' equity/total assets | | 12.74 | 13.17 | 12.74 | 13.17 |
| Total tangible shareholder's equity/total tangible assets (2) | (H/J) | 8.47 | 9.20 | 8.47 | 9.20 |

Table of Contents

| | | | | | | |
|--|---------------|----------|----------|----------|----------|---|
| Performance ratios (4) | | | | | | |
| GAAP return on assets | | 1.17 | %0.84 | % 1.03 | %0.76 | % |
| Adjusted return on assets (2) | (A/D) | 1.17 | 0.92 | 1.11 | 0.89 | |
| GAAP return on equity | | 8.88 | 6.80 | 7.79 | 6.28 | |
| Adjusted return on equity (2) | (A/E) | 8.89 | 7.45 | 8.41 | 7.31 | |
| Adjusted return on tangible common equity (2)(5) | (A+O)/(J) | 14.82 | 11.96 | 14.13 | 12.01 | |
| Efficiency ratio (2) | (C-O)/(B+M+P) | 56.37 | 61.72 | 57.91 | 61.83 | |
| Supplementary data (in thousands) | | | | | | |
| Tax benefit on tax-credit investments (6) | (M) | \$2,119 | \$1,696 | \$2,715 | \$3,320 | |
| Non-interest income charge on tax-credit investments (7) | (N) | (1,594) | (1,453) | (2,100) | (2,782) | |
| Net income on tax-credit investments | (M+N) | 525 | 243 | 615 | 538 | |
| Intangible amortization | (O) | 1,246 | 770 | 2,514 | 1,571 | |
| Fully taxable equivalent income adjustment | (P) | 2,033 | 2,644 | 3,853 | 5,154 | |

-
- (1) Net securities losses/(gains) for the period ending June 30, 2018 includes the change in fair value of the Company's equity securities in compliance with the Company's adoption of ASU 2016-01.
- (2) Non-GAAP financial measure.
- (3) Total tangible shareholders' equity is computed by taking total shareholders' equity less the intangible assets at period-end. Total tangible assets is computed by taking total assets less the intangible assets at period-end.
- (4) Ratios are annualized and based on average balance sheet amounts, where applicable.
Adjusted return on tangible common equity is computed by dividing the total adjusted income adjusted for the
- (5) tax-affected amortization of intangible assets, assuming a 27.32% marginal rate for June 30, 2018 and a 40% marginal rate for June 30, 2017, by tangible equity.
- (6) The tax benefit is the direct reduction to the income tax provision due to tax credits and deductions generated from investments in historic rehabilitation and low-income housing.
- (7) The non-interest income charge is the reduction to the tax-advantaged commercial project investments, which are incurred as the tax credits are generated.

Table of Contents

GENERAL

Management's discussion and analysis of financial condition and results of operations is intended to assist in understanding the financial condition and results of operations of the Company. The following discussion and analysis should be read in conjunction with the Company's consolidated financial statements and the notes thereto appearing in Part I, Item 1 of this document and with the Company's consolidated financial statements and the notes thereto and Management's Discussion and Analysis of Financial Condition and Results of Operations included in the 2017 Annual Report on Form 10-K. In the following discussion, income statement comparisons are against the same period of the previous year and balance sheet comparisons are against the previous fiscal year-end, unless otherwise noted. Operating results discussed herein are not necessarily indicative of the results for the year 2018 or any future period. In management's discussion and analysis of financial condition and results of operations, certain reclassifications have been made to make prior periods comparable. Tax-equivalent adjustments in the first half of 2018 are the result of increasing income from tax-advantaged loans and securities by an amount equal to the taxes that would be paid if the income were fully taxable based on a 27% marginal rate (including state income taxes net of federal benefit), which is reduced from 2017 due to the federal tax reform enacted at the end of 2017 and effective beginning in 2018. In the discussion, references to earnings per share and "EPS" refer to diluted earnings per common share unless otherwise specified.

Berkshire Hills Bancorp, Inc. ("Berkshire" or "the Company") is a Delaware corporation headquartered in Boston and the holding company for Berkshire Bank ("the Bank") and Berkshire Insurance Group. Established in 1846, the Bank operates as a commercial bank under a Massachusetts trust company charter. Berkshire Bank operates under the brand America's Most Exciting Bank®.

Berkshire is a regional financial services company that seeks to distinguish itself over the long term based on the following attributes:

- Strong earnings momentum and improving profitability
- Boston-based regional banking company delivering franchise value in attractive markets
- Distinctive culture drives results
- Disciplined regional consolidator
- Focused on profitability goals and building shareholder value

Shown below is a profile of the Company:

Table of Contents

FORWARD-LOOKING STATEMENTS

Certain statements contained in this document that are not historical facts may constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (referred to as the Securities Act), and Section 21E of the Securities Exchange Act of 1934, as amended (referred to as the Securities Exchange Act), and are intended to be covered by the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. You can identify these statements from the use of the words “may,” “will,” “should,” “could,” “would,” “plan,” “potential,” “estimate,” “believe,” “intend,” “anticipate,” “expect,” “target” and similar expressions. These forward-looking statements are subject to significant risks, assumptions and uncertainties, including among other things, changes in general economic and business conditions, increased competitive pressures, changes in the interest rate environment, legislative and regulatory change, changes in the financial markets, and other risks and uncertainties disclosed from time to time in documents that Berkshire Hills Bancorp files with the Securities and Exchange Commission, including the Annual Report on Form 10-K for the fiscal year ended December 31, 2017 and the Risk Factors in Item 1A of this report. Because of these and other uncertainties, Berkshire’s actual results, performance or achievements, or industry results, may be materially different from the results indicated by these forward-looking statements. In addition, Berkshire’s past results of operations do not necessarily indicate Berkshire’s combined future results. You should not place undue reliance on any of the forward-looking statements, which speak only as of the dates on which they were made. Berkshire is not undertaking an obligation to update forward-looking statements, even though its situation may change in the future, except as required under federal securities law. Berkshire qualifies all of its forward-looking statements by these cautionary statements.

SUMMARY

2018 results included the operations of Worcester-based Commerce Bancshares Corp., which were acquired in October 2017, expanding Berkshire’s Greater Boston presence and market share. With the benefit of this acquisition and other initiatives, quarterly earnings per share and return on assets increased strongly to record levels in the second quarter of 2018. Highlights of the year-over-year improvement in second quarter performance metrics included:

- 73% increase in net income to \$34 million
- 40% increase in earnings per share to \$0.74
- 48% increase in net revenue to \$121 million
- 39% improvement in return on assets to 1.17%
- 31% improvement in return on equity to 8.9%

These results were achieved while the Company was absorbing the increased compliance costs related to crossing the \$10 billion asset threshold, and while the Company was investing in its Boston headquarters relocation and team buildout. Results also benefited from a lower tax rate following federal tax reform. In recognition of improved earnings, Berkshire increased its quarterly shareholder dividend by 5% to \$0.22 per common share in the first quarter of 2018, matching a similar increase in the first quarter of 2017.

Berkshire’s Xtraordinary Day of Service in June tackled 74 community projects across our markets, totaling nearly 7,000 volunteer hours and 92% of the workforce. Berkshire’s Foundation announced the appointment of a Corporate Social Responsibility (CSR) Officer to expand Berkshire’s multiple community engagement activities and implement an all-encompassing CSR strategy. The Company’s strengthened financial condition was recognized with an A- bank deposit rating assigned by the KBRA Bond Rating Agency. Berkshire’s stock was added to the S&P 600 SmallCap[®] index during the most recent quarter; this index tracks U.S. small cap companies and is included in the S&P Composite 1500[®] index, facilitating an expanded market for the Company’s stock.

Economic conditions remain good in the Company’s markets, and the Company maintains a focus on Greater Boston, Albany, and the Mid-Atlantic as its strongest regional markets. The yield curve increased and flattened in 2018 as a result of three 25 basis point increases by the Federal Reserve Bank in its target fed funds rate in December 2017,

March 2018, and June 2018.

77

Table of Contents

COMPARISON OF FINANCIAL CONDITION AT JUNE 30, 2018 AND DECEMBER 31, 2017

Summary: Total assets increased by \$0.3 billion, or 3%, in the first half of 2018 due to a \$0.4 billion, or 5%, increase in total loans. The asset growth was funded by \$0.1 billion, or 1%, net growth in deposits and a \$0.2 billion, or 20%, increase in borrowings. Asset quality metrics remained strong, and the strong loan growth resulted in modest changes in liquidity and capital metrics. Interest rate sensitivity remained generally positive to higher rates. Book value per share increased by 1% to \$32.49 and the non-GAAP measure of tangible book value per common share increased by 2% to \$20.28.

Securities: Total securities remained unchanged at \$1.9 billion in the half, and there were no significant changes in the composition of the portfolio. The portfolio yield decreased modestly to 3.47% in the most recent quarter from the fourth quarter of 2017, including the reduction in the benefit of tax advantaged securities as a result of tax reform. This reduction primarily reduced the yield on municipal securities, which continue to meet the Company's investment objectives. The weighted average life of the bond portfolio increased to 6.2 years from 5.6 years at the start of the year, including the effect of slower prepayment speeds resulting from higher interest rates. The unrealized loss on the securities portfolio measured 1.6% of cost at quarter-end, compared to a 0.6% gain at the start of the year, reflecting lower bond prices stemming from the increase in interest rates since the beginning of the year. Due to a change in accounting principles, beginning in 2018, the change in net fair value of marketable equity securities is recorded to non-interest income rather than to accumulated other comprehensive income. The Company has elected to disclose these securities separately on the statement of financial condition.

Loans: The \$411 million, or 5%, increase in total loans included a \$294 million increase in residential mortgages and a \$126 million increase in commercial loans. Mortgage loan growth was primarily comprised of jumbo fixed rate loans in Eastern Massachusetts originated by Berkshire and its local correspondent banks. The Company sells most of its conforming mortgage originations, while local jumbo loans are retained for investment to support relationship and market objectives. Growth in the first half of 2018 included seasonally higher purchase mortgage originations. Growth in commercial loans included the benefit of the Company's expansion in Greater Boston. Commercial loans comprised 60% of total loans at midyear and continue to be a central strategic focus. The Company expanded its commercial teams in Greater Boston and New Jersey based on growth opportunities in those markets. Berkshire's total non-owner occupied commercial real estate exposure measured 242% of regulatory capital at period-end, compared to the 300% regulatory monitoring guidelines (based on regulatory definitions). Construction loan exposure was 37% of bank regulatory capital, compared to the 100% regulatory monitoring guideline.

The second quarter loan portfolio yield increased to 4.73% due to the benefit of higher interest rates and increased purchased loan accretion. The benefit of this accretion was 0.25% in the most recent quarter, compared to 0.21% in the fourth quarter of 2017. At midyear, 42% of total loans contractually repriced within one year, 22% repriced in one to five years, and 36% repriced after five years. While scheduled repricing was unchanged from year-end, the expected average loan lives are estimated to have shortened slightly due to the volume of variable rate commercial loans originated which is believed to have more than offset the growth in fixed rate mortgages and the impact of slower projected prepayment speeds tied to rising rates.

Asset Quality: Asset quality metrics generally remained favorable in the first half of 2018. Annualized net loan charge-offs for this period were 0.19% of average loans and non-performing assets were little changed at 0.20% of total assets at period-end. Accruing delinquent loans increased to 0.62% of loans from 0.55% during the first half of the year, due primarily to one commercial real estate loan which was 90+ days delinquent and well-secured and in the process of collection at midyear. At period-end, the total contractual balance of purchased credit impaired loans was \$172 million, with a \$71 million carrying value. Asset resolution strategies in the first half of the year contributed to the reduction in these balances from \$209 million and \$97 million at the start of the year. The midyear contractual balance included Boston area taxi medallion loans acquired at a significant discount with Commerce, and which had a net carrying value less than \$30 million at midyear. Criticized loans measured 1.8% of total assets at period-end,

compared to 1.6% at the start of the year, as reductions of criticized acquired loans partially offset increases related to commercial real estate loans from business activities. The ratio of the allowance to total loans increased to 0.64% from 0.62% during the first half of the year. At period-end, this ratio measured

78

Table of Contents

0.74% for business activities loans and 0.29% for acquired loans, compared to 0.75% and 0.27% respectively at the prior year-end.

Deposits and Borrowings: The \$89 million, or 1%, increase in total deposits in the first half of 2018 included a \$123 million increase in NOW accounts due to higher municipal balances and a new deposit sweep program established with Berkshire's wealth management customers. The decrease in demand deposits and money market accounts included a \$78 million decrease related to commercial payroll service accounts, as well as runoff into higher yielding instruments. Payroll service deposits totaled \$434 million at midyear; these balances fluctuate daily depending on the timing of payroll cycles. Time deposit growth was concentrated in brokered deposits which offset the payroll fluctuations and provided funding for loan growth. Total deposits averaged \$8.6 billion in the most recent quarter, which was a 3% increase over the fourth quarter of 2017. Total borrowings increased by \$227 million during the first half of the year as FHLB borrowings were used primarily to support loan growth. Borrowing costs also increased due to higher rates and a widening of LIBOR spreads. Due primarily to higher market interest rates, the average cost of deposits was 0.83% in the most recent quarter, compared to 0.66% in the fourth quarter of 2017.

Derivative Financial Instruments: The notional balance of derivative financial instruments increased to \$3.0 billion at period-end from \$2.5 billion at the start of the year. This included a \$0.3 billion increase related to commercial loan interest rate swaps and matching hedges originated in the first half of the year. Growth in derivatives also included a \$0.2 billion seasonal increase in residential mortgage interest rate lock commitments. The gains on these mortgage derivatives resulted in a \$2 million increase in the net fair value of total derivatives to \$6 million at period-end.

Shareholders' Equity: Shareholders' equity increased by \$20 million, or 1%, in the first half of 2018. The benefit of retained earnings was partially offset by a reduction in accumulated other comprehensive income resulting from the unrealized bond losses discussed previously in the Securities section. As a result, there was a slight increase in leverage, with the ratio of equity to assets measuring 12.7% at period-end, while the non-GAAP measure of tangible equity to tangible assets was 8.5%. Based on earnings growth, the return on equity improved to 8.9% in the most recent quarter, while the non-GAAP measure of adjusted return on tangible common equity improved to 14.8%. The Company focuses on this measure in assessing internal capital generation to support dividends and organic growth.

Table of Contents

COMPARISON OF OPERATING RESULTS FOR THE THREE MONTHS AND SIX MONTHS ENDED JUNE 30, 2018 AND JUNE 30, 2017

Summary: Revenue and expense in 2018 included the Commerce operations acquired on October 13, 2017. As a result, most categories of revenue and expense increased over the same period of 2017. Most categories of interest income and expense also increased due to the increase in market interest rates. Additionally, 2018 operations included the benefit of First Choice cost saves and hedge terminations and restructuring actions which affected 2017 results. Based on its pro forma analysis in the Company's Form 10-K, the Company expected the Commerce acquisition to be accretive to earnings and earnings per share, including the cost saves targeted to be achieved in 2018. Operations in 2018 also benefited from the lower federal income tax rate, which reduced the effective tax rate compared to 2017. Earnings per share reflected the shares issued as merger consideration for the Commerce acquisition.

Second quarter net income increased year-over-year by \$14 million, or 73%, while six month net income increased by \$24 million, or 69%. Earnings per share increased by 40% to \$0.74 for the second quarter and by 33% to \$1.28 for the first six months of the year, including the new merger related shares. The Company utilizes the non-GAAP measure of adjusted earnings per share to evaluate earnings related to ongoing operations. This measure excludes merger related costs and other specified net charges. Adjusted earnings per share increased year-over-year by \$0.16, or 28%, to \$0.74 in the second quarter and by \$0.26, or 23%, to \$1.38 in the first six months of the year. Operating results included the benefit of a lower effective tax rate and higher purchased loan accretion in 2018. The return on assets improved to 1.17% in the most recent quarter. The return on equity improved to 8.9% and the non-GAAP measure of adjusted return on tangible common equity improved to 14.8%. The Company evaluates this measure as an indicator of internal capital generation to support dividends and growth. The improvement in profitability in 2018 demonstrated positive operating leverage driven by revenue growth and was further evidenced by an improvement in the efficiency ratio to 56.4% in the most recent quarter.

Revenue: Quarterly net revenue advanced year-over-year by 18% and 16% for the second quarter and first half, respectively. Much of this increase was attributed to the Commerce acquisition, based on the pro forma analysis of combined operations in the most recent Form 10-K. Revenue in the most recent period totaled \$121 million, or \$485 million on an annualized basis. Annualized revenue totaled \$10.49 per share in the most recent quarter, compared to \$10.92 in the same quarter of 2017.

Net Interest Income: Net interest income increased year-over-year by 31% and 29% in the second quarter and first half, respectively. Average earning assets increased by 24% for both of these periods, including the benefit of the Commerce acquisition and growth in loans from business activities. The net interest margin increased year-over-year in both the first and second quarter, reaching 3.50% in the second quarter of 2018 compared to 3.36% in 2017. The contribution from purchased loan accretion in the second quarter was 0.25% in 2018 compared to 0.12% in 2017. Partially offsetting this benefit, the second quarter contribution of taxable equivalent loan and securities yields decreased by 4 basis points due primarily to a lower tax rate resulting from federal income tax reform. The net interest margin increased by 5 basis points before these impacts, reflecting the benefit of the Company's positive interest rate sensitivity and the Commerce acquisition, including a higher average balance of transaction accounts, which have a lower comparative interest cost.

Non-Interest Income: Loan and deposit fee income increased year-over-year 24% for the first half of the year. Loan fee growth included higher SBA loan sale gains and higher commercial loan interest rate swap fee income. Deposit fees increased primarily due to the addition of the Commerce operations; this benefit was partially offset by higher earnings credit rates on commercial demand deposits as compensation for deposit services. Mortgage industry revenue contracted year-over-year due to lower demand as a result of higher interest rates. The Company's first half mortgage banking revenue declined year-over-year by 30% and was mostly offset by a reduction in estimated related expenses. Non-interest income is net of charges related to the amortization of tax credit investments which benefit tax expense. Non-interest income includes items not viewed as related to ongoing operations, including securities gains/losses and

hedge termination losses. Berkshire crossed the \$10 billion asset threshold at the time of the Commerce acquisition. Due to the Durbin Amendment of the Dodd-Frank act, the Company must reduce its card processing fees included in deposit fees, effective July 1, 2018. The Company

80

Table of Contents

estimates that this annualized revenue loss will be approximately \$5 million; this impact was included in the Company's analysis of the net accretive benefits targeted for the Commerce acquisition.

Loan Loss Provision: The first half loan loss provision increased by 21% due primarily to the increase in the size of the portfolio. The provision exceeded net loan charge-offs and boosted the ratio of the allowance to total loans. The provision for loan losses is a charge to earnings in an amount sufficient to maintain the allowance for loan losses at a level deemed adequate by the Company. It is an estimate of the probable and estimable loan losses in the portfolio as of period-end. The level of the allowance is a critical accounting estimate and the level of the allowance was included in the discussion of financial condition.

Non-Interest Expense: Total non-interest expense increased year-over-year by 4% for the second quarter and first half of 2018. Non-interest expense include charges viewed as not related to future operations, consisting primarily of merger and restructuring charges. The non-GAAP measure of adjusted operating expense excludes these items. This measure increased by 7% and 11% for the above periods respectively, including costs related to the acquired Commerce operations. Management views the year-over-year results as indicating positive operating leverage, as the revenue increase exceeded expense growth. This was achieved while the Company added overhead costs for increased regulatory compliance related to crossing the \$10 billion asset threshold. The Company also increased its investment in employees and its communities as part of the reinvestment of benefits resulting from federal tax reform. Additionally, the Company has added to its banking teams in Greater Boston and in the Mid Atlantic. As previously noted, mortgage banking expenses were reduced as a result of the related revenue decline. Expenses have benefited from the implementation of cost saves for the First Choice Bank and Commerce acquisitions. The Company is assessing plans to consolidate approximately six branch offices during the next several quarters, with a target to reduce ongoing expenses after an initial restructuring charge. Two branches were added in attractive markets in the first half of the year. Due to an amendment to the Dodd-Frank legislation, the Company is no longer required to submit formal capital stress tests and will not have that incremental expense which was planned, although informal stress testing will continue. As a consequence of crossing the \$10 billion asset threshold, management anticipates that FDIC insurance expense will increase by approximately \$1.3 million per year beginning in the fourth quarter of 2018. Total full-time equivalent staff measured 2,004 positions at midyear, compared to 1,992 positions at the start of the year.

Income Tax Expense: The Company's statutory tax rate decreased year-over-year reflecting the benefit of federal income tax reform which became effective in 2018. The federal statutory tax rate decreased to 21% from 35%, while the state effective tax rate net of federal benefit increased to 5% from 2%. The overall effective tax rate decreased to 21% from 30% in the first half of the year, falling to 20% in the most recent quarter due to additional benefit from tax credit investment projects, which provided \$0.01 per share in benefit, net of related amortization charges in non-interest income.

Total Comprehensive Income: Total comprehensive income includes net income together with other comprehensive income. Other comprehensive income was a loss of \$6 million and \$20 million for the second quarter and first half of 2018, compared to income of \$2 million and \$1 million in the same periods of the prior year. This change primarily reflected the unrealized bond losses in 2018 due to lower bond market prices as a result of increases in market interest rates.

Liquidity and Cash Flows: Liquidity declined modestly in the first half of 2018, primarily due to the strong loan growth. The ratio of loans/deposits increased to 99% from 95%. To support additional wholesale funding, the Company increased the assets qualifying to support FHLBB borrowings. At midyear, the Bank had \$1.2 billion in unused FHLBB borrowing availability, compared to \$1.1 billion at the start of the year. At period-end, the holding company had cash and equivalents totaling \$69 million. In the first quarter of 2018, the holding company downstreamed \$50 million in cash into the Bank as paid in capital to support further bank growth. Additional

information about liquidity and cash flows is contained in the related section of the most recent Form 10-K.

Capital Resources: Please see the “Shareholders’ Equity” section of the Comparison of Financial Condition for a discussion of shareholders’ equity together with the note on Shareholders’ Equity in the consolidated financial

Table of Contents

statements. Additional information about regulatory capital is contained in the notes to the consolidated financial statements and in the most recent Form 10-K. There was a slight increase in leverage in the first half of 2018 due to the strong loan growth. The increase in earnings and profitability have increased the Company's internal generation of tangible equity which the Company views as supportive of dividends, organic growth, and long term strengthening of capital metrics. The Company conducts informal capital stress tests but, based on recent amendments to the Dodd-Frank act, it will not be required to submit formal analyses to supervisory authorities. As noted above, the holding company contributed additional cash equity to the Bank in the first quarter. Additionally, subsequent to midyear, the Company converted a \$35 million subordinated note from the Bank into bank equity, to further strengthen Bank capital to support future growth.

Off-Balance Sheet Arrangements and Contractual Obligations: In the normal course of operations, Berkshire engages in a variety of financial transactions that, in accordance with generally accepted accounting principles are not recorded in the Company's financial statements. These transactions involve, to varying degrees, elements of credit, interest rate, and liquidity risk. Such transactions are used primarily to manage customers' requests for funding and take the form of loan commitments and lines of credit. Further information about the Company's off-balance sheet arrangements and information relating to payments due under contractual obligations is presented in the most recent Form 10-K. Changes in the fair value of derivative financial instruments and hedging activities are included on the balance sheet and information related to these matters is reported in the related footnote to the consolidated financial statements, and was included in management's discussion of changes in financial condition. There were no major changes in off-balance sheet arrangements and contractual obligations during the first half of 2018.

Fair Value Measurements: The most significant fair value measurements recorded by the Company are those related to assets and liabilities acquired in business combinations. The premium or discount value of acquired loans has historically been the most significant element of these measurements. Berkshire provides a summary of estimated fair values of financial instruments at each period-end. The premium or discount value of loans has historically been the most significant element of this period-end presentation. This premium or discount is a Level 3 estimate and reflects management's subjective judgments. At period-end, the premium value of the loan portfolio was \$143 million, or 1.7% of the carrying value, compared to \$175 million, or 2.1% of carrying value at year-end 2017. The Company makes further measurements of fair value of certain assets and liabilities, as described in the related note in the financial statements. The most significant measurements of recurring fair values of financial instruments primarily relate to securities available for sale, loans held for sale, and derivative instruments. These measurements were generally based on Level 2 market based inputs.

Table of Contents

APPLICATION OF CRITICAL ACCOUNTING POLICIES

The Company's significant accounting policies are described in Note 1 to the consolidated financial statements included in its most recent Annual Report on Form 10-K. Modifications to significant accounting policies made during the year are described in Note 1 to the consolidated financial statements included in Item 1 of this report. The preparation of the consolidated financial statements in accordance with GAAP and practices generally applicable to the financial services industry requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, and expenses, and to disclose contingent assets and liabilities. Actual results could differ from those estimates.

Management has identified the Company's most critical accounting policies as related to:

- Allowance for Loan Losses
- Acquired Loans
- Income Taxes
- Goodwill and Identifiable Intangible Assets
- Determination of Other-Than-Temporary Impairment of Securities
- Fair Value of Financial Instruments

These particular significant accounting policies are considered most critical in that they are important to the Company's financial condition and results, and they require management's subjective and complex judgment as a result of the need to make estimates about the effects of matters that are inherently uncertain. The accounting policies and estimates, including the nature of the estimates and types of assumptions used, are described in Part II, Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, included in the Company's most recent Form 10-K and pertain to discussion in Item 2, Management's Discussion and Analysis of Financial Condition and Results of Operations, of this report.

Table of Contents

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There were no material changes to the way that the Company measures market risk in the first half of 2018. For further discussion about the Company's Quantitative and Qualitative Aspects of Market Risk, please review Item 7A of the most recent report on Form 10-K which sets forth the methodologies employed by the Company and the various aspects of its analysis of its interest rate sensitivity. Berkshire's objective is to maintain a neutral or asset sensitive interest rate risk profile, as measured by the sensitivity of net interest income to market interest rate changes.

The Company estimates that its interest rate profile remains slightly asset sensitive at midyear 2018. Asset sensitivity decreased in the first half of the year due to growth of loans supported by shorter term funding. At period-end, modeled net interest income was nearly flat in the second year of an up 200 basis point ramp. The loss representing the economic value of equity at risk increased modestly to 7% at midyear from 5% at the start of the year in a 200 basis point upward move in interest rates. Of note, while deposit costs have risen, deposit interest rate sensitivity remains below the 40% beta level utilized in the Company's modeling. The Company's modeling assumes no shift in the deposit mix in rate change scenarios. Estimated net interest income and net income at risk under the forward curve scenario also remained positive. This positive sensitivity is compared to a baseline of flat interest rates; this baseline scenario demonstrates medium term pressure on the net interest margin from the roll-down of long term assets resulting from scheduled repricing.

The Company believes the modeled positive sensitivity of its interest income has been partially offset by the flattening of the yield curve, changes in deposit mix, the mix of business growth, and competitive market conditions. Deposit activity in the banking industry is beginning to react to the trend of increasing short term rates following the prolonged time when rates were very low. Uncertainties also exist regarding the impact of lower federal income taxes on industry pricing competition. The Company believes that its diversified markets and sources may provide it with comparative benefit in managing its deposit pricing and balance sheet management to achieve its market, earnings, and risk objectives.

Table of Contents

ITEM 4. CONTROLS AND PROCEDURES

a) Disclosure controls and procedures.

The principal executive officers, including the principal financial officer, based on their evaluation of disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of the end of the period covered by this Quarterly Report on Form 10-Q, have concluded that the Company's disclosure controls and procedures were effective.

b) Changes in internal control over financial reporting.

There were no changes in the Company's internal control over financial reporting that occurred during the last fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Table of Contents

PART II

ITEM 1. LEGAL PROCEEDINGS

As of June 30, 2018, neither the Company nor the Bank was involved in any pending legal proceedings believed by management to be material to the Company's financial condition or results of operations. Periodically, there have been various claims and lawsuits involving the Bank, such as claims to enforce liens, condemnation proceedings on properties in which the Bank holds security interests, claims involving the making and servicing of real property loans, and other issues incident to the Bank's business. However, other than the items noted below, neither the Company nor the Bank is a defendant 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. Additionally, an estimate of future, probable losses cannot be estimated as of June 30, 2018.

On April 28, 2016, Berkshire Hills and Berkshire Bank were served with a complaint filed in the United States District Court, District of Massachusetts, Springfield Division. The complaint was filed by an individual Berkshire Bank depositor, who claims to have filed the complaint on behalf of a purported class of Berkshire Bank depositors, and alleges violations of the Electronic Funds Transfer Act and certain regulations thereunder, among other matters. On July 15, 2016, the complaint was amended to add purported claims under the Massachusetts Consumer Protection Act. The complaint seeks, in part, compensatory, consequential, statutory, and punitive damages. Berkshire Hills and Berkshire Bank deny the allegations contained in the complaint and are vigorously defending this lawsuit.

On January 29, 2018, the Bank was served with an amended complaint filed nominally against Berkshire Hills in the Business Litigation Session of the Massachusetts Superior Court sitting in Suffolk County. The amended complaint was filed by two residuary beneficiaries of an estate planning trust that was administered by the Bank as successor trustee following the death of the trust donor, and alleges the Bank breached its fiduciary duty and violated the Massachusetts Consumer Protection Act in the course of performing its duties as trustee. The complaint seeks compensatory, statutory, and punitive damages. Berkshire Hills and Berkshire Bank deny the allegations contained in the complaint and are vigorously defending this lawsuit.

Table of Contents

ITEM 1A. RISK FACTORS

In addition to the other information set forth in this report, you should carefully consider the factors discussed below and in Part I, “Item 1A. Risk Factors” in our most recent Annual Report on Form 10-K, which could materially affect the Company's business, financial condition, or future operating results. The risks described in this form are not the only risks presently facing the Company. Additional risks and uncertainties not currently known to the Company, or currently deemed to be immaterial, also may materially adversely affect the Company's business, financial condition, and/or operating results.

There were no major changes in risk factors in the first half of 2018.

Table of Contents

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

(a) Recent Sales of Unregistered Securities

The Company occasionally engages in the practice of transferring unregistered securities for the purpose of completing business transactions. These shares are issued to vendors or other organizations as consideration for services performed in accordance with each contract. During the six months ended June 30, 2018 and June 30, 2017, the Company transferred 1,437 and 8,038 shares, respectively.

(b) Not applicable.

(c) The following table provides certain information with regard to shares repurchased by the Company in the second quarter of 2018:

| 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 |
|------------------|----------------------------------|------------------------------|--|--|
| April 1-30, 2018 | — | \$ — | — | 500,000 |
| May 1-31, 2018 | — | — | — | 500,000 |
| June 1-30, 2018 | — | — | — | 500,000 |
| Total | — | \$ — | — | 500,000 |

On December 2, 2015, the Company announced that its Board of Directors authorized a new stock repurchase program, pursuant to which the Company may repurchase up to 500 thousand shares of the Company's common stock, representing approximately 1.6% of the Company's then outstanding shares. The timing of the purchases will depend on certain factors, including but not limited to, market conditions and prices, available funds, and alternative uses of capital. The stock repurchase program may be carried out through open-market purchases, block trades, negotiated private transactions or pursuant to a trading plan adopted in accordance with Rule 10b5-1 under the Securities Exchange Act of 1934. Any repurchased shares will be recorded as treasury shares. The repurchase plan will continue until it is completed or terminated by the Board of Directors. As of June 30, 2018, no shares had been purchased under this program, and the available shares represented approximately 1.1% of outstanding shares at that date.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

None.

Table of Contents

ITEM 6. EXHIBITS

- 3.1 Amended and Restated Certificate of Incorporation of Berkshire Hills Bancorp, Inc.
- 3.2 Amended and Restated Bylaws of Berkshire Hills Bancorp, Inc. (1)
- 4.1 Form of Common Stock Certificate of Berkshire Hills Bancorp, Inc. (2)
- 31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1 Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2 Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 101 Shareholder Interactive data files pursuant to Rule 405 of Regulation S-T: (i) the Consolidated Statements of Condition, (ii) the Consolidated Statements of Income, (iii) the Consolidated Statements of Comprehensive Income, (iv) the Consolidated Statements of Changes in Shareholders' Equity, (v) the Consolidated Statements of Cash Flows, and (vi) the Notes to Consolidated Financial Statements tagged as blocks of text and in detail.

(1) Incorporated herein by reference from the Exhibits to the Form 8-K as filed on June 26, 2017.

(2) Incorporated herein by reference from the Exhibits to the Form S-1, Registration Statement and amendments thereto, initially filed on March 10, 2000, Registration No. 333-32146.

Table of Contents

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

BERKSHIRE HILLS
BANCORP, INC.

Dated: August 9, 2018 By: /s/ Michael P. Daly
Michael P. Daly
Chief Executive Officer

Dated: August 9, 2018 By: /s/ James M. Moses
James M. Moses
Senior Executive Vice
President, Chief
Financial Officer