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

# Form 10-K

(Mark One)

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

**For the fiscal year ended December 31, 2011**

**OR**

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

**For the transition period from to**

**Commission file number 000-26481**

# FINANCIAL INSTITUTIONS, INC.
**(Exact name of registrant as specified in its charter)**

| **NEW YORK** | **16-0816610** |
|---|---|
| **(State or other jurisdiction of incorporation or organization)** | **(I.R.S. Employer Identification No.)** |
| **220 LIBERTY STREET, WARSAW, NEW YORK** | **14569** |
| **(Address of principal executive offices)** | **(ZIP Code)** |

**Registrant's telephone number, including area code: (585) 786-1100**

**Securities registered under Section 12(b) of the Exchange Act:**

| **Title of each class** | **Name of exchange on which registered** |
|---|---|
| Common stock, par value $.01 per share | NASDAQ Global Select Market |

**Securities registered under Section 12(g) of the Exchange Act:**
**NONE**

Indicate by check mark if the regsitrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ¨ No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ¨ No x

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this form 10-K or any amendment to this Form 10-K. ¨

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

| | |
|---|---|
| Large accelerated filer ¨ | Accelerated filer x |
| Non-accelerated filer ¨ | Smaller reporting company ¨ |

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

The aggregate market value of common equity held by non-affiliates of the registrant, as computed by reference to the June 30, 2011 closing price reported by NASDAQ, was approximately $210,055,000.

As of March 1, 2012, there were issued and outstanding, exclusive of treasury shares, 13,811,791 shares of the registrant's common stock.

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the registrant's proxy statement for the 2012 Annual Meeting of Shareholders are incorporated by reference in Part III of this Annual Report on Form 10-K.

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## PART I

### FORWARD LOOKING INFORMATION

Statements in this Annual Report on Form 10-K that are based on other than historical data are forward-looking within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements provide current expectations or forecasts of future events and include, among others:

- statements with respect to the beliefs, plans, objectives, goals, guidelines, expectations, anticipations, and future financial condition, results of operations and performance of Financial Institutions, Inc. ("the parent" or "FII") and its subsidiaries (collectively "the Company," "we," "our," "us"); and
- statements preceded by, followed by or that include the words "may," "could," "should," "would," "believe," "anticipate," "estimate," "expect," "intend," "plan," "projects," or similar expressions.

These forward-looking statements are not guarantees of future performance, nor should they be relied upon as representing management's views as of any subsequent date. Forward-looking statements involve significant risks and uncertainties and actual results may differ materially from those presented, either expressed or implied, in this Annual Report on Form 10-K, including, but not limited to, those presented in the Management's Discussion and Analysis of Financial Condition and Results of Operations. Factors that might cause such differences include, but are not limited to:

- If we experience greater credit losses than anticipated, earnings may be adversely impacted;
- Geographic concentration may unfavorably impact our operations;
- We depend on the accuracy and completeness of information about or from customers and counterparties;
- We are subject to environmental liability risk associated with our lending activities;
- We are highly regulated and may be adversely affected by changes in banking laws, regulations and regulatory practices;
- Ongoing financial reform legislation may result in new regulations that could require us to maintain higher capital levels and/or increase our costs of operations or limit certain activities or lines of business;
- New or changing tax, accounting, and regulatory rules and interpretations could significantly impact our strategic initiatives, results of operations, cash flows, and financial condition;
- Changes in New York State banking regulations or other laws could adversely affect us;
- If our security systems, or those of merchants, merchant acquirers or other third parties containing information about customers, are compromised, we may be subject to liability and damage to our reputation;
- We could be subject to losses if we fail to properly safeguard sensitive and confidential information;
- Our information systems may experience an interruption or breach in security;
- We rely on other companies to provide key components of our business infrastructure;
- We may not be able to attract and retain skilled people;
- The potential for business interruption exists throughout our organization;
- Our expansion efforts, particularly through new and acquired branches, may not be successful if we fail to manage our growth effectively;
- We may fail to realize any benefits and may incur unanticipated losses related to the assets we acquire and liabilities we assume from current or future acquisitions;
- We are subject to interest rate risk;
- Our business may be adversely affected by conditions in the financial markets and economic conditions generally;
- Our earnings are significantly affected by the fiscal and monetary policies of the federal government and its agencies;
- The soundness of other financial institutions could adversely affect us;
- Our market value could result in an impairment of goodwill;
- We operate in a highly competitive industry and market area;Liquidity is essential to our businesses;
- We may need to raise additional capital in the future and such capital may not be available on acceptable terms or at all;
- We rely on dividends from our subsidiaries for most of our revenue;
- The market price for our common stock varies, and you should purchase common stock for long-term investment only;

- We may issue debt and equity securities or securities convertible into equity securities, any of which may be senior to our common stock as to distributions and in liquidation, which could negatively affect the value of our common stock;
- We may not pay dividends on our common stock; and
- Our certificate of incorporation, our bylaws, and certain banking laws contain anti-takeover provisions.

We caution readers not to place undue reliance on any forward-looking statements, which speak only as of the date made, and advise readers that various factors, including those described above, could affect our financial performance and could cause our actual results or circumstances for future periods to differ materially from those anticipated or projected. See also Item 1A, Risk Factors, in this Form 10-K for further information. Except as required by law, we do not undertake, and specifically disclaim any obligation to publicly release any revisions to any forward-looking statements to reflect the occurrence of anticipated or unanticipated events or circumstances after the date of such statements.

## ITEM 1. BUSINESS

### GENERAL

Financial Institutions, Inc. is a financial holding company organized in 1931 under the laws of New York State ("New York" or "NYS"). Through its subsidiaries, including its wholly-owned, New York chartered banking subsidiary, Five Star Bank, Financial Institutions, Inc. provides a broad array of deposit, lending and other financial services to retail, commercial, and municipal customers in Western and Central New York. All references in this Annual Report on Form 10-K to the parent company are to Financial Institutions, Inc. ("FII"). Unless otherwise indicated, or unless the context requires otherwise, all references in this Annual Report on Form 10-K to "the Company," "we," "our" or "us" means Financial Institutions, Inc. and its subsidiaries on a consolidated basis. Five Star Bank is referred to as Five Star Bank, "FSB" or "the Bank". FII is a legal entity separate and distinct from its subsidiaries, assisting those subsidiaries by providing financial resources and oversight. Our executive offices are located at 220 Liberty Street, Warsaw, New York.

We conduct business primarily through our banking subsidiary, Five Star Bank, which adopted its current name in 2005 when we merged three of our bank subsidiaries, Wyoming County Bank, National Bank of Geneva and Bath National Bank into our New York chartered bank subsidiary, First Tier Bank & Trust, which was renamed Five Star Bank. In addition, our business operations include a wholly-owned broker-dealer and investment adviser subsidiary, Five Star Investment Services, Inc. ("FSIS").

#### Our Business Strategy

Our business strategy has been to maintain a community bank philosophy, which consists of focusing on and understanding the individualized banking needs of the businesses, professionals and other residents of the local communities surrounding our banking centers. We believe this focus allows us to be more responsive to our customers' needs and provide a high level of personal service that differentiates us from larger competitors, resulting in long-standing and broad based banking relationships. Our core customers are primarily comprised of small- to medium-sized businesses, professionals and community organizations who prefer to build a banking relationship with a community bank that offers and combines high quality, competitively-priced banking products and services with personalized service. Because of our identity and origin as a locally operated bank, we believe that our level of personal service provides a competitive advantage over larger banks, which tend to consolidate decision-making authority outside local communities.

A key aspect of our current business strategy is to foster a community-oriented culture where our customers and employees establish long-standing and mutually beneficial relationships. We believe that we are well-positioned to be a strong competitor within our market area because of our focus on community banking needs and customer service, our comprehensive suite of deposit and loan products typically found at larger banks, our highly experienced management team and our strategically located banking centers. A central part of our strategy is generating core deposits to support growth of a diversified and high-quality loan portfolio.

### MARKET AREAS AND COMPETITION

We provide a wide range of consumer and commercial banking and financial services to individuals, municipalities and businesses through a network of over 50 offices and more than 70 ATMs in fourteen contiguous counties of Western and Central New York: Allegany, Cattaraugus, Cayuga, Chautauqua, Chemung, Erie, Genesee, Livingston, Monroe, Ontario, Seneca, Steuben, Wyoming and Yates Counties. Our banking activities, though concentrated in the communities where we maintain branches, also extend into neighboring counties. In addition, we have expanded our consumer indirect lending presence to the Capital District of New York and Northern Pennsylvania.

Our market area is economically diversified in that we serve both rural markets and the larger more affluent markets of suburban Rochester and suburban Buffalo. Rochester and Buffalo are the two largest metropolitan areas in New York outside of New York City, with a combined metropolitan area of over two million people. We anticipate increasing our presence in and around these metropolitan statistical areas in the coming years.

We face significant competition in both making loans and attracting deposits, as both Western and Central New York have a high density of financial institutions. Our competition for loans comes principally from commercial banks, savings banks, savings and loan associations, mortgage banking companies, credit unions, insurance companies and other financial service companies. Our most direct competition for deposits has historically come from commercial banks, savings banks and credit unions. We face additional competition for deposits from non-depository competitors such as the mutual fund industry, securities and brokerage firms and insurance companies. We generally compete with other financial service providers on factors such as: level of customer service, responsiveness to customer needs, availability and pricing of products, and geographic location.

**INVESTMENT ACTIVITIES**

Our investment policy is contained within our overall Asset-Liability Management and Investment Policy. This policy dictates that investment decisions will be made based on the safety of the investment, liquidity requirements, potential returns, cash flow targets, need for collateral and desired risk parameters. In pursuing these objectives, we consider the ability of an investment to provide earnings consistent with factors of quality, maturity, marketability, pledgeable nature and risk diversification. Our Treasurer, guided by our Asset-Liability Committee ("ALCO"), is responsible for investment portfolio decisions within the established policies.

Our investment securities strategy centers on providing liquidity to meet loan demand and redeeming liabilities, meeting pledging requirements, managing credit risks, managing overall interest rate risks and maximizing portfolio yield. Our current policy generally limits security purchases to the following:

- U.S. treasury securities;
- U.S. government agency securities, which are securities issued by official Federal government bodies (e.g. the Government National Mortgage Association ("GNMA")) and U.S. government-sponsored enterprise ("GSE") securities, which are securities issued by independent organizations that are in part sponsored by the federal government (e.g., the Federal Home Loan Bank ("FHLB") system, the Federal National Mortgage Association ("FNMA"), the Federal Home Loan Mortgage Corporation ("FHLMC"), the Small Business Administration ("SBA") and the Federal Farm Credit Bureau);
- Mortgage-backed securities ("MBS") include mortgage-backed pass-through securities ("pass-throughs") and collateralized mortgage obligations ("CMO") issued by GNMA, FNMA and FHLMC;
- Investment grade municipal securities, including revenue, tax and bond anticipation notes, statutory installment notes and general obligation bonds;
- Certain creditworthy un-rated securities issued by municipalities;
- Certificates of deposit;
- Equity securities at the holding company level; and
- Limited partnership investments in Small Business Investment Companies.

## LENDING ACTIVITIES

### General

We offer a broad range of loans including commercial business and revolving lines of credit, commercial mortgages, equipment loans, residential mortgage loans and home equity loans and lines of credit, home improvement loans, automobile loans and personal loans. Newly originated and refinanced fixed rate residential mortgage loans are either retained in our portfolio or sold to the secondary market with servicing rights retained.

We continually evaluate and update our lending policy. The key elements of our lending philosophy include the following:

- To ensure consistent underwriting, employees must share a common view of the risks inherent in lending activities as well as the standards to be applied in underwriting and managing credit risk;
- Pricing of credit products should be risk-based;
- The loan portfolio must be diversified to limit the potential impact of negative events; and
- Careful, timely exposure monitoring through dynamic use of our risk rating system is required to provide early warning and assure proactive management of potential problems.

### Commercial Business and Commercial Mortgage Lending

We originate commercial business loans in our primary market areas and underwrite them based on the borrower's ability to service the loan from operating income. We offer a broad range of commercial lending products, including term loans and lines of credit. Short and medium-term commercial loans, primarily collateralized, are made available to businesses for working capital (including inventory and receivables), business expansion (including acquisition of real estate, expansion and improvements) and the purchase of equipment. Commercial business loans are offered to the agricultural industry for short-term crop production, farm equipment and livestock financing. As a general practice, where possible, a collateral lien is placed on any available real estate, equipment or other assets owned by the borrower and a personal guarantee of the owner is obtained. As of December 31, 2011, $75.0 million, or 32%, of the aggregate commercial business loan portfolio were at fixed rates, while $158.8 million, or 68%, were at variable rates.

We also offer commercial mortgage loans to finance the purchase of real property, which generally consists of real estate with completed structures and, to a smaller extent, agricultural real estate financing. Commercial mortgage loans are secured by first liens on the real estate and are typically amortized over a 10 to 20 year period. The underwriting analysis includes credit verification, appraisals and a review of the borrower's financial condition and repayment capacity. As of December 31, 2011, $122.1 million, or 31%, of the aggregate commercial mortgage portfolio were at fixed rates, while $271.1 million, or 69%, were at variable rates.

We utilize government loan guarantee programs where available and appropriate.

### Government Guarantee Programs

We participate in government loan guarantee programs offered by the SBA, U.S. Department of Agriculture, Rural Economic and Community Development and Farm Service Agency, among others. As of December 31, 2011, we had loans with an aggregate principal balance of $60.1 million that were covered by guarantees under these programs. The guarantees typically only cover a certain percentage of these loans. By participating in these programs, we are able to broaden our base of borrowers while minimizing credit risk.

### Residential Mortgage Lending

We originate fixed and variable rate one-to-four family residential mortgages collateralized by owner-occupied properties located in our market areas. We offer a variety of real estate loan products, which are generally amortized over periods of up to 30 years. Loans collateralized by one-to-four family residential real estate generally have been originated in amounts of no more than 80% of appraised value or have mortgage insurance. Mortgage title insurance and hazard insurance are normally required. We sell certain one-to-four family residential mortgages to the secondary mortgage market and typically retain the right to service the mortgages. To assure maximum salability of the residential loan products for possible resale, we have formally adopted the underwriting, appraisal, and servicing guidelines of the FHLMC as part of our standard loan policy. As of December 31, 2011, the residential mortgage servicing portfolio totaled $297.8 million, the majority of which has been sold to FHLMC. As of December 31, 2011, our residential mortgage loan portfolio totaled $113.9 million, or 8% of our total loan portfolio. We do not engage in sub-prime or other high-risk residential mortgage lending as a line-of-business.

**Consumer Lending**

We offer a variety of loan products to our consumer customers, including home equity loans and lines of credit, automobile loans, secured installment loans and various other types of secured and unsecured personal loans. At December 31, 2011, outstanding consumer loan balances were concentrated in indirect automobile loans and home equity products.

We selectively originate a mix of new and used indirect consumer loans through franchised new car dealers. The consumer indirect loan portfolio is primarily comprised of loans with terms that typically range from 36 to 84 months. We have expanded our relationships with franchised new car dealers in Western, Central and the Capital District of New York, and most recently, Northern Pennsylvania. As of December 31, 2011, the consumer indirect portfolio totaled $487.7 million, or 33% of our total loan portfolio.

We also originate, independently of the indirect loans described above, consumer automobile loans, recreational vehicle loans, boat loans, home improvement loans, closed-end home equity loans, home equity lines of credit, personal loans (collateralized and uncollateralized) and deposit account collateralized loans. The terms of these loans typically range from 12 to 180 months and vary based upon the nature of the collateral and the size of loan. The majority of the consumer lending program is underwritten on a secured basis using the customer's home or the financed automobile, mobile home, boat or recreational vehicle as collateral. As of December 31, 2011, $117.6 million, or 51%, of the home equity portfolio was at fixed rates, while $114.2 million, or 49%, was at variable rates. Approximately 69% of the loans in the home equity portfolio are first lien positions at December 31, 2011. The other consumer portfolio totaled $24.3 million as of December 31, 2011, all of which were fixed rate loans.

**Credit Administration**

Our loan policy establishes standardized underwriting guidelines, as well as the loan approval process and the committee structures necessary to facilitate and ensure the highest possible loan quality decision-making in a timely and businesslike manner. The policy establishes requirements for extending credit based on the size, risk rating and type of credit involved. The policy also sets limits on individual loan officer lending authority and various forms of joint lending authority, while designating which loans are required to be approved at the committee level.

Our credit objectives are as follows:

- Compete effectively and service the legitimate credit needs of our target market;
- Enhance our reputation for superior quality and timely delivery of products and services;
- Provide pricing that reflects the entire relationship and is commensurate with the risk profiles of our borrowers;
- Retain, develop and acquire profitable, multi-product, value added relationships with high quality borrowers;
- Focus on government guaranteed lending and establish a specialization in this area to meet the needs of the small businesses in our communities; and
- Comply with the relevant laws and regulations.

Our policy includes loan reviews, under the supervision of the Audit and Risk Oversight committees of the Board of Directors and directed by our Chief Risk Officer, in order to render an independent and objective evaluation of our asset quality and credit administration process.

Risk ratings are assigned to loans in the commercial business and commercial mortgage portfolios. The risk ratings are specifically used as follows:

- Profile the risk and exposure in the loan portfolio and identify developing trends and relative levels of risk;
- Identify deteriorating credits;
- Reflect the probability that a given customer may default on its obligations; and
- Assist with risk-based pricing.

Through the loan approval process, loan administration and loan review program, management seeks to continuously monitor our credit risk profile and assesses the overall quality of the loan portfolio and adequacy of the allowance for loan losses.

We have several procedures in place to assist in maintaining the overall quality of our loan portfolio. Delinquent loan reports are monitored by credit administration to identify adverse levels and trends. Loans, including impaired loans, are generally classified as non-accruing if they are past due as to maturity or payment of principal or interest for a period of more than 90 days, unless such loans are well-collateralized and in the process of collection. Loans that are on a current payment status or past due less than 90 days may also be classified as non-accruing if repayment in full of principal and/or interest is uncertain.

**Allowance for Loan Losses**

The allowance for loan losses is established through charges to earnings in the form of a provision for loan losses. The allowance reflects management's estimate of the amount of probable loan losses in the portfolio, based on factors such as:

- Specific allocations for individually analyzed credits;
- Risk assessment process;
- Historical net charge-off experience;
- Evaluation of the loan portfolio with loan reviews;
- Levels and trends in delinquent and non-accruing loans;
- Trends in volume and terms;
- Effects of changes in lending policy;
- Experience, ability and depth of management;
- National and local economic trends and conditions;
- Concentrations of credit;
- Interest rate environment;
- Customer leverage;
- Information (availability of timely financial information); and
- Collateral values.

Our methodology in the estimation of the allowance for loan losses includes the following broad areas:

1. Impaired commercial business and commercial mortgage loans, generally in excess of $50 thousand are reviewed individually and assigned a specific loss allowance, if considered necessary, in accordance with U.S. generally accepted accounting principles ("GAAP").

2. The remaining portfolios of commercial business and commercial mortgage loans are segmented by risk rating into the following loan classification categories: uncriticized or pass, special mention, substandard and doubtful. Uncriticized loans, special mention loans, substandard loans and all doubtful loans not assigned a specific loss allowance are assigned allowance allocations based on historical net loan charge-off experience for each of the respective loan categories, supplemented with additional reserve amounts, if considered necessary, based upon qualitative factors. These qualitative factors include the levels and trends in delinquencies and non-accruing loans, trends in volume and terms of loans, effects of changes in lending policy, experience, ability, and depth of management, national and local economic conditions, concentrations of credit, interest rate environment, customer leverage, information (availability of timely financial information), and collateral values, among others.

3. The retail loan portfolio is segmented into the following types of loans: residential real estate, home equity (home equity loans and lines of credit), consumer indirect and other consumer. Allowance allocations for the real estate related loan portfolios (residential and home equity) are based on the average loss experience for the previous eight quarters, supplemented with qualitative factors similar to the elements described above. Allowance allocations for the consumer indirect and other consumer portfolios are based on vintage analyses performed with historical loss experience at 36 months and 24 months aging, respectively. The allocations on these portfolios are also supplemented with qualitative factors.

Management presents a quarterly review of the adequacy of the allowance for loan losses to our Board of Directors based on the methodology described above. See also the section titled "Allowance for Loan Losses" in Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations".

## SOURCES OF FUNDS

Our primary sources of funds are deposits, borrowed funds, scheduled amortization and prepayments of principal from loans and mortgage-backed securities, maturities and calls of investment securities and funds provided by operations.

### Deposits

We maintain a full range of deposit products and accounts to meet the needs of the residents and businesses in our primary service area. Products include an array of checking and savings account programs for individuals and small businesses, including money market accounts, certificates of deposit, sweep investment capabilities as well as Individual Retirement Accounts and other qualified plan accounts. We rely primarily on competitive pricing of our deposit products, customer service and long-standing relationships with customers to attract and retain these deposits and seek to make our services convenient to the community by offering 24-hour ATM access at some of our facilities, access to other ATM networks available at other local financial institutions and retail establishments, and telephone banking services including account inquiry and balance transfers. We also take advantage of the use of technology by allowing our customers banking access via the Internet and various advanced systems for cash management for our business customers.

We had no traditional brokered deposits at December 31, 2011; however, we do participate in the Certificate of Deposit Account Registry Service ("CDARS") program, which enables depositors to receive FDIC insurance coverage for deposits otherwise exceeding the maximum insurable amount. Through the CDARS program, deposits in excess of the maximum insurable amount are placed with multiple participating financial institutions. Reciprocal CDARS deposits totaled $46.5 million at December 31, 2011.

### Borrowings

We have access to a variety of borrowing sources and use both short-term and long-term borrowings to support our asset base. Borrowings from time-to-time include federal funds purchased, securities sold under agreements to repurchase and FHLB advances. We also offer customers a deposit account that sweeps balances in excess of an agreed upon target amount into overnight repurchase agreements.

## OPERATING SEGMENTS

Our primary operating segment is our subsidiary bank, FSB. Our brokerage subsidiary, FSIS, is also deemed an operating segment; however, it does not meet the applicable thresholds for separate disclosure requirements.

## OTHER INFORMATION

All of the reports we file with the SEC, including this Annual Report on Form 10-K, Quarterly Reports on Form 10-Q and Current Reports on Form 8-K, as well as any amendments thereto may be read at the public reference facility maintained by the SEC at its public reference room at 100 F. Street, N.E., Room 1580, Washington, DC 20549 and copies of all or any part thereof may be obtained from that office upon payment of the prescribed fees. You may call the SEC at 1-800-SEC-0330 for further information on the operation of the public reference room and you can request copies of the documents upon payment of a duplicating fee, by writing to the SEC. In addition, the SEC maintains a website that contains reports, proxy and information statements and other information regarding registrants, including us, that file electronically with the SEC which can be accessed at www.sec.gov.

We also make available, free of charge, through our website, all reports filed with the SEC, including our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q and Current Reports on Form 8-K, as well as any amendments to those reports, as soon as reasonably practicable after those documents are filed with, or furnished to, the SEC. These filings may be viewed by accessing the *Company Filings* subsection of the *SEC Filings* section under the *Investor Relations* tab on our website ( www.fiiwarsaw.com ). Information available on our website is not a part of, and is not incorporated into, this Annual Report on Form 10-K.

## SUPERVISION AND REGULATION

The Company and our subsidiaries are subject to an extensive system of laws and regulations that are intended primarily for the protection of customers and depositors and not for the protection of our security holders. These laws and regulations govern such areas as capital, permissible activities, allowance for loan losses, loans and investments, and rates of interest that can be charged on loans. Described below are elements of selected laws and regulations. The descriptions are not intended to be complete and are qualified in their entirety by reference to the full text of the statutes and regulations described.

**Holding Company Regulation** . As a bank holding company and financial holding company, we are subject to comprehensive regulation by the Board of Governors of the Federal Reserve System, frequently referred to as the Federal Reserve Board ("FRB"), under the Bank Holding Company Act, as amended by, among other laws, the Gramm-Leach-Bliley Act of 1999 (the "Gramm-Leach-Bliley Act"), and by the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"), enacted on July 21, 2010. We must file reports with the FRB and such additional information as the FRB may require, and our holding company and non-banking affiliates are subject to examination by the FRB. Under FRB policy, a bank holding company must serve as a source of strength for its subsidiary banks. Under this policy, the FRB may require, and has required in the past, a holding company to contribute additional capital to an undercapitalized subsidiary bank. The Bank Holding Company Act provides that a bank holding company must obtain FRB approval before:

- Acquiring, directly or indirectly, ownership or control of any voting shares of another bank or bank holding company if, after such acquisition, it would own or control more than 5% of such shares (unless it already owns or controls the majority of such shares);
- Acquiring all or substantially all of the assets of another bank or bank holding company, or
- Merging or consolidating with another bank holding company.

The Bank Holding Company Act generally prohibits a bank holding company from acquiring direct or indirect ownership or control of more than 5% of the voting shares of any company which is not a bank or bank holding company, or from engaging directly or indirectly in activities other than those of banking, managing or controlling banks, or providing services for its subsidiaries. The principal exceptions to these prohibitions involve certain non-bank activities which, by statute or by FRB regulation or order, have been identified as activities closely related to the business of banking or managing or controlling banks. The list of activities permitted by the FRB includes, among other things: lending; operating a savings institution, mortgage company, finance company, credit card company or factoring company; performing certain data processing operations; providing certain investment and financial advice; underwriting and acting as an insurance agent for certain types of credit related insurance; leasing property on a full-payout, non-operating basis; selling money orders, travelers' checks and United States Savings Bonds; real estate and personal property appraising; providing tax planning and preparation services; and, subject to certain limitations, providing securities brokerage services for customers. These activities may also be affected by federal legislation.

The Gramm-Leach-Bliley Act amended portions of the Bank Holding Company Act to authorize bank holding companies, such as us, directly or through non-bank subsidiaries to engage in securities, insurance and other activities that are financial in nature or incidental to a financial activity. In order to undertake these activities, a bank holding company must become a "financial holding company" by submitting to the appropriate Federal Reserve Bank a declaration that the company elects to be a financial holding company and a certification that all of the depository institutions controlled by the company are well capitalized and well managed.

**Depository Institution Regulation.** Our bank subsidiary is subject to regulation by the Federal Deposit Insurance Corporation ("FDIC"). This regulatory structure includes:

- Real estate lending standards, which provide guidelines concerning loan-to-value ratios for various types of real estate loans;
- Risk-based capital rules, including accounting for interest rate risk, concentration of credit risk and the risks posed by non-traditional activities;
- Rules requiring depository institutions to develop and implement internal procedures to evaluate and control credit and settlement exposure to their correspondent banks;
- Rules restricting types and amounts of equity investments; and
- Rules addressing various safety and soundness issues, including operations and managerial standards, standards for asset quality, earnings and compensation standards.

**Capital Adequacy Requirements.** The FRB and FDIC have issued substantially similar risk-based and leverage capital guidelines applicable to bank holding companies and banks. In addition, these regulatory agencies may from time to time require that a bank holding company or bank maintain capital above the minimum levels, based on its financial condition or actual or anticipated growth.

The FRB's risk-based guidelines establish a two-tier capital framework. Tier 1 capital generally consists of common shareholders' equity, retained earnings, a limited amount of qualifying perpetual preferred stock, qualifying trust preferred securities and non-controlling interests in the equity accounts of consolidated subsidiaries, less goodwill and certain intangibles. Tier 2 capital generally consists of certain hybrid capital instruments and perpetual debt, mandatory convertible debt securities and a limited amount of subordinated debt, qualifying preferred stock, loan loss allowance, and unrealized holding gains on certain equity securities. The sum of Tier 1 and Tier 2 capital represents qualifying total capital, at least 50% of which must consist of Tier 1 capital.

Risk-based capital ratios are calculated by dividing Tier 1 and total capital by risk-weighted assets. Assets and off-balance sheet exposures are assigned to one of four categories of risk-weights, based primarily on relative credit risk. For bank holding companies, generally the minimum Tier 1 risk-based capital ratio is 4% and the minimum total risk-based capital ratio is 8%. Our Tier 1 and total risk-based capital ratios under these guidelines at December 31, 2011 were 12.20% and 13.45%, respectively.

The FRB's leverage capital guidelines establish a minimum leverage ratio determined by dividing Tier 1 capital by adjusted average total assets. The minimum leverage ratio is 3% for bank holding companies that meet certain specified criteria, including having the highest regulatory rating. All other bank holding companies generally are required to maintain a leverage ratio of at least 4%. At December 31, 2011, we had a leverage ratio of 8.63%. See also the section titled "Capital Resources" in Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" and Note 10, Regulatory Matters, of the notes to consolidated financial statements.

The federal regulatory authorities' risk-based capital guidelines are based upon the 1988 capital accord ("Basel I") of the Basel Committee on Banking Supervision (the "Basel Committee"). The Basel Committee is a committee of central banks and bank supervisors/regulators from the major industrialized countries that develops broad policy guidelines for use by each country's supervisors in determining the supervisory policies and regulations to which they apply. Actions of the Committee have no direct effect on banks in participating countries. In 2004, the Basel Committee published a new capital accord ("Basel II") to replace Basel I. Basel II provides two approaches for setting capital standards for credit risk – an internal ratings-based approach tailored to individual institutions' circumstances and a standardized approach that bases risk weightings on external credit assessments to a much greater extent than permitted in existing risk-based capital guidelines. Basel II also would set capital requirements for operational risk and refine the existing capital requirements for market risk exposures.

A final rule implementing the advanced approaches of Basel II in the United States would apply only to certain large or internationally active banking organizations, or "core banks" – defined as those with consolidated total assets of $250 billion or more or consolidated on-balance sheet foreign exposures of $10 billion or more, became effective as of April 1, 2008. Certain other U.S. banking organizations would have the option to adopt the requirements of this rule. We are not required to comply with the advanced approaches of Basel II.

On September 3, 2009, the United States Department of Treasury (the "Treasury") issued a policy statement (the "Treasury Policy Statement") entitled "Principles for Reforming the U.S. and International Regulatory Capital Framework for Banking Firms," which contemplates changes to the existing regulatory capital regime involving substantial revisions to major parts of the Basel I and Basel II capital frameworks and affecting all regulated banking organizations and other systemically important institutions. The Treasury Policy Statement calls for, among other things, higher and stronger capital requirements for all banking firms, with changes to the regulatory capital framework to be phased in over a period of several years.

On December 17, 2009, the Basel Committee issued a set of proposals (the "2009 Capital Proposals") that would significantly revise the definitions of Tier 1 capital and Tier 2 capital. Among other things, the 2009 Capital Proposals would re-emphasize that common equity is the predominant component of Tier 1 capital. Concurrently with the release of the 2009 Capital Proposals, the Basel Committee also released a set of proposals related to liquidity risk exposure (the "2009 Liquidity Proposals"). The 2009 Liquidity Proposals include the implementation of (i) a "liquidity coverage ratio" or LCR, designed to ensure that a bank maintains an adequate level of unencumbered, high-quality assets sufficient to meet the bank's liquidity needs over a 30-day time horizon under an acute liquidity stress scenario and (ii) a "net stable funding ratio" or NSFR, designed to promote more medium and long-term funding of the assets and activities of banks over a one-year time horizon.

The Dodd-Frank Act includes certain provisions concerning the capital regulations of the U.S. banking regulators, which are often referred to as the "Collins Amendment." These provisions are intended to subject bank holding companies to the same capital requirements as their bank subsidiaries and to eliminate or significantly reduce the use of hybrid capital instruments, especially trust preferred securities, as regulatory capital. Under the Collins Amendment, trust preferred securities issued by a company with total consolidated assets of less than $15 billion before May 19, 2010 and treated as regulatory capital are grandfathered, but any such securities issued later are not eligible as regulatory capital. The banking regulators developed regulations setting minimum risk-based and leverage capital requirements for holding companies and banks on a consolidated basis that are no less stringent than the generally applicable requirements in effect for depository institutions under the prompt corrective action regulations discussed below. The FRB adopted final regulations effective July 28, 2011, which established a capital floor and amended advanced risk-based capital adequacy standards. The rule mandated that the capital requirements for insured depository institutions be the minimum for covered institutions, a provision of the Dodd-Frank Act. The rule also implemented elements of the Collins Amendment.

The banking regulators also must seek to make capital standards countercyclical so that the required levels of capital increase in times of economic expansion and decrease in times of economic contraction. The FRB has not yet issued proposed rules for these countercyclical capital standards.

In December 2010 and January 2011, the Basel Committee published the final texts of reforms on capital and liquidity generally referred to as "Basel III." Although Basel III is intended to be implemented by participating countries for large, internationally active banks, its provisions are likely to be considered by U.S. banking regulators in developing new regulations applicable to other banks in the United States, including Five Star Bank.

For banks in the United States, among the most significant provisions of Basel III concerning capital are the following:

- A minimum ratio of common equity to risk-weighted assets reaching 4.5%, plus an additional 2.5% as a capital conservation buffer, by 2019 after a phase-in period.
- A minimum ratio of Tier 1 capital to risk-weighted assets reaching 6.0% by 2019 after a phase-in period.
- A minimum ratio of total capital to risk-weighted assets, plus the additional 2.5% capital conservation buffer, reaching 10.5% by 2019 after a phase -in period.
- An additional countercyclical capital buffer to be imposed by applicable national banking regulators periodically at their discretion, with advance notice.
- Restrictions on capital distributions and discretionary bonuses applicable when capital ratios fall within the buffer zone.
- Deduction from common equity of deferred tax assets that depend on future profitability to be realized.
- Increased capital requirements for counterparty credit risk relating to OTC derivatives, repos and securities financing activities.
- For capital instruments issued on or after January 13, 2013 (other than common equity), a loss-absorbency requirement such that the instrument must be written off or converted to common equity if a trigger event occurs, either pursuant to applicable law or at the direction of the banking regulator. A trigger event is an event under which the banking entity would become nonviable without the write-off or conversion, or without an injection of capital from the public sector. The issuer must maintain authorization to issue the requisite shares of common equity if conversion were required.

The Basel III provisions on liquidity include complex criteria establishing the LCR and NSFR. The purpose of the LCR is to ensure that a bank maintains adequate unencumbered, high quality liquid assets to meet its liquidity needs for 30 days under a severe liquidity stress scenario. The purpose of the NSFR is to promote more medium and long-term funding of assets and activities, using a one-year horizon. Although Basel III is described as a "final text," it is subject to the resolution of certain issues and to further guidance and modification, as well as to adoption by U.S. banking regulators, including decisions as to whether and to what extent it will apply to U.S. banks that are not large, internationally active banks.

**Prompt Corrective Action.** The Federal Deposit Insurance Corporation Improvement Act of 1991, among other things, identifies five capital categories for insured depository institutions (well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized) and requires the respective federal bank regulatory agencies to implement systems for "prompt corrective action" for insured depository institutions that do not meet minimum capital requirements within these categories. This act imposes progressively more restrictive constraints on operations, management and capital distributions, depending on the category in which an institution is classified. Failure to meet the capital guidelines could also subject a banking institution to capital raising requirements. An "undercapitalized" bank must develop a capital restoration plan and its parent holding company must guarantee that bank's compliance with the plan. The liability of the parent holding company under any such guarantee is limited to the lesser of five percent of the bank's assets at the time it became "undercapitalized" or the amount needed to comply with the plan. Furthermore, in the event of the bankruptcy of the parent holding company, such guarantee would take priority over the parent's general unsecured creditors. In addition, the Federal Deposit Insurance Corporation Improvement Act requires the various regulatory agencies to prescribe certain non-capital standards for safety and soundness relating generally to operations and management, asset quality and executive compensation and permits regulatory action against a financial institution that does not meet these standards.

The various federal bank regulatory agencies have adopted substantially similar regulations that define the five capital categories identified by the Federal Deposit Insurance Corporation Improvement Act, using the total risk-based capital, Tier 1 risk-based capital and leverage capital ratios as the relevant capital measures. These regulations establish various degrees of corrective action to be taken when an institution is considered undercapitalized. Under the regulations, a "well capitalized" institution must have a Tier 1 risk-based capital ratio of at least 6%, a total risk-based capital ratio of at least 10% and a leverage ratio of at least 5% and not be subject to a capital directive or order. An institution is "adequately capitalized" if it has a Tier 1 risk-based capital ratio of at least 4%, a total risk-based capital ratio of at least 8% and a leverage ratio of at least 4% (3% in certain circumstances). An institution is "undercapitalized" if it has a Tier 1 risk-based capital ratio of less than 4%, a total risk-based capital ratio of less than 8% or a leverage ratio of less than 4% (3% in certain circumstances). An institution is "significantly undercapitalized" if it has a Tier 1 risk-based capital ratio of less than 3%, a total risk-based capital ratio of less than 6% or a leverage ratio of less than 3%. An institution is "critically undercapitalized" if its tangible equity is equal to or less than 2% of total assets. Generally, an institution may be reclassified in a lower capitalization category if it is determined that the institution is in an unsafe or unsound condition or engaged in an unsafe or unsound practice.

As of December 31, 2011, our subsidiary bank met the requirements to be classified as "well-capitalized".

**Dividends.** The FRB policy is that a bank holding company should pay cash dividends only to the extent that its net income for the past year is sufficient to cover both the cash dividends and a rate of earnings retention that is consistent with the holding company's capital needs, asset quality and overall financial condition, and that it is inappropriate for a bank holding company experiencing serious financial problems to borrow funds to pay dividends. Furthermore, a bank that is classified under the prompt corrective action regulations as "undercapitalized" will be prohibited from paying any dividends.

In December 2008, under the Treasury's Troubled Asset Relief Program ("TARP") Capital Purchase Program, we entered into a Securities Purchase Agreement—Standard Terms with the Treasury pursuant to which, among other things, we sold to the Treasury for an aggregate purchase price of $37.5 million, 7,503 shares of fixed rate cumulative perpetual preferred stock, Series A ("Series A" preferred stock) and a warrant to purchase up to 378,175 shares of our common stock, par value $0.01 per share, at an exercise price of $14.88 per share (the "Warrant").

Pursuant to the terms of the Purchase Agreement, our ability to declare or pay dividends on any of our shares was limited. Specifically, we were prohibited from paying any dividend with respect to shares of common stock, other junior securities or preferred stock ranking *pari passu* with the Series A preferred stock or repurchasing or redeeming any shares of the our common stock, other junior securities or preferred stock ranking *pari passu* with the Series A preferred stock in any quarter unless all accrued and unpaid dividends were paid on the Series A preferred stock for all past dividend periods (including the latest completed dividend period), subject to certain limited exceptions.

We fully redeemed the Series A preferred stock during the first quarter of 2011 and repurchased the Warrant in the following quarter. The complete redemption of the Series A preferred stock removed the TARP restrictions pertaining to our ability to declare and pay dividends and repurchase our common stock, as well as certain restrictions associated with executive compensation.

Our primary source for cash dividends is the dividends we receive from our subsidiary bank. Our bank is subject to various regulatory policies and requirements relating to the payment of dividends, including requirements to maintain capital above regulatory minimums. Approval of the New York State Department of Financial Services is required prior to paying a dividend if the dividend declared by the Bank exceeds the sum of the Bank's net profits for that year and its retained net profits for the preceding two calendar years.

**Federal Deposit Insurance Assessments.** The Bank's deposits are insured to the maximum extent permitted by the Deposit Insurance Fund ("DIF"). Upon enactment of the Emergency Economic Stabilization Act of 2008 on October 3, 2008, federal deposit insurance coverage levels under the DIF temporarily increased from $100,000 to $250,000 per deposit category, per depositor, per institution, through December 31, 2009. On May 20, 2009, the Helping Families Save Their Homes Act extended the temporary increase through December 31, 2013. The Dodd-Frank Act permanently increases the maximum amount of deposit insurance to $250,000 per deposit category, per depositor, per institution retroactive to January 1, 2008, and noninterest-bearing transaction accounts have unlimited deposit insurance through December 31, 2013.

As the insurer, the FDIC is authorized to conduct examinations of, and to require reporting by, FDIC-insured institutions. The FDIC also may prohibit any FDIC-insured institution from engaging in any activity the FDIC determines by regulation or order to pose a serious threat to the DIF. The FDIC also has the authority to initiate enforcement actions against banks. Insurance of deposits may be terminated by the FDIC upon a finding that the institution has engaged or is engaging in unsafe and unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC or written agreement entered into with the FDIC. The management of the Bank does not know of any practice, condition or violation that might lead to termination of deposit insurance.

The FDIC maintains the DIF by assessing depository institutions an insurance premium on a quarterly basis under a risk-based assessment system. The amount of the assessment is a function of the institution's risk category, of which there are four, and assessment base. An institution's risk category is determined according to its supervisory ratings and capital levels and is used to determine the institution's assessment rate. The assessment rate for risk categories are calculated according to a formula, which relies on supervisory ratings and either certain financial ratios or long-term debt ratings. An insured bank's assessment base is currently determined by its level of deposits. Because the system is risk-based, it allows banks to pay lower assessments to the FDIC as their capital level and supervisory ratings improve. By the same token, if these indicators deteriorate, the institution will have to pay higher assessments to the FDIC.

Under the Federal Deposit Insurance Act, the FDIC Board has the authority to set the annual assessment rate range for the various risk categories within certain regulatory limits and to impose special assessments upon insured depository institutions when deemed necessary by the FDIC's Board. As part of the Deposit Insurance Fund Restoration Plan adopted by the FDIC in October 2008, on February 27, 2009, the FDIC adopted the final rule modifying the risk-based assessment system, which set initial base assessment rates between 12 and 45 basis points, beginning April 1, 2009. The FDIC imposed an emergency special assessment on June 30, 2009, which totaled $923 thousand for our Bank. In addition, in September 2009, the FDIC extended the Restoration Plan period to eight years. In November 2009, the FDIC adopted a final rule requiring prepayment of 13 quarters of FDIC premiums. The Bank's required prepayment amounted to $9.9 million and was collected in December 2009.

In October 2010, the FDIC adopted a new Restoration Plan for the DIF to ensure that the fund reserve ratio reaches 1.35% by September 30, 2020, as required by the Dodd-Frank Act. Under the Restoration Plan, the FDIC did not institute the uniform three-basis point increase in assessment rates scheduled to take place on January 1, 2011 and maintained the current schedule of assessment rates for all depository institutions. At least semi-annually, the FDIC will update its loss and income projections for the DIF and, if needed, will increase or decrease assessment rates, following notice-and-comment rulemaking, if required.

In November 2010, the FDIC issued a notice of proposed rulemaking to change the deposit insurance assessment base from total domestic deposits to average total assets minus average tangible equity, as required by the Dodd-Frank Act, effective April 1, 2011. The FDIC also issued a notice of proposed rulemaking to revise the deposit insurance assessment system for large institutions. The FDIC proposed to create a two tier system—one for large institutions that have more than $10 billion in assets, and another for "highly complex" institutions that have over $50 billion in assets and are fully owned by a parent with over $500 billion in assets. These proposals did not apply to us or the Bank.

On February 9, 2011, the FDIC adopted a final rule which redefines the deposit insurance assessment base as required by the Dodd-Frank Act. The final rule sets the deposit insurance assessment base as average consolidated total assets minus average tangible equity. It also sets a new assessment rate schedule which reflects assessment rate adjustments including potentially reduced rates tied to unsecured debt and potentially increased rates for brokered deposits. The final rule became effective on April 1, 2011. Under the new rule, our FDIC insurance premiums decreased $994 thousand to $1.5 million in 2011 compared to $2.5 million in 2010.

**Transactions with Affiliates.** FII and FSB are affiliates within the meaning of the Federal Reserve Act. The Federal Reserve Act imposes limitations on a bank with respect to extensions of credit to, investments in, and certain other transactions with, its parent bank holding company and the holding company's other subsidiaries. Furthermore, bank loans and extensions of credit to affiliates also are subject to various collateral requirements.

**Community Reinvestment Act.** Under the Community Reinvestment Act, every FDIC-insured institution is obligated, consistent with safe and sound banking practices, to help meet the credit needs of its entire community, including low and moderate income neighborhoods. The Community Reinvestment Act requires the appropriate federal banking regulator, in connection with the examination of an insured institution, to assess the institution's record of meeting the credit needs of its community and to consider this record in its evaluation of certain applications, such as a merger or the establishment of a branch. An unsatisfactory rating may be used as the basis for the denial of an application and will prevent a bank holding company of the institution from making an election to become a financial holding company.

As of its last Community Reinvestment Act examination, Five Star Bank received a rating of "outstanding."

**Interstate Banking and Branching.** The FRB may approve an application of a bank holding company to acquire control of, or acquire all or substantially all of the assets of, a bank located in a state other than the bank holding company's home state, without regard to whether the transaction is prohibited by the laws of any state. The FRB may not approve the acquisition of a bank that has not been in existence for the minimum time period (not exceeding five years) specified by the law of the target bank's home state. The FRB also may not approve an application if the bank holding company (and its bank affiliates) controls or would control more than ten percent of the insured deposits in the U.S. or, generally, 30% or more of the deposits in the target bank's home state or in any state in which the target bank maintains a branch. Individual states may waive the 30% statewide concentration limit. Each state may limit the percentage of total insured deposits in the state that may be held or controlled by a bank or bank holding company to the extent the limitation does not discriminate against out-of-state banks or bank holding companies.

The federal banking agencies are authorized to approve interstate bank merger transactions without regard to whether these transactions are prohibited by the law of any state, unless the home state of one of the banks opted out of interstate mergers prior to June 1, 1997. Interstate acquisitions of branches are permitted only if the law of the state in which the branch is located permits these acquisitions. Interstate mergers and branch acquisitions are subject to the nationwide and statewide-insured deposit concentration limits described above.

**Privacy Rules.** Federal banking regulators, as required under the Gramm-Leach-Bliley Act, have adopted rules limiting the ability of banks and other financial institutions to disclose nonpublic information about consumers to non-affiliated third parties. The rules require disclosure of privacy policies to consumers and, in some circumstances, allow consumers to prevent disclosure of certain personal information to non-affiliated third parties. The privacy provisions of the Gramm-Leach-Bliley Act affect how consumer information is transmitted through diversified financial services companies and conveyed to outside vendors.

**International Money Laundering Abatement and Financial Anti-Terrorism Act of 2001.** The President signed the USA Patriot Act of 2001 into law in October 2001. This act contains the International Money Laundering Abatement and Financial Anti-Terrorism Act of 2001 (the "IMLAFA"). The IMLAFA substantially broadens existing anti-money laundering legislation and the extraterritorial jurisdiction of the U.S., imposes new compliance and due diligence obligations, creates new crimes and penalties, compels the production of documents located both inside and outside the U.S., including those of foreign institutions that have a correspondent relationship in the U.S., and clarifies the safe harbor from civil liability to customers. The Treasury Department has issued a number of regulations implementing the USA Patriot Act that apply certain of its requirements to financial institutions such as our banking and broker-dealer subsidiaries. The regulations impose obligations on financial institutions to maintain appropriate policies, procedures and controls to detect, prevent and report money laundering and terrorist financing. The increased obligations of financial institutions, including us, to identify their customers, watch for and report suspicious transactions, respond to requests for information by regulatory authorities and law enforcement agencies, and share information with other financial institutions, requires the implementation and maintenance of internal procedures, practices and controls which have increased, and may continue to increase, our costs and may subject us to liability.

As noted above, enforcement and compliance-related activity by government agencies has increased. Money laundering and anti-terrorism compliance is among the areas receiving a high level of focus in the present environment.

**Regulatory Reform.** On July 21, 2010, the Dodd-Frank Act was signed into law. The Dodd-Frank Act (as amended) implements far-reaching changes across the financial regulatory landscape, including provisions that, among other things, has or will:

- Centralized responsibility for consumer financial protection by creating a new agency, the Bureau of Consumer Financial Protection, with broad rulemaking, supervision and enforcement authority for a wide range of consumer protection laws that apply to all banks and certain others, including the examination and enforcement powers with respect to any bank with more than $10 billion in assets.
- Require new capital rules and apply the same leverage and risk-based capital requirements that apply to insured depository institutions to most bank holding companies.
- Changed the assessment base for federal deposit insurance from the amount of insured deposits to consolidated average assets less tangible capital. As a result, this change generally imposes more deposit insurance cost on institutions with assets of $10 billion or more.
- Increase the minimum ratio of net worth to insured deposits of the Deposit Insurance Fund from 1.15% to 1.35% and require the FDIC, in setting assessments, to offset the effect of the increase on institutions with assets of less than $10 billion.
- Provide for new disclosure and other requirements relating to executive compensation and corporate governance, including guidelines or regulations on incentive-based compensation and a prohibition on compensation arrangements that encourage inappropriate risks or that could provide excessive compensation.
- Made permanent the $250 thousand limit for federal deposit insurance and provided unlimited federal deposit insurance until December 31, 2012 for non-interest bearing demand transaction accounts and IOLTA accounts at all insured depository institutions.
- Repealed the federal prohibitions on the payment of interest on commercial demand deposits, thereby permitting depository institutions to pay interest on business transaction and other accounts.
- Allow de novo interstate branching by banks.
- Increased the authority of the FRB to examine us and our non-bank subsidiary.
- Required all bank holding companies to serve as a source of financial strength to their depository institution subsidiaries in the event such subsidiaries suffer from financial distress.
- Restrict proprietary trading by banks, bank holding companies and others, and their acquisition and retention of ownership interests in and sponsorship of hedge funds and private equity funds. This restriction is commonly referred to as the "Volcker Rule." There is an exception in the Volcker Rule to allow a bank to organize and offer hedge funds and private equity funds to customers if certain conditions are met. These conditions include, among others, requirements that the bank provides *bona fide* investment advisory services; the funds are organized only in connection with such services and to customers of such services; the bank does not have more than a *de minimis* interest in the funds, limited to a 3% ownership interest in any single fund and an aggregated investment in all funds of 3% of Tier 1 capital; the bank does not guarantee the obligations or performance of the funds; and no director or employee of the bank has an ownership interest in the fund unless he or she provides services directly to the funds. The FRB issued proposed rules in November 2011.

Many aspects of the Dodd-Frank Act are subject to rulemaking and will take effect over several years, making it difficult to anticipate the overall financial impact on us and the financial services industry more generally. Provisions in the legislation may require us to maintain higher capital levels and/or increase our cost of operations and limit certain activities or lines of business.

**TARP-Related Compensation and Corporate Governance Requirements.** The Emergency Economic Stabilization Act of 2008 ("EESA") was signed into law on October 3, 2008 and authorized the Treasury to provide funds to be used to restore liquidity and stability to the U.S. financial system pursuant to the TARP. Under the authority of EESA, Treasury instituted the TARP Capital Purchase Program to encourage U.S. financial institutions to build capital to increase the flow of financing to U.S. businesses and consumers and to support the U.S. economy. As noted above, on December 23, 2008, we participated in this program by issuing 7,503 shares of our Series A preferred stock to the Treasury for a purchase price of $37.5 million in cash and issued the Warrant to the Treasury.

Participation in the TARP Capital Purchase Program included certain requirements and restrictions regarding payment of dividends and compensation that were expanded significantly by the American Recovery and Reinvestment Act of 2009 ("ARRA"), as implemented by the Treasury's Interim Final Rule on TARP Standards for Compensation and Corporate Governance. Our redemption of the Series A preferred stock during the first quarter of 2011, as described under "Dividends", effectively ended these requirements and restrictions.

**Incentive Compensation.** On April 14, 2011, the Federal Reserve issued a proposed regulation on incentive compensation policies (the "Incentive Compensation Proposal") intended to ensure that the incentive compensation policies of banking organizations do not undermine the safety and soundness of such organizations by encouraging excessive risk-taking. The Incentive Compensation Proposal, which covers all employees that have the ability to materially affect the risk profile of an organization, either individually or as part of a group, is based upon the key principles that a banking organization's incentive compensation arrangements should (i) provide incentives that do not encourage risk-taking beyond the organization's ability to effectively identify and manage risks, (ii) be compatible with effective internal controls and risk management, and (iii) be supported by strong corporate governance, including active and effective oversight by the organization's board of directors. Banking organizations were instructed to begin an immediate review of their incentive compensation policies to ensure that they do not encourage excessive risk-taking and implement corrective programs as needed. Where there are deficiencies in the incentive compensation arrangements, they must be immediately addressed.

Additionally, the Incentive Compensation Proposal will require the Federal Reserve to review, as part of the regular, risk-focused examination process, the incentive compensation arrangements of banking organizations, such as us, that are not "large, complex banking organizations." These reviews will be tailored to each organization based on the scope and complexity of the organization's activities and the prevalence of incentive compensation arrangements. The findings of the supervisory initiatives will be included in reports of examination. Deficiencies will be incorporated into the organization's supervisory ratings, which can affect the organization's ability to make acquisitions and take other actions. Enforcement actions may be taken against a banking organization if its incentive compensation arrangements, or related risk-management control or governance processes, pose a risk to the organization's safety and soundness and the organization is not taking prompt and effective measures to correct the deficiencies.

The scope and content of the U.S. banking regulators' policies on executive compensation are continuing to develop and are likely to continue evolving in the near future. It cannot be determined at this time whether compliance with such policies will adversely affect our ability to hire, retain and motivate our key employees.

**Sarbanes-Oxley Act of 2002.** The Sarbanes-Oxley Act of 2002 implemented a broad range of corporate governance, accounting and reporting measures for companies that have securities registered under the Exchange Act, including publicly-held bank holding companies such as Financial Institutions. Specifically, the Sarbanes-Oxley Act of 2002 and the various regulations promulgated thereunder, established, among other things: (i) requirements for audit committees, including independence, expertise, and responsibilities; (ii) responsibilities regarding financial statements for the Chief Executive Officer and Chief Financial Officer of the reporting company; (iii) the forfeiture of bonuses or other incentive-based compensation and profits from the sale of the reporting company's securities by the Chief Executive Officer and Chief Financial Officer in the twelve-month period following the initial publication of any financial statements that later require restatement; (iv) the creation of an independent accounting oversight board; (v) standards for auditors and regulation of audits, including independence provisions that restrict non-audit services that accountants may provide to their audit clients; (vi) disclosure and reporting obligations for the reporting company and their directors and executive officers, including accelerated reporting of stock transactions and a prohibition on trading during pension blackout periods; (vii) a prohibition on personal loans to directors and officers, except certain loans made by insured financial institutions on non-preferential terms and in compliance with other bank regulatory requirements; and (viii) a range of civil and criminal penalties for fraud and other violations of the securities laws.

**Consumer Laws and Regulations.** In addition to the laws and regulations discussed herein, the Bank is also subject to certain consumer laws and regulations that are designed to protect consumers in transactions with banks. While the list set forth herein is not exhaustive, these laws and regulations include, among others, the Truth in Lending Act, the Truth in Savings Act, the Electronic Funds Transfer Act, the Expedited Funds Availability Act, the Equal Credit Opportunity Act, the Fair Housing Act, the Home Mortgage Disclosure Act and the Real Estate Settlement Procedures Act. These laws and regulations mandate certain disclosure requirements and regulate the manner in which financial institutions must deal with customers when taking deposits or making loans to such customers. The Bank must comply with the applicable provisions of these consumer protection laws and regulations as part of its ongoing customer relations. The Check Clearing for the 21st Century Act (the "Check 21 Act"), which became effective on October 28, 2004, creates a new negotiable instrument, called a "substitute check", which banks are required to accept as the legal equivalent of a paper check if it meets the requirements of the Check 21 Act. The Check 21 Act is designed to facilitate check truncation, to foster innovation in the check payment system, and to improve the payment system by shortening processing times and reducing the volume of paper checks.

**Other Future Legislation and Changes in Regulations.** In addition to the specific proposals described above, from time to time, various legislative and regulatory initiatives are introduced in Congress and state legislatures, as well as by regulatory agencies. Such initiatives may include proposals to expand or contract the powers of bank holding companies and depository institutions or proposals to substantially change the financial institution regulatory system. Such legislation could change banking statutes our operating environment in substantial and unpredictable ways. If enacted, such legislation could increase or decrease the cost of doing business, limit or expand permissible activities or affect the competitive balance among banks, savings associations, credit unions, and other financial institutions. We cannot predict whether any such legislation will be enacted, and, if enacted, the effect that it, or any implementing regulations, would have on our financial condition or results of operations. A change in statutes, regulations or regulatory policies applicable to us or our subsidiaries could have a material effect on our business.

**Impact of Inflation and Changing Prices**

Our financial statements included herein have been prepared in accordance with GAAP, which requires us to measure financial position and operating results principally using historic dollars. Changes in the relative value of money due to inflation or recession are generally not considered. The primary effect of inflation on our operations is reflected in increased operating costs. In our view, changes in interest rates affect the financial condition of a financial institution to a far greater degree than changes in the inflation rate. While interest rates are generally influenced by changes in the inflation rate, they do not necessarily change at the same rate or in the same magnitude. Interest rates are sensitive to many factors that are beyond our control, including changes in the expected rate of inflation, general and local economic conditions and the monetary and fiscal policies of the United States government, its agencies and various other governmental regulatory authorities.

**Regulatory and Economic Policies**

Our business and earnings are affected by general and local economic conditions and by the monetary and fiscal policies of the U.S. government, its agencies and various other governmental regulatory authorities. The FRB regulates the supply of money in order to influence general economic conditions. Among the instruments of monetary policy available to the FRB are (i) conducting open market operations in U.S. government obligations, (ii) changing the discount rate on financial institution borrowings, (iii) imposing or changing reserve requirements against financial institution deposits, and (iv) restricting certain borrowings and imposing or changing reserve requirements against certain borrowings by financial institutions and their affiliates. These methods are used in varying degrees and combinations to directly affect the availability of bank loans and deposits, as well as the interest rates charged on loans and paid on deposits. For that reason, the policies of the FRB could have a material effect on our earnings.

**EMPLOYEES**

At December 31, 2011, we had 613 employees. None of the employees are subject to a collective bargaining agreement and management believes its relations with employees are good.

**EXECUTIVE OFFICERS OF REGISTRANT**

The following table sets forth current information regarding our executive officers and certain other significant employees (ages are as of May 9, 2012, the date of the 2012 Annual Meeting of Shareholders).

| Name | Age | Started In | Positions/Offices |
|---|---|---|---|
| Peter G. Humphrey | 57 | 1977 | President and Chief Executive Officer of the Company and the Bank since 1994. |
| Karl F. Krebs | 56 | 2009 | Executive Vice President and Chief Financial Officer of the Company and the Bank since 2009. Senior Financial Specialist at West Valley Environmental Services, LLC, prior to joining FII in 2009. President of Robar General Funding Corp., a mortgage and construction loan broker, from 2006 to 2008. Senior Vice President and Line-of-Business Finance Director at Five Star Bank from 2005 to 2006 and Senior Vice President at Wyoming County Bank from 2004 to 2005. |
| Rita M. Bartol | 51 | 2010 | Senior Vice President and Director of Human Resources of the Company and the Bank since late 2010. Senior Vice President and Director of Human Resources at Cardinal Financial Corporation, a financial holding company, in 2010 and Vice President and Director of Human Resources at Union Bankshares Corporation from 2006 to 2010. Vice President and Human Resources and Organizational Development Manager at M & T Bank Corporation from 1998 to 2005. |
| Martin K. Birmingham | 45 | 2005 | Executive Vice President and Regional President / Commercial Banking Executive Officer of the Bank since 2009. Senior Vice President and Regional President of the Bank since 2005. Senior Team Leader and Regional President of the Rochester Market at Bank of America (formally Fleet Boston Financial) from 2000 to 2005. |
| George D. Hagi | 59 | 2006 | Executive Vice President and Chief Risk Officer of the Company and the Bank since 2006. Senior Vice President and Director of Risk Management at First National Bankshares of Florida and FNB Corp. from 1997 to 2005. |
| Richard J. Harrison | 66 | 2003 | Executive Vice President and Senior Retail Lending Administrator of the Bank since 2009. Senior Vice President and Senior Retail Lending Administrator of the Bank since 2003. Executive Vice President and Chief Credit Officer at Savings Bank of the Finger Lakes from 2001 to 2003. |
| Kevin B. Klotzbach | 59 | 2001 | Senior Vice President and Treasurer of the Bank since 2001. |
| R. Mitchell McLaughlin | 54 | 1981 | Executive Vice President and Chief Information Officer of the Bank since 2009. Senior Vice President and Chief Information Officer of the Bank since 2006. |
| John L. Rizzo | 62 | 2010 | Senior Vice President and Corporate Secretary of the Company and the Bank since 2010. General counsel for the Company and the Bank since 2007. Genesee County (New York) Attorney from 1976 to 2010. |

## ITEM 1A. RISK FACTORS

An investment in our common stock is subject to risks inherent to our business. The material risks and uncertainties that management believes affect us are described below. Before making an investment decision, you should carefully consider the risks and uncertainties described below, together with all of the other information included or incorporated by reference herein. The risks and uncertainties described below are not the only ones facing us. Additional risks and uncertainties that management is not aware of or focused on or that management currently deems immaterial may also impair our business operations. This Annual Report on Form 10-K is qualified in its entirety by these risk factors. Further, to the extent that any of the information contained in this Annual Report on Form 10-K constitutes forward-looking statements, the risk factors set forth below also are cautionary statements identifying important factors that could cause our actual results to differ materially from those expressed in any forward-looking statements made by or on behalf of us.

If any of the following risks actually occur, our financial condition and results of operations could be materially and adversely affected. If this were to happen, the value of our common stock could decline significantly, and you could lose all or part of your investment.

### CREDIT RISKS

**If we experience greater credit losses than anticipated, earnings may be adversely impacted.**

As a lender, we are exposed to the risk that customers will be unable to repay their loans according to their terms and that any collateral securing the payment of their loans may not be sufficient to assure repayment. Credit losses are inherent in the business of making loans and could have a material adverse impact on our results of operations.

We make various assumptions and judgments about the collectability of our loan portfolio, including the creditworthiness of our borrowers and the value of the real estate and other assets serving as collateral, and we provide an allowance for estimated loan losses based on a number of factors. We believe that the allowance for loan losses is adequate. However, if our assumptions or judgments are wrong, the allowance for loan losses may not be sufficient to cover the actual credit losses. We may have to increase the allowance in the future in response to the request of one of our primary banking regulators, to adjust for changing conditions and assumptions, or as a result of any deterioration in the quality of our loan portfolio. The actual amount of future provisions for credit losses may vary from the amount of past provisions.

**Geographic concentration may unfavorably impact our operations.**

Substantially all of our business and operations are concentrated in the Western and Central New York region. As a result of this geographic concentration, our results depend largely on economic conditions in these and surrounding areas. Deterioration in economic conditions in our market could:

- increase loan delinquencies;
- increase problem assets and foreclosures;
- increase claims and lawsuits;
- decrease the demand for our products and services; and
- decrease the value of collateral for loans, especially real estate, in turn reducing customers' borrowing power, the value of assets associated with non-performing loans and collateral coverage.

Generally, we make loans to small to mid-sized businesses whose success depends on the regional economy. These businesses generally have fewer financial resources in terms of capital or borrowing capacity than larger entities. Adverse economic and business conditions in our market areas could reduce our growth rate, affect our borrowers' ability to repay their loans and, consequently, adversely affect our business, financial condition and performance. For example, we place substantial reliance on real estate as collateral for our loan portfolio. A sharp downturn in real estate values in our market area could leave many of these loans inadequately collateralized. If we are required to liquidate the collateral securing a loan to satisfy the debt during a period of reduced real estate values, the impact on our results of operations could be materially adverse.

**We depend on the accuracy and completeness of information about or from customers and counterparties.**

In deciding whether to extend credit or enter into other transactions, we may rely on information furnished by or on behalf of customers and counterparties, including financial statements, credit reports, and other financial information. We may also rely on representations of those customers, counterparties, or other third parties, such as independent auditors, as to the accuracy and completeness of that information. Reliance on inaccurate or misleading financial statements, credit reports, or other financial information could cause us to enter into unfavorable transactions, which could have a material adverse effect on our financial condition and results of operations.

**We are subject to environmental liability risk associated with our lending activities.**

A significant portion of our loan portfolio is secured by real property. During the ordinary course of business, we may foreclose on and take title to properties securing certain loans. In doing so, there is a risk that hazardous or toxic substances could be found on these properties. If hazardous or toxic substances are found, we may be liable for remediation costs, as well as for personal injury and property damage. Environmental laws may require us to incur substantial expenses and may materially reduce the affected property's value or limit our ability to use or sell the affected property. In addition, future laws or more stringent interpretations or enforcement policies with respect to existing laws may increase our exposure to environmental liability. Although we have policies and procedures to perform an environmental review before initiating any foreclosure action on real property, these reviews may not be sufficient to detect all potential environmental hazards. The remediation costs and any other financial liabilities associated with an environmental hazard could have a material adverse effect on our financial condition and results of operations.

**REGULATORY/LEGAL/COMPLIANCE RISKS**

**We are highly regulated and may be adversely affected by changes in banking laws, regulations and regulatory practices.**

We are subject to extensive supervision, regulation and examination. This regulatory structure gives the regulatory authorities extensive discretion in connection with their supervisory and enforcement activities and examination policies to address not only compliance with applicable laws and regulations (including laws and regulations governing consumer credit, and anti-money laundering and anti-terrorism laws), but also capital adequacy, asset quality and risk, management ability and performance, earnings, liquidity, and various other factors. As part of this regulatory structure, we are subject to policies and other guidance developed by the regulatory agencies with respect to capital levels, the timing and amount of dividend payments, the classification of assets and the establishment of adequate loan loss reserves for regulatory purposes. Under this structure the regulatory agencies have broad discretion to impose restrictions and limitations on our operations if they determine, among other things, that our operations are unsafe or unsound, fail to comply with applicable law or are otherwise inconsistent with laws and regulations or with the supervisory policies of these agencies.

This supervisory framework could materially impact the conduct, growth and profitability of our operations. Any failure on our part to comply with current laws, regulations, other regulatory requirements or safe and sound banking practices or concerns about our financial condition, or any related regulatory sanctions or adverse actions against us, could increase our costs or restrict our ability to expand our business and result in damage to our reputation.

**Ongoing financial reform legislation may result in new regulations that could require us to maintain higher capital levels and/or increase our costs of operations or limit certain activities or lines of business.**

On July 21, 2010, President Obama signed the Dodd-Frank Act into law. This new law has significantly changed the current bank regulatory structure and affects the lending, deposit, investment, trading and operating activities of financial institutions and their holding companies. The Dodd-Frank Act requires various federal agencies to adopt a broad range of new implementing rules and regulations, and to prepare numerous studies and reports for Congress. The federal agencies are given significant discretion in drafting the implementing rules and regulations, and consequently, many of the details and much of the rulemaking of the Dodd-Frank Act will not be known for many months or years, making it difficult to anticipate the overall financial impact on us. However, compliance with this new law and its implementing regulations are expected to result in additional operating costs that could have a material adverse effect on our financial condition and results of operations.

**New or changing tax, accounting, and regulatory rules and interpretations could significantly impact our strategic initiatives, results of operations, cash flows, and financial condition.**

The financial services industry is extensively regulated. Federal and state banking regulations are designed primarily to protect the deposit insurance funds and consumers, not to benefit a company's stockholders. These regulations may sometimes impose significant limitations on operations. The significant federal and state banking regulations that affect us are described in the section captioned "Supervision and Regulation" included in Part I, Item 1, "Business". These regulations, along with the currently existing tax, accounting, securities, insurance, and monetary laws, regulations, rules, standards, policies, and interpretations control the methods by which financial institutions conduct business, implement strategic initiatives and tax compliance, and govern financial reporting and disclosures. These laws, regulations, rules, standards, policies, and interpretations are constantly evolving and may change significantly over time.

**Changes in New York State banking regulations or other laws could adversely affect us.**

As of October 3, 2011 the NYS Banking Department and the NYS Insurance Department merged into a single Department of Financial Services, or DFS. Beginning April 1, 2012, the Superintendent of the DFS may assess expenses in such proportion as he or she deems just and reasonable against banks and insurers. The DFS is authorized to create a special account called the "consumer protection account," which will consist of fees and penalties received by the department of state and DFS, as well as other monies received in the form of penalties. These monies will be available to the DFS to pay for costs related to its consumer and investor protection activities. If the consumer protection account is insufficient to cover those costs, the balance would be recoverable through assessments against the industry.

The bill makes New York's "wild card" authority (that was set to expire September 10, 2011) permanent. Under this authority, the Banking Board has the power to grant to New York chartered banking organizations, as well as licensed foreign bank branches and agencies, powers possessed by a counterpart federally-chartered banking institution.

In recent years, credit unions and savings institutions have lobbied in the State of New York to allow local government entities such as cities, towns, counties, public schools, fire districts and public libraries the option of depositing public funds in local credit unions or community savings institutions, a line of business currently serviced primarily by commercial banks, including our Bank.

These changes or the possibility of these changes could adversely affect us.

**OPERATIONAL RISKS**

**If our security systems, or those of merchants, merchant acquirers or other third parties containing information about customers, are compromised, we may be subject to liability and damage to our reputation.**

As part of our business, we collect, process and retain sensitive and confidential client and customer information on our behalf and on behalf of other third parties. Customer data also may be stored on systems of third-party service providers and merchants that may have inadequate security systems. Third-party carriers regularly transport customer data, and may lose sensitive customer information. Unauthorized access to our networks or any of our other information systems potentially could jeopardize the security of confidential information stored in our computer systems or transmitted by our customers or others. If our security systems or those of merchants, processors or other third-party service providers are compromised such that this confidential information is disclosed to unauthorized parties, we may be subject to liability. For example, in the event of a security breach, we may incur losses related to fraudulent use of debit cards issued by us as well as the operational costs associated with reissuing cards. Although we take preventive measures to address these factors, such measures are costly and may become more costly in the future. Moreover, these measures may not protect us from liability, which may not be adequately covered by insurance, or from damage to our reputation.

**We could be subject to losses if we fail to properly safeguard sensitive and confidential information.**

As part of our normal operations, we maintain and transmit confidential information about our clients as well as proprietary information relating to our business operations. We maintain a system of internal controls designed to provide reasonable assurance that fraudulent activity, including misappropriation of assets, fraudulent financial reporting, and unauthorized access to sensitive or confidential data is either prevented or timely detected. Our systems or our third-party service providers' systems could be victimized by unauthorized users or corrupted by computer viruses or other malicious software code, or authorized persons could inadvertently or intentionally release confidential or proprietary information. Such disclosure could, among other things:

- seriously damage our reputation,
- allow competitors access to our proprietary business information,
- subject us to liability for a failure to safeguard client data,
- result in the loss of our existing customers,
- subject us to regulatory action, and
- require significant capital and operating expenditures to investigate and remediate the breach.

**Our information systems may experience an interruption or breach in security.**

We rely heavily on communications and information systems to conduct our business. Any failure, interruption or breach in security of these systems could result in failures or disruptions in our customer relationship management, general ledger, deposit, loan and other systems. While we have policies and procedures designed to prevent or limit the effect of the failure, interruption or security breach of our information systems, there can be no assurance that any such failures, interruptions or security breaches will not occur or, if they do occur, that they will be adequately addressed. The occurrence of any failures, interruptions or security breaches of our information systems could damage our reputation, result in a loss of customer business, subject us to additional regulatory scrutiny, or expose us to civil litigation and possible financial liability, any of which could have a material adverse effect on our financial condition and results of operations.

**We rely on other companies to provide key components of our business infrastructure.**

Third party vendors provide key components of our business infrastructure such as internet connections, network access and core application processing. While we have selected these third party vendors carefully, we do not control their actions. Any problems caused by these third parties, including as a result of their not providing us their services for any reason or their performing their services poorly, could adversely affect our ability to deliver products and services to our customers or otherwise conduct our business efficiently and effectively. Replacing these third party vendors could also entail significant delay and expense.

**We may not be able to attract and retain skilled people.**

Our success depends, in large part, on our ability to attract and retain skilled people. Competition for the best people in most activities engaged in by us can be intense, and we may not be able to hire sufficiently skilled people or to retain them. Further, the rural location of our principal executive offices and many of our bank branches make it difficult for us to attract skilled people to such locations. The unexpected loss of services of one or more of our key personnel could have a material adverse impact on our business because of their skills, knowledge of our markets, years of industry experience, and the difficulty of promptly finding qualified replacement personnel.

**The potential for business interruption exists throughout our organization.**

Integral to our performance is the continued efficacy of our technical systems, operational infrastructure, relationships with third parties and the vast array of associates and key executives in our day-to-day and ongoing operations. Failure by any or all of these resources subjects us to risks that may vary in size, scale and scope. This includes, but is not limited to, operational or technical failures, ineffectiveness or exposure due to interruption in third party support as expected, as well as the loss of key individuals or failure on the part of key individuals to perform properly. Although management has established policies and procedures, including implementation and testing of a comprehensive contingency plan, to address such failures, the occurrence of any such event could have a material adverse effect on our business, which, in turn, could have a material adverse effect on our financial condition and results of operations.

**Our expansion efforts, particularly through new and acquired branches, may not be successful if we fail to manage our growth effectively.**

A key component of our strategy to grow and improve profitability is to expand our branch network into communities within or adjacent to markets where we currently conduct business. We intend to continue to pursue a growth strategy for our business. Operating branches outside of our current market areas may subject us to additional risk, including the local risks related to the new market areas, management of employees from a distance, additional credit risks, logistical operational issues and management time constraints.

We regularly evaluate potential acquisitions and expansion opportunities, and, if appropriate opportunities present themselves, we expect to engage in selected acquisitions of financial institutions in the future, branch acquisitions, or other business growth initiatives or undertakings. There can be no assurance that we will successfully identify appropriate opportunities, that we will be able to negotiate or finance such activities or that such activities, if undertaken, will be successful. While we believe we have the executive management resources and internal systems in place to successfully manage our future growth, we can provide no assurance that we will be able to manage the costs and implementation risks associated with this strategy so that expansion of our branch network will be profitable.

**We may fail to realize any benefits and may incur unanticipated losses related to the assets we acquire and liabilities we assume from current or future acquisitions.**

On January 19, 2012, Five Star Bank entered into an agreement to acquire four retail banking branches currently owned by HSBC Bank USA, N.A. and four retail banking branches currently owned by First Niagara Bank, N.A. The transactions are subject to customary closing conditions, including regulatory approvals, and are expected to close by the end of the third quarter of 2012.

The success of this acquisition and future acquisitions will depend, in part, on our ability to successfully combine the businesses and assets we acquired with our business, and our ability to successfully manage the loan portfolios that were acquired. As with any acquisition involving a financial institution, there may also be business and service changes and disruptions that result in the loss of customers or cause customers to close their accounts and move their business to competing financial institutions. It is possible that the integration process could result in the loss of key employees, the disruption of ongoing business, or inconsistencies in standards, controls, procedures and policies that adversely affect our ability to maintain relationships with clients, customers, depositors and employees, or to achieve the anticipated benefits of the transactions. The loss of some of our key employees or those of the branches being acquired could adversely affect our ability to successfully conduct business in the markets in which those branches operated, which could adversely affect our financial results. Integration efforts will also divert attention and resources from our management. In addition, general market and economic conditions or governmental actions affecting the financial industry generally may inhibit our ability to successfully integrate these operations. If we experience difficulties with the integration process, the anticipated benefits of the transactions may not be realized fully, or at all, or may take longer to realize than expected. Finally, any cost savings that are realized may be offset by losses in revenues or other charges to earnings.

**EXTERNAL RISKS**

**We are subject to interest rate risk.**

Our earnings and cash flows are largely dependent upon our net interest income. Interest rates are highly sensitive to many factors that are beyond our control, including general economic conditions and policies of various governmental and regulatory agencies and, in particular, the Federal Reserve. Changes in monetary policy, including changes in interest rates, could influence not only the interest we receive on loans and investments and the amount of interest we pay on deposits and borrowings, but such changes could also affect (i) our ability to originate loans and obtain deposits; (ii) the fair value of our financial assets and liabilities; and (iii) the average duration of our mortgage-backed securities portfolio and other interest-earning assets. If the interest rates paid on deposits and other borrowings increase at a faster rate than the interest rates received on loans and other investments, our net interest income, and therefore earnings, could be adversely affected. Earnings could also be adversely affected if the interest rates received on loans and other investments fall more quickly than the interest rates paid on deposits and other borrowings.

Although management believes it has implemented effective asset and liability management strategies to reduce the potential effects of changes in interest rates on our results of operations, any substantial, unexpected or prolonged change in market interest rates could have a material adverse effect on our financial condition and results of operations. Also, our interest rate risk modeling techniques and assumptions likely may not fully predict or capture the impact of actual interest rate changes on our balance sheet.

**Our business may be adversely affected by conditions in the financial markets and economic conditions generally.**

From December 2007 through June 2009, the U.S. economy was in recession. Business activity across a wide range of industries and regions in the U.S. was greatly reduced. Although economic conditions have begun to improve, certain sectors, such as real estate, remain weak and unemployment remains high. Local governments and many businesses are still in serious difficulty due to lower consumer spending and reduced tax collections.

Market conditions also led to the failure or merger of several prominent financial institutions and numerous regional and community-based financial institutions. These failures, as well as projected future failures, have had a significant negative impact on the capitalization level of the deposit insurance fund of the FDIC, which, in turn, has led to past increases in deposit insurance premiums paid by financial institutions.

Our financial performance generally, and in particular the ability of borrowers to pay interest on and repay principal of outstanding loans and the value of collateral securing those loans, as well as demand for loans and other products and services we offer, is highly dependent on the business environment in the markets where we operate, in the State of New York and in the United States as a whole. A favorable business environment is generally characterized by, among other factors, economic growth, efficient capital markets, low inflation, low unemployment, high business and investor confidence, and strong business earnings. Unfavorable or uncertain economic and market conditions can be caused by declines in economic growth, business activity or investor or business confidence; limitations on the availability or increases in the cost of credit and capital; increases in inflation or interest rates; high unemployment, natural disasters; or a combination of these or other factors.

Overall, during 2010 and 2011, the business environment has been adverse for many households and businesses in the United States and worldwide. While economic conditions in the New York, the United States and worldwide have begun to improve, there can be no assurance that this improvement will continue. Such conditions could adversely affect our financial condition and results of operations.

Approximately 20% of our investment securities portfolio at December 31, 2011 is comprised of municipal securities issued by or on behalf of New York and its political subdivisions, agencies or instrumentalities, the interest on which is exempt from regular federal income tax. Risks associated with investing in municipal securities include political, economic and regulatory factors which may affect the issuers. The fiscal concerns facing New York may lead credit rating agencies to downgrade its debt obligations. It is uncertain how the financial markets may react to any potential future ratings downgrade in New York's debt obligations. In the event New York was downgraded, local municipalities with a high dependency on state aid could be adversely impacted.

**Our earnings are significantly affected by the fiscal and monetary policies of the federal government and its agencies.**

The policies of the Federal Reserve impact us significantly. The Federal Reserve regulates the supply of money and credit in the United States. Its policies directly and indirectly influence the rate of interest earned on loans and paid on borrowings and interest-bearing deposits and can also affect the value of financial instruments we hold. Those policies determine to a significant extent our cost of funds for lending and investing. Changes in those policies are beyond our control and are difficult to predict. Federal Reserve policies can also affect our borrowers, potentially increasing the risk that they may fail to repay their loans. For example, a tightening of the money supply by the Federal Reserve could reduce the demand for a borrower's products and services. This could adversely affect the borrower's earnings and ability to repay its loan, which could have a material adverse effect on our financial condition and results of operations.

**The soundness of other financial institutions could adversely affect us.**

Financial services institutions are interrelated as a result of trading, clearing, counterparty, or other relationships. We have exposure to many different industries and counterparties, and we routinely execute transactions with counterparties in the financial services industry, including commercial banks, brokers and dealers, investment banks, and other institutional clients. Many of these transactions expose us to credit risk in the event of a default by our counterparty or client. In addition, our credit risk may be exacerbated when the collateral held by us cannot be realized or is liquidated at prices not sufficient to recover the full amount of the credit or derivative exposure due us. Any such losses could have a material adverse effect on our financial condition and results of operations.

**Our market value could result in an impairment of goodwill.**

Our goodwill is evaluated for impairment on an annual basis or when triggering events or circumstances indicate impairment may exist. Significant and sustained declines in our stock price and market capitalization, significant declines in our expected future cash flows, significant adverse changes in the business climate or slower growth rates could result in impairment of goodwill. At December 31, 2011, we had goodwill of $37.4 million, representing approximately 16% of shareholders' equity. If impairment of goodwill was determined to exist, we would be required to write down our goodwill as a charge to earnings, which could have a material adverse impact on our results of operations or financial condition. For further discussion, see Note 1, Summary of Significant Accounting Policies, and Note 6, Goodwill and Other Intangible Assets, to the Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K.

**We operate in a highly competitive industry and market area.**

We face substantial competition in all areas of our operations from a variety of different competitors, many of which are larger and may have more financial resources. Such competitors primarily include national, regional and internet banks within the various markets in which we operate. We also face competition from many other types of financial institutions, including, without limitation, savings and loan associations, credit unions, finance companies, brokerage firms, insurance companies and other financial intermediaries. The financial services industry could become even more competitive as a result of legislative, regulatory and technological changes and continued consolidation. Banks, securities firms and insurance companies can merge under the umbrella of a financial holding company, which can offer virtually any type of financial service, including banking, securities underwriting, insurance (both agency and underwriting), and merchant banking. Also, technology has lowered barriers to entry and made it possible for nonbanks to offer products and services traditionally provided by banks, such as automatic transfer and automatic payment systems. Many of our competitors have fewer regulatory constraints and may have lower cost structures. Additionally, due to their size, many competitors may be able to achieve economies of scale and, as a result, may offer a broader range of products and services as well as better pricing for those products and services than we can.

Our ability to compete successfully depends on a number of factors, including, among other things:

- the ability to develop, maintain and build upon long-term customer relationships based on top quality service, high ethical standards and safe, sound assets;
- the ability to expand our market position;
- the scope, relevance and pricing of products and services offered to meet customer needs and demands;
- the rate at which we introduce new products and services relative to our competitors;
- customer satisfaction with our level of service; and
- industry and general economic trends.

Failure to perform in any of these areas could significantly weaken our competitive position, which could adversely affect our growth and profitability, which, in turn, could have a material adverse effect on our financial condition and results of operations.

**LIQUIDITY RISKS**

**Liquidity is essential to our businesses.**

Our liquidity could be impaired by an inability to access the capital markets or unforeseen outflows of cash. This situation may arise due to circumstances that we may be unable to control, such as a general market disruption or an operational problem that affects third parties or us. Our efforts to monitor and manage liquidity risk may not be successful or sufficient to deal with dramatic or unanticipated reductions in our liquidity. In such events, our cost of funds may increase, thereby reducing our net interest income, or we may need to sell a portion of our investment and/or loan portfolio, which, depending upon market conditions, could result in us realizing a loss.

**We may need to raise additional capital in the future and such capital may not be available on acceptable terms or at all.**

We may need to raise additional capital in the future to provide sufficient capital resources and liquidity to meet our commitments and business needs. Our ability to raise additional capital, if needed, will depend on, among other things, conditions in the capital markets at that time, which are outside of our control, and our financial performance.

In addition, we are highly regulated, and our regulators could require us to raise additional common equity in the future. We and our regulators perform a variety of analyses of our assets, including the preparation of stress case scenarios, and as a result of those assessments we could determine, or our regulators could require us, to raise additional capital.

We cannot assure that such capital will be available on acceptable terms or at all. Any occurrence that may limit our access to the capital markets, such as a decline in the confidence of debt purchasers, depositors of the Bank or counterparties participating in the capital markets, or a downgrade of our debt rating, may adversely affect our capital costs and ability to raise capital and, in turn, our liquidity. An inability to raise additional capital on acceptable terms when needed could have a material adverse impact on our business, financial condition, results of operations or liquidity.

**We rely on dividends from our subsidiaries for most of our revenue.**

We are a separate and distinct legal entity from our subsidiaries. A substantial portion of our revenue comes from dividends from our Bank subsidiary. These dividends are the principal source of funds we use to pay dividends on our common and preferred stock, and to pay interest and principal on our debt. Various federal and/or state laws and regulations limit the amount of dividends that our Bank subsidiary and nonbank subsidiary may pay to us. Also, our right to participate in a distribution of assets upon a subsidiary's liquidation or reorganization is subject to the prior claims of the subsidiary's creditors. In the event our bank subsidiary is unable to pay dividends to us, we may not be able to service debt, pay obligations, or pay dividends on our common and preferred stock. The inability to receive dividends from our bank subsidiary could have a material adverse effect on our business, financial condition, and results of operations.

## RISKS RELATED TO AN INVESTMENT IN OUR COMMON STOCK

**The market price for our common stock varies, and you should purchase common stock for long-term investment only.**

Although our common stock is currently traded on the NASDAQ Global Select Market, we cannot assure you that there will, at any time in the future, be an active trading market for our common stock. Even if there is an active trading market for our common stock, we cannot assure you that you will be able to sell all of your shares of common stock at one time or at a favorable price, if at all. As a result, you should purchase shares of common stock described herein only if you are capable of, and seeking, to make a long-term investment in our common stock.

**We may issue debt and equity securities or securities convertible into equity securities, any of which may be senior to our common stock as to distributions and in liquidation, which could negatively affect the value of our common stock.**

In the future, we may attempt to increase our capital resources by entering into debt or debt-like financing that is unsecured or secured by all or up to all of our assets, or by issuing additional debt or equity securities, which could include issuances of secured or unsecured commercial paper, medium-term notes, senior notes, subordinated notes, preferred stock or securities convertible into or exchangeable for equity securities. In the event of our liquidation, our lenders and holders of our debt and preferred securities would receive a distribution of our available assets before distributions to the holders of our common stock. Because our decision to incur debt and issue securities in our future offerings will depend on market conditions and other factors beyond our control, we cannot predict or estimate the amount, timing or nature of our future offerings and debt financings. Further, market conditions could require us to accept less favorable terms for the issuance of our securities in the future.

**We may not pay dividends on our common stock.**

Holders of our common stock are only entitled to receive such dividends as our Board of Directors may declare out of funds legally available for such payments. Although we have historically declared cash dividends on our common stock, we are not required to do so and may reduce or eliminate our common stock dividend in the future. This could adversely affect the market price of our common stock.

**Our certificate of incorporation, our bylaws, and certain banking laws may have an anti-takeover effect.**

Provisions of our certificate of incorporation, our bylaws, and federal and state banking laws, including regulatory approval requirements, could make it more difficult for a third party to acquire us, even if doing so would be perceived to be beneficial to our shareholders. The combination of these provisions may discourage others from initiating a potential merger, takeover or other change of control transaction, which, in turn, could adversely affect the market price of our common stock.

## ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

## ITEM 2. PROPERTIES

We own a 27,400 square foot building in Warsaw, New York that serves as our headquarters, and principal executive and administrative offices. Additionally, we are obligated under a lease commitment through 2017 for a 17,750 square foot regional administrative facility in Pittsford, New York.

We are engaged in the banking business through 50 branch offices, of which 33 are owned and 17 are leased, in fourteen contiguous counties of Western and Central New York: Allegany, Cattaraugus, Cayuga, Chautauqua, Chemung, Erie, Genesee, Livingston, Monroe, Ontario, Seneca, Steuben, Wyoming and Yates Counties. The operating leases for our branch offices expire at various dates through the year 2036 and generally include options to renew.

We believe that our properties have been adequately maintained, are in good operating condition and are suitable for our business as presently conducted, including meeting the prescribed security requirements. For additional information, see Note 5, Premises and Equipment, Net, and Note 9, Commitments and Contingencies, in the accompanying financial statements included in Part II, Item 8, “Financial Statements and Supplementary Data”, all of which are included elsewhere in this report and incorporated herein by reference thereto.

## ITE M 3. LEGAL PROCEEDINGS

From time to time we are a party to or otherwise involved in legal proceedings arising in the normal course of business. Management does not believe that there is any pending or threatened proceeding against us, which, if determined adversely, would have a material adverse effect on our business, results of operations or financial condition.

## ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

## PART II

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

Our common stock is traded on the NASDAQ Global Select Market under the ticker symbol "FISI." At December 31, 2011, 13,803,116 shares of our common stock were outstanding and held by approximately 1,400 shareholders of record. During 2011, the high sales price of our common stock was $20.36 and the low sales price was $12.18. The closing price per share of common stock on December 31, 2011, the last trading day of our fiscal year, was $16.14. We declared dividends of $0.47 per common share during the year ended December 31, 2011. See additional information regarding the market price and dividends paid in Part II, Item 6, "Selected Financial Data".

We have paid regular quarterly cash dividends on our common stock and our Board of Directors presently intends to continue this practice, subject to our results of operations and the need for those funds for debt service and other purposes. See the discussions in the section captioned "Supervision and Regulation" included in Part I, Item 1, "Business", in the section captioned "Liquidity and Capital Resources" included in Part II, Item 7, in "Management's Discussion and Analysis of Financial Condition and Results of Operations" and in Note 10, Regulatory Matters, in the accompanying financial statements included in Part II, Item 8, "Financial Statements and Supplementary Data", all of which are included elsewhere in this report and incorporated herein by reference thereto.

**Equity Compensation Plan Information**

The following table sets forth, as of December 31, 2011, information about our equity compensation plans that have been approved by our shareholders, including the number of shares of our common stock exercisable under all outstanding options, warrants and rights, the weighted average exercise price of all outstanding options, warrants and rights and the number of shares available for future issuance under our equity compensation plans. We have no equity compensation plans that have not been approved by our shareholders.

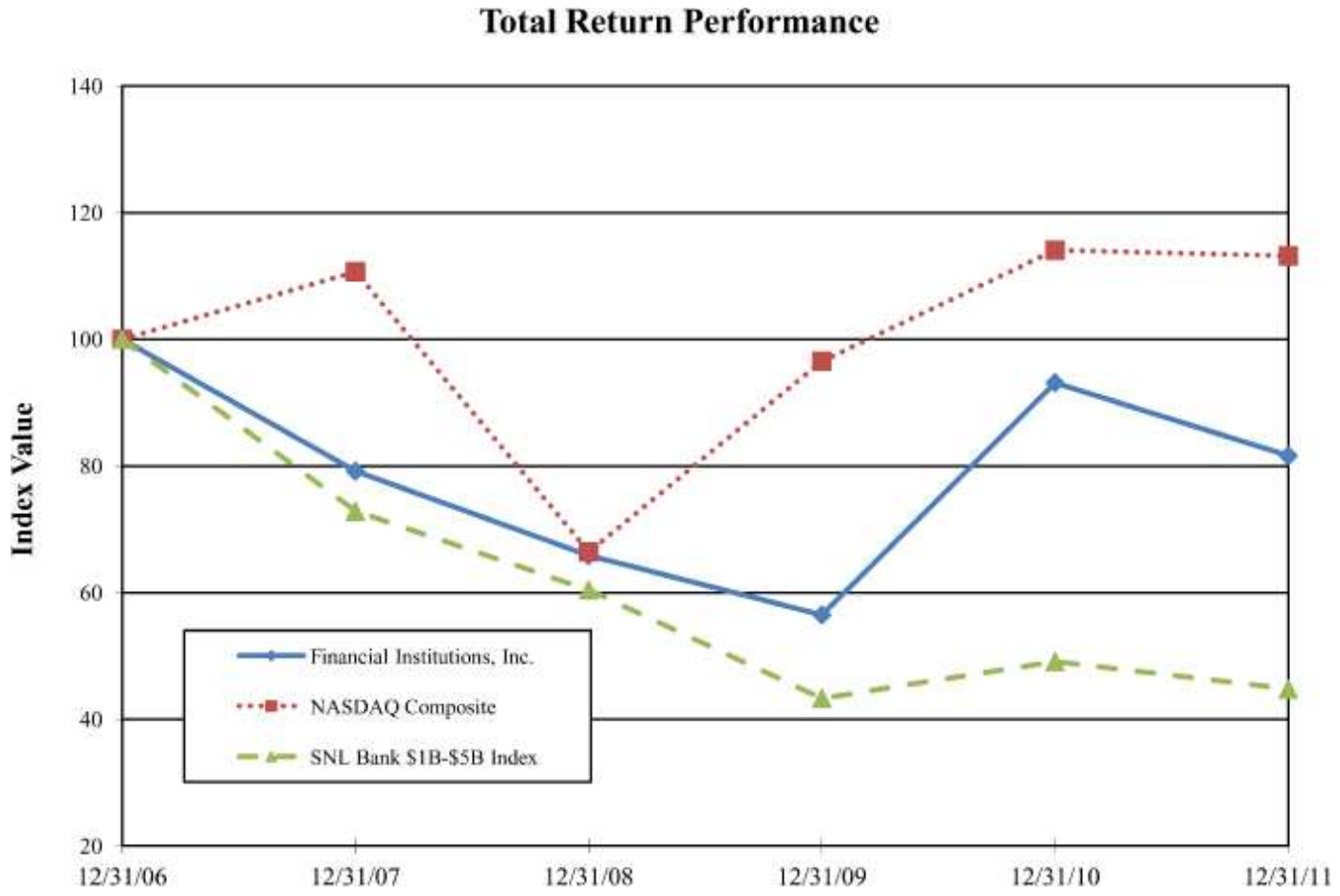
| Plan Category | Number of securities to be issued upon exercise of outstanding options, warrants and rights (a) | Weighted average exercise price of outstanding options, warrants and rights (b) | Number of securities remaining for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c) |
|---|---|---|---|
| Equity compensation plans approved by shareholders | 534,712 (1) | $ 20.70 (1) | 664,350 (2) |
| Equity compensation plans not approved by shareholders | — | $ — | — |

(1) Includes 166,654 shares of unvested restricted stock awards outstanding as of December 31, 2011. The weighted average exercise price excludes such awards.

(2) Represents the 940,000 aggregate shares approved for issuance under our two active equity compensation plans, reduced by 278,930 shares, which are the 170,082 restricted stock awards issued under these plans to date plus an adjustment of 108,848 shares. Pursuant to the terms of the plans, for purposes of calculating the number of shares available for issuance, each share of common stock granted pursuant to a restricted stock award shall count as 1.64 shares of common stock.

**Stock Performance Graph**

The stock performance graph below compares (a) the cumulative total return on our common stock for the period beginning December 31, 2006 as reported by the NASDAQ Global Select Market, through December 31, 2011, (b) the cumulative total return on stocks included in the NASDAQ Composite Index over the same period, and (c) the cumulative total return, as compiled by SNL Financial L.C., of Major Exchange (NYSE, AMEX and NASDAQ) Banks with $1 billion to $5 billion in assets over the same period. Cumulative return assumes the reinvestment of dividends. The graph was prepared by SNL Financial, LC and is expressed in dollars based on an assumed investment of $100.




| | Period Ending | | | | | |
|---|---|---|---|---|---|---|
| **Index** | **12/31/06** | **12/31/07** | **12/31/08** | **12/31/09** | **12/31/10** | **12/31/11** |
| Financial Institutions, Inc. | 100.00 | 79.17 | 65.84 | 56.47 | 93.13 | 81.59 |
| NASDAQ Composite | 100.00 | 110.66 | 66.42 | 96.54 | 114.06 | 113.16 |
| SNL Bank $1B-$5B Index | 100.00 | 72.84 | 60.42 | 43.31 | 49.09 | 44.77 |

## ITEM 6. SELECTED FINANCIAL DATA

| (Dollars in thousands, except selected ratios and per share data) | At or for the year ended December 31, 2011 | 2010 | 2009 | 2008 | 2007 |
|---|---|---|---|---|---|
| **Selected financial condition data:** | | | | | |
| Total assets | $ 2,336,353 | $ 2,214,307 | $ 2,062,389 | $ 1,916,919 | $ 1,857,876 |
| Loans, net | 1,461,516 | 1,325,524 | 1,243,265 | 1,102,330 | 948,652 |
| Investment securities | 650,815 | 694,530 | 620,074 | 606,038 | 754,720 |
| Deposits | 1,931,599 | 1,882,890 | 1,742,955 | 1,633,263 | 1,575,971 |
| Borrowings | 150,698 | 103,877 | 106,390 | 70,820 | 68,210 |
| Shareholders' equity | 237,194 | 212,144 | 198,294 | 190,300 | 195,322 |
| Common shareholders' equity [1] | 219,721 | 158,359 | 144,876 | 137,226 | 177,741 |
| Tangible common shareholders' equity [2] | 182,352 | 120,990 | 107,507 | 99,577 | 139,786 |
| **Selected operations data:** | | | | | |
| Interest income | $ 95,118 | $ 96,509 | $ 94,482 | $ 98,948 | $ 105,212 |
| Interest expense | 13,255 | 17,720 | 22,217 | 33,617 | 47,139 |
| Net interest income | 81,863 | 78,789 | 72,265 | 65,331 | 58,073 |
| Provision for loan losses | 7,780 | 6,687 | 7,702 | 6,551 | 116 |
| Net interest income after provision for loan losses | 74,083 | 72,102 | 64,563 | 58,780 | 57,957 |
| Noninterest income (loss) [3] | 23,925 | 19,454 | 18,795 | (48,778) | 20,680 |
| Noninterest expense | 63,794 | 60,917 | 62,777 | 57,461 | 57,428 |
| Income (loss) before income taxes | 34,214 | 30,639 | 20,581 | (47,459) | 21,209 |
| Income tax expense (benefit) | 11,415 | 9,352 | 6,140 | (21,301) | 4,800 |
| Net income (loss) | $ 22,799 | $ 21,287 | $ 14,441 | $ (26,158) | $ 16,409 |
| Preferred stock dividends and accretion | 3,182 | 3,725 | 3,697 | 1,538 | 1,483 |
| Net income (loss) applicable to common shareholders | $ 19,617 | $ 17,562 | $ 10,744 | $ (27,696) | $ 14,926 |
| **Stock and related per share data:** | | | | | |
| Earnings (loss) per common share: | | | | | |
| Basic | $ 1.50 | $ 1.62 | $ 0.99 | $ (2.54) | $ 1.34 |
| Diluted | 1.49 | 1.61 | 0.99 | (2.54) | 1.33 |
| Cash dividends declared on common stock | 0.47 | 0.40 | 0.40 | 0.54 | 0.46 |
| Common book value per share [1] | 15.92 | 14.48 | 13.39 | 12.71 | 16.14 |
| Tangible common book value per share [2] | 13.21 | 11.06 | 9.94 | 9.22 | 12.69 |
| Market price (NASDAQ: FISI): | | | | | |
| High | 20.36 | 20.74 | 15.99 | 22.50 | 23.71 |
| Low | 12.18 | 10.91 | 3.27 | 10.06 | 16.18 |
| Close | 16.14 | 18.97 | 11.78 | 14.35 | 17.82 |

[1] Excludes preferred shareholders' equity.

[2] Excludes preferred shareholders' equity, goodwill and other intangible assets.

[3] The 2011, 2010, 2009 and 2008 figures include other-than-temporary impairment ("OTTI") charges of $18 thousand, $594 thousand, $4.7 million and $68.2 million, respectively. There were no OTTI charges in 2007.

| (Dollars in thousands, except per share data) | At or for the year ended December 31, 2011 | 2010 | 2009 | 2008 | 2007 |
|---|---|---|---|---|---|
| **Selected financial ratios and other data:** | | | | | |
| **Performance ratios:** | | | | | |
| Net income (loss), returns on: | | | | | |
| Average assets | 1.00% | 0.98% | 0.71% | -1.37% | 0.86% |
| Average equity | 9.82 | 10.07 | 7.43 | -14.30 | 8.84 |
| Average common equity [1] | 9.47 | 11.14 | 7.61 | -16.84 | 8.89 |
| Average tangible common equity [2] | 11.55 | 14.59 | 10.37 | -21.87 | 11.50 |
| Common dividend payout ratio [3] | 31.33 | 24.69 | 40.40 | NA | 34.33 |
| Net interest margin (fully tax-equivalent) | 4.04 | 4.07 | 4.04 | 3.93 | 3.53 |
| Efficiency ratio [4] | 60.55% | 60.36% | 65.52% | 64.07% | 68.77% |
| **Capital ratios:** | | | | | |
| Leverage ratio | 8.63% | 8.31% | 7.96% | 8.05% | 9.35% |
| Tier 1 risk-based capital | 12.20 | 12.34 | 11.95 | 11.83 | 15.74 |
| Total risk-based capital | 13.45 | 13.60 | 13.21 | 13.08 | 16.99 |
| Equity to assets [5] | 10.20 | 9.75 | 9.55 | 9.60 | 9.73 |
| Common equity to assets [1] [5] | 9.10 | 7.28 | 6.94 | 8.63 | 8.81 |
| Tangible common equity to tangible assets [2] [5] | 7.58% | 5.65% | 5.19% | 6.78% | 6.95% |
| **Asset quality:** | | | | | |
| Non-performing loans | $ 7,076 | $ 7,582 | $ 8,681 | $ 8,196 | $ 8,077 |
| Non-performing assets | 9,187 | 8,895 | 10,442 | 9,252 | 9,498 |
| Allowance for loan losses | 23,260 | 20,466 | 20,741 | 18,749 | 15,521 |
| Net loan charge-offs | $ 4,986 | $ 6,962 | $ 5,710 | $ 3,323 | $ 1,643 |
| Non-performing loans to total loans | 0.48% | 0.56% | 0.69% | 0.73% | 0.84% |
| Non-performing assets to total assets | 0.39 | 0.40 | 0.51 | 0.48 | 0.51 |
| Net charge-offs to average loans | 0.36 | 0.54 | 0.47 | 0.32 | 0.18 |
| Allowance for loan losses to total loans | 1.57 | 1.52 | 1.64 | 1.67 | 1.61 |
| Allowance for loan losses to non-performing loans | 329% | 270% | 239% | 229% | 192% |
| **Other data:** | | | | | |
| Number of branches | 50 | 50 | 50 | 51 | 50 |
| Full time equivalent employees | 575 | 577 | 572 | 600 | 621 |

(1) Excludes preferred shareholders' equity.

(2) Excludes preferred shareholders' equity, goodwill and other intangible assets.

(3) Common dividend payout ratio equals dividends declared during the year divided by earnings per share for the year. There is no ratio shown for years where we both declared a dividend and incurred a loss because the ratio would result in a negative payout since the dividend declared (paid out) will always be greater than 100% of earnings.

(4) Efficiency ratio equals noninterest expense less other real estate expense and amortization of intangible assets as a percentage of net revenue, defined as the sum of tax-equivalent net interest income and noninterest income before net gains and impairment charges on investment securities and proceeds from company owned life insurance included in income (all from continuing operations).

(5) Ratios calculated using average balances for the periods shown.

## SELECTED QUARTERLY DATA

| (Dollars in thousands, except per share data) | 2011 Fourth Quarter | 2011 Third Quarter | 2011 Second Quarter | 2011 First Quarter |
|---|---|---|---|---|
| Interest income | $ 23,875 | $ 23,774 | $ 23,830 | $ 23,639 |
| Interest expense | 2,721 | 3,156 | 3,577 | 3,801 |
| Net interest income | 21,154 | 20,618 | 20,253 | 19,838 |
| Provision for loan losses | 2,162 | 3,480 | 1,328 | 810 |
| Net interest income, after provision for loan losses | 18,992 | 17,138 | 18,925 | 19,028 |
| Noninterest income | 5,767 | 8,036 | 4,974 | 5,148 |
| Noninterest expense | 16,279 | 17,012 | 15,153 | 15,350 |
| Income before income taxes | 8,480 | 8,162 | 8,746 | 8,826 |
| Income tax expense | 2,718 | 2,664 | 3,027 | 3,006 |
| Net income | $ 5,762 | $ 5,498 | $ 5,719 | $ 5,820 |
| Preferred stock dividends | 369 | 368 | 370 | 2,075 |
| Net income applicable to common shareholders | $ 5,393 | $ 5,130 | $ 5,349 | $ 3,745 |
| Earnings per common share [1]: | | | | |
| Basic | $ 0.39 | $ 0.38 | $ 0.39 | $ 0.33 |
| Diluted | 0.39 | 0.37 | 0.39 | 0.33 |
| Market price (NASDAQ: FISI): | | | | |
| High | $ 17.26 | $ 17.98 | $ 17.93 | $ 20.36 |
| Low | 12.18 | 13.63 | 15.20 | 16.40 |
| Close | 16.14 | 14.26 | 16.42 | 17.52 |
| Dividends declared | $ 0.13 | $ 0.12 | $ 0.12 | $ 0.10 |

| (Dollars in thousands, except per share data) | 2010 Fourth Quarter | 2010 Third Quarter | 2010 Second Quarter | 2010 First Quarter |
|---|---|---|---|---|
| Interest income | $ 24,297 | $ 24,186 | $ 24,202 | $ 23,824 |
| Interest expense | 4,229 | 4,393 | 4,526 | 4,572 |
| Net interest income | 20,068 | 19,793 | 19,676 | 19,252 |
| Provision for loan losses | 1,980 | 2,184 | 2,105 | 418 |
| Net interest income, after provision for loan losses | 18,088 | 17,609 | 17,571 | 18,834 |
| Noninterest income | 5,274 | 5,131 | 4,966 | 4,083 |
| Noninterest expense | 16,373 | 14,936 | 14,870 | 14,738 |
| Income before income taxes | 6,989 | 7,804 | 7,667 | 8,179 |
| Income tax expense | 1,891 | 2,141 | 2,469 | 2,851 |
| Net income | $ 5,098 | $ 5,663 | $ 5,198 | $ 5,328 |
| Preferred stock dividends | 933 | 932 | 931 | 929 |
| Net income applicable to common shareholders | $ 4,165 | $ 4,731 | $ 4,267 | $ 4,399 |
| Earnings per common share [1]: | | | | |
| Basic | $ 0.38 | $ 0.44 | $ 0.39 | $ 0.41 |
| Diluted | 0.38 | 0.43 | 0.39 | 0.40 |
| Market price (NASDAQ: FISI): | | | | |
| High | $ 20.74 | $ 19.94 | $ 19.48 | $ 15.40 |
| Low | 16.80 | 14.14 | 14.07 | 10.91 |
| Close | 18.97 | 17.66 | 17.76 | 14.62 |
| Dividends declared | $ 0.10 | $ 0.10 | $ 0.10 | $ 0.10 |

[1] Earnings per share data is computed independently for each of the quarters presented. Therefore, the sum of the quarterly earnings per common share amounts may not equal the total for the year.

**2011 FOURTH QUARTER RESULTS**

Net income was $5.8 million for the fourth quarter of 2011 compared with $5.1 million for the fourth quarter of 2010. After preferred dividends, fourth quarter diluted earnings per share for 2011 was $0.39 compared with $0.38 per share for the fourth quarter of 2010.

Net interest income totaled $21.2 million for the three months ended December 31, 2011, an increase of $1.1 million or 5% over the fourth quarter of 2010. Average earning assets increased $77.0 million during the fourth quarter 2011 compared to the same quarter last year, as a $127.4 million increase in average loans was partially offset by a $50.4 million decrease in investment securities and interest earning deposits.

The net interest margin on a tax-equivalent basis was 4.07% in the fourth quarter of 2011, compared with 4.01% in the fourth quarter of 2010. Our yield on earning-assets decreased 25 basis points in the fourth quarter of 2011 compared with the same quarter last year. This was due to the effect of reinvesting cash flows in the low interest rate environment. The cost of interest-bearing liabilities decreased 38 basis points compared with the fourth quarter of 2010, primarily a result of the redemption of our 10.20% junior subordinated debentures and the continued re-pricing of the our certificates of deposit.

The provision for loan losses was $2.2 million for the fourth quarter of 2011 compared with $2.0 million for the fourth quarter of 2010. Net charge-offs were $1.9 million, or 0.51% annualized, of average loans, up from $1.2 million, or 0.37% annualized, of average loans in the fourth quarter of 2010. Net charge-offs for the fourth quarter of 2011 includes $905 thousand for the charge-off of a commercial business relationship. See the sections “Allowance for Loan Losses” and “Non-performing Assets and Potential Problem Loans” for additional information on net charge-offs and non-performing loans.

Noninterest income totaled $5.8 million for the fourth quarter of 2011, a 9% increase over the fourth quarter of 2010. The majority of the increase related to higher pre-tax net gains from the sale of investment securities of $656 thousand during the fourth of quarter 2011 compared with $30 thousand during the fourth quarter of 2010.

Noninterest expense was $16.3 million for the fourth quarter of 2011, a decrease of $94 thousand million or 1% from the fourth quarter of 2010.

Income tax expense for the fourth quarter of 2011 was $2.7 million compared to $1.9 million for the fourth quarter of 2010. The change in income tax expense was primarily due to a $1.5 million increase in pretax income between the years.

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

*The following is a discussion and analysis of our financial position and results of operations and should be read in conjunction with the information set forth under Part I, Item 1A, "Risks Factors", and our consolidated financial statements and notes thereto appearing under Part II, Item 8, "Financial Statements and Supplementary Data" of this report.*

### OVERVIEW

#### Business Overview

Financial Institutions, Inc. is a financial holding company headquartered in New York State, providing banking and nonbanking financial services to individuals and businesses primarily in our Western and Central New York footprint. We have also expanded our indirect lending network to include relationships with franchised automobile dealers in the Capital District of New York and Northern Pennsylvania. Through our wholly-owned banking subsidiary, Five Star Bank, we provide a wide range of services, including business and consumer loan and depository services, as well as other traditional banking services. Through our nonbanking subsidiary, Five Star Investment Services, we provide brokerage and investment advisory services to supplement our banking business.

Our primary sources of revenue, are net interest income (predominantly from interest earned on our loans and securities, net of interest paid on deposits and other funding sources), and noninterest income, particularly fees and other revenue from financial services provided to customers or ancillary services tied to loans and deposits. Business volumes and pricing drive revenue potential, and tend to be influenced by overall economic factors, including market interest rates, business spending, consumer confidence, economic growth, and competitive conditions within the marketplace. We are not able to predict market interest rate fluctuations with certainty and our asset/liability management strategy may not prevent interest rate changes from having a material adverse effect on our results of operations and financial condition.

#### Recent Developments

On January 19, 2012, Five Star Bank entered into an agreement to acquire four retail banking branches currently owned by HSBC Bank USA, N.A. located in Elmira, Elmira Heights, Horseheads and Albion, New York and four retail banking branches currently owned by First Niagara Bank, N.A located in Medina, Waterloo, Batavia and Brockport, New York. The deposits associated with these branches total approximately $376 million, while loans total approximately $94 million. The transactions are subject to customary closing conditions, including regulatory approvals, and are expected to close by the end of the third quarter of this year.

#### 2011 Significant Events

**Common Stock Offering.** In March 2011, we completed the sale of 2,813,475 shares of our common stock through an underwritten public offering at a price of $16.35 per share in an effort to restructure our capital position and improve the quality of our capital. The net proceeds of the offering, after deducting underwriting discounts and commissions and offering expenses, amounted to $43.1 million. A portion of the proceeds from this offering was used to redeem our Series A preferred stock and the junior subordinated debentures.

**Redemption of Series A Preferred Stock.** In March 2011, we completed the full redemption of our $37.5 million Series A preferred stock issued in connection with the TARP Capital Purchase Program. The redemption resulted in a one-time, non-cash redemption charge of $1.2 million, reflecting the accelerated accretion of the remaining discount on the preferred stock, which reduced 2011 diluted earnings per common share by $0.09.

The complete redemption of the Series A preferred stock removed the TARP restrictions pertaining to our ability to declare and pay dividends and repurchase our common stock, as well as certain restrictions associated with executive compensation.

In May 2011, we repurchased the warrant to purchase up to 378,175 shares of our common stock at an exercise price of $14.88 per share issued to the Treasury. The repurchase price of $2.1 million was recorded as a reduction of additional paid-in capital.

**Redemption of Junior Subordinated Debentures.** In August 2011, we redeemed all of the 10.20% junior subordinated debentures at a redemption price equaling 105.1% of the principal amount redeemed, plus all accrued and unpaid interest. As a result of the redemption, we recognized a loss on extinguishment of debt of $1.1 million, consisting of the redemption premium of $852 thousand and a write-off of the remaining unamortized issuance costs of $231 thousand, which reduced 2011 diluted earnings per common share by $0.05.

**2011 Performance Summary**

Our net income was $22.8 million for the year ended December 31, 2011, compared to a net income of $21.3 million for the year ended December 31, 2010. For 2011, net income available to common shareholders was $19.6 million, or $1.49 per diluted common share. Net income available to common shareholders was $17.6 million for 2010, or $1.61 per diluted common share. Cash dividends of $0.47 and $0.40 per common share were declared in 2011 and 2010, respectively.

We had total assets of $2.336 billion at December 31, 2011 compared to $2.214 billion at December 31, 2010. At December 31, 2011, shareholders' equity totaled $237.2 million with book value per common share at $15.92, compared to $212.1 million with book value per common share at $14.48 at the end of 2010. Tangible common equity to tangible common assets improved to 7.58% during 2011 from 5.65% in 2010. The Tier 1 capital ratio was 12.20% as of December 31, 2011 compared to 12.34% at December 31, 2010.

Key factors behind these results are discussed below.

- At December 31, 2011, loans were $1.485 billion, up 10% from year-end 2010, primarily in commercial and consumer indirect loans, as we have focused our business development efforts in these areas in accordance with our strategic objectives. Total deposits at December 31, 2011, were $1.932 billion, up 3% from year-end 2010, primarily attributable to a $40.7 million increase in retail deposits. Our deposit mix remains favorably weighted in lower cost demand, savings and money market accounts, which comprised 64% of total deposits at the end of 2011.

- Nonperforming loans were $7.1 million at December 31, 2011, compared to $7.6 million at December 31, 2010, as our loan portfolio continues to benefit from responsible underwriting and lending practices.

- The provision for loan losses was $7.8 million and $6.7 million, respectively, for 2011 and 2010. Net charge-offs were $5.0 million in 2011 (or 0.36% of average loans) compared to $7.0 million in 2010 (or 0.54% of average loans).

- At year-end 2011, the allowance for loan losses of $23.3 million represented 1.57% of total loans (covering 329% of non-performing loans), compared to $20.5 million or 1.52% (covering 270% of non-performing loans) at year-end 2010.

- Taxable equivalent net interest income was $83.9 million for 2011 or 4% higher than $80.7 million in 2010. Taxable equivalent interest income decreased $1.2 million, while interest expense decreased by $4.5 million. The increase in taxable equivalent net interest income was a function of a favorable volume variance (increasing taxable equivalent net interest income by $7.8 million), partially offset by an unfavorable rate variance (decreasing taxable equivalent net interest income by $4.5 million).

- The net interest margin for 2011 was 4.04%, 3 basis points lower than 4.07% in 2010.

- Noninterest income was $23.9 million for 2011 compared to $19.5 million for 2010. Core fee-based revenues (defined as service charges on deposit accounts, ATM and debit fees, and broker-dealer fees and commissions) totaled $14.9 million, unchanged from 2010. Net mortgage banking income was $1.7 million for 2011, a slight decrease from $1.8 million in 2010.

- Net investment securities gains (defined as net gain on sales and calls of investment securities and impairment charges on investment securities) were $3.0 million for 2011, compared to net investment securities losses of $425 thousand for 2010. During 2011 we recognized an additional $2.8 million in gains from the sale of investment securities and $576 thousand less in impairment charges than in 2010. The increase was primarily attributable to the net gain we experienced in 2011 in sales and calls of investment securities that included a gain of $2.3 million achieved on the sale of four pooled trust preferred securities that had previously been written down.

- Noninterest expense for 2011 was $63.8 million, an increase of $2.9 million or 5% over 2010. Salaries and employee benefits increased $2.6 million, professional services increased by $420 thousand and we recognized a loss on extinguishment of debt of $1.1 million as a result of redeeming our 10.20% junior subordinated debentures. FDIC assessments decreased by $1.0 million and other noninterest expense decreased by $404 thousand. As previously disclosed, other noninterest expense for 2010 includes $1.0 million of losses relating to irregular instances of fraudulent debit card activity.

- The efficiency ratio was 60.55% for 2011 and 60.36% for 2010.

- Income tax expense for 2011 was $11.4 million compared to $9.4 million for 2010. The change in income tax expense was primarily due to a $3.6 million increase in pretax income between the years.

***RESULTS OF OPERATIONS FOR THE YEARS ENDED DECEMBER 31, 2011 AND DECEMBER 31, 2010***

**Net Interest Income and Net Interest Margin**

Net interest income is the primary source of our revenue. Net interest income is the difference between interest income on interest-earning assets, such as loans and investment securities, and the interest expense on interest-bearing deposits and other borrowings used to fund interest-earning and other assets or activities. Net interest income is affected by changes in interest rates and by the amount and composition of earning assets and interest-bearing liabilities, as well as the sensitivity of the balance sheet to changes in interest rates, including characteristics such as the fixed or variable nature of the financial instruments, contractual maturities and repricing frequencies.

Interest rate spread and net interest margin are utilized to measure and explain changes in net interest income. Interest rate spread is the difference between the yield on earning assets and the rate paid for interest-bearing liabilities that fund those assets. The net interest margin is expressed as the percentage of net interest income to average earning assets. The net interest margin exceeds the interest rate spread because noninterest-bearing sources of funds ("net free funds"), principally noninterest-bearing demand deposits and stockholders' equity, also support earning assets. To compare tax-exempt asset yields to taxable yields, the yield on tax-exempt investment securities is computed on a taxable equivalent basis. Net interest income, interest rate spread, and net interest margin are discussed on a taxable equivalent basis.

The following table reconciles interest income per the consolidated statements of income to interest income adjusted to a fully taxable equivalent basis for the years ended December 31 (in thousands):

| | 2011 | 2010 | 2009 |
|---|---|---|---|
| Interest income per consolidated statements of income | $ 95,118 | $ 96,509 | $ 94,482 |
| Adjustment to fully taxable equivalent basis | 2,062 | 1,895 | 2,692 |
| Interest income adjusted to a fully taxable equivalent basis | 97,180 | 98,404 | 97,174 |
| Interest expense per consolidated statement of income | 13,255 | 17,720 | 22,217 |
| Net interest income on a taxable equivalent basis | $ 83,925 | $ 80,684 | $ 74,957 |

Taxable equivalent net interest income of $83.9 million for 2011 was $3.2 million or 4% higher than 2010. The impact of a decline in average yields on our assets was diminished by a 5% increase in interest-earning assets. The average balance of loans rose $98.4 million or 8% to $1.394 billion, reflecting growth in the commercial and consumer indirect loan portfolios, and the average balance of interest-earning assets rose $98.6 million to $2.080 billion. Consistent with our strategic plan, we continue to pursue loan development efforts in the commercial and consumer indirect lending portfolios in accordance with prudent underwriting standards.

The increase in taxable equivalent net interest income was a function of a favorable volume variance (as balance sheet changes in both volume and mix increased taxable equivalent net interest income by $7.8 million), partially offset by an unfavorable rate variance (decreasing taxable equivalent net interest income by $4.5 million). The change in mix and volume of earning assets increased taxable equivalent interest income by $6.3 million, while the change in volume and composition of interest-bearing liabilities decreased interest expense by $1.5 million, for a net favorable volume impact of $7.8 million on taxable equivalent net interest income. Rate changes on earning assets reduced interest income by $7.4 million, while changes in rates on interest-bearing liabilities lowered interest expense by $2.9 million, for a net unfavorable rate impact of $4.5 million.

The net interest margin for 2011 was 4.04% compared to 4.07% in 2010.

The slight decrease in net interest margin was attributable to a 3 basis point lower contribution from net free funds (primarily attributable to lower rates on interest-bearing liabilities reducing the value of noninterest-bearing deposits and other net free funds). The interest rate spread remained unchanged from the year ended December 31, 2010 at 3.87%, as a 30 basis point decrease in the yield on earning assets offset the 30 basis point decrease in the cost of interest-bearing liabilities.

The Federal Reserve left the Federal funds rate unchanged at 0.25% during 2011 and 2010. During 2011, the Federal Reserve disclosed that short-term interest rates would be held near zero through at least the middle of 2013, in anticipation of low growth and little risk of inflation. In January 2012, the Federal Reserve further announced that it is unlikely that the short-term interest rates will increase until at least 2014.

For 2011, the yield on average earning assets of 4.67% was 30 basis points lower than 2010. Loan yields decreased 33 basis points to 5.53%. Commercial mortgage and consumer indirect loans in particular, down 31 and 66 basis points, respectively, continued to experience lower yields given the competitive pricing pressures and re-pricing of loans in a low interest rate environment. The yield on investment securities dropped 38 basis points to 2.93%, also impacted by the lower interest rate environment and prepayments of mortgage-related investment securities. Overall, earning asset rate changes reduced interest income by $7.5 million.

The cost of average interest-bearing liabilities of 0.80% in 2011 was 30 basis points lower than 2010. The average cost of interest-bearing deposits was 0.74% in 2011, 23 basis points lower than 2010, reflecting the low-rate environment, mitigated by a focus on product pricing to retain balances. The cost of borrowings decreased 175 basis points to 1.58% for 2011, primarily a result of the redemption of the 10.20% junior subordinated debentures. The interest-bearing liability rate changes reduced interest expense by $2.9 million.

Average interest-earning assets of $2.080 billion in 2011 were $98.6 million or 5% higher than 2010. Average investment securities increased $5.0 million while average loans increased $98.4 million or 8%. Commercial loans increased $42.1 million and consumer loans increased $73.5 million, offset by a $17.2 million decrease in residential mortgage loans.

Average interest-bearing liabilities of $1.662 billion in 2011 were up $51.6 million or 3% versus 2010. The impacts of the recent recession have positively impacted our deposit balances, as consumers tend to save more when consumer confidence is low. On average, interest-bearing deposits grew $22.8 million, while average noninterest-bearing demand deposits (a principal component of net free funds) increased by $38.4 million. Average borrowings increased $28.9 million, representing a $50.0 million increase and $21.1 million decrease in short-term and long-term borrowings, respectively.

The following tables present, for the periods indicated, information regarding: (i) the average balance sheet; (ii) the amount of interest income from interest-earning assets and the resulting annualized yields (tax-exempt yields have been adjusted to a tax-equivalent basis using the applicable Federal tax rate in each year); (iii) the amount of interest expense on interest-bearing liabilities and the resulting annualized rates; (iv) net interest income; (v) net interest rate spread; (vi) net interest income as a percentage of average interest-earning assets ("net interest margin"); and (vii) the ratio of average interest-earning assets to average interest-bearing liabilities. Investment securities are at amortized cost for both held to maturity and available for sale securities. Loans include net unearned income, net deferred loan fees and costs and non-accruing loans. Dollar amounts are shown in thousands.

| | Years ended December 31, | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2011 | | | 2010 | | | 2009 | | |
| | Average Balance | Interest | Average Rate | Average Balance | Interest | Average Rate | Average Balance | Interest | Average Rate |
| **Interest-earning assets:** | | | | | | | | | |
| Federal funds sold and other interest-earning deposits | $ 140 | $ — | 0.20% | $ 5,034 | $ 10 | 0.21% | $ 37,214 | $ 82 | 0.22% |
| Investment securities: | | | | | | | | | |
| Taxable | 545,112 | 14,185 | 2.60 | 571,856 | 17,101 | 2.99 | 454,552 | 16,466 | 3.62 |
| Tax-exempt | 140,657 | 5,890 | 4.19 | 108,900 | 5,416 | 4.97 | 155,054 | 7,920 | 5.11 |
| Total investment securities | 685,769 | 20,075 | 2.93 | 680,756 | 22,517 | 3.31 | 609,606 | 24,386 | 4.00 |
| Loans: | | | | | | | | | |
| Commercial business | 215,598 | 10,311 | 4.78 | 206,167 | 9,939 | 4.82 | 204,235 | 9,612 | 4.71 |
| Commercial mortgage | 370,843 | 21,216 | 5.72 | 338,149 | 20,389 | 6.03 | 306,763 | 19,309 | 6.29 |
| Residential mortgage | 121,742 | 6,868 | 5.64 | 138,954 | 8,157 | 5.87 | 161,055 | 9,701 | 6.02 |
| Home equity | 216,428 | 9,572 | 4.42 | 202,189 | 9,224 | 4.56 | 193,929 | 9,121 | 4.70 |
| Consumer indirect | 444,527 | 26,549 | 5.97 | 382,977 | 25,379 | 6.63 | 313,239 | 21,838 | 6.97 |
| Other consumer | 24,686 | 2,589 | 10.49 | 26,950 | 2,789 | 10.35 | 30,791 | 3,125 | 10.15 |
| Total loans | 1,393,824 | 77,105 | 5.53 | 1,295,386 | 75,877 | 5.86 | 1,210,012 | 72,706 | 6.01 |
| Total interest-earning assets | 2,079,733 | 97,180 | 4.67 | 1,981,176 | 98,404 | 4.97 | 1,856,832 | 97,174 | 5.23 |
| Less: Allowance for loan losses | 21,567 | | | 20,883 | | | 20,355 | | |
| Other noninterest-earning assets | 218,983 | | | 206,303 | | | 197,439 | | |
| Total assets | $2,277,149 | | | $2,166,596 | | | $2,033,916 | | |
| **Interest-bearing liabilities:** | | | | | | | | | |
| Deposits: | | | | | | | | | |
| Interest-bearing demand | $ 383,122 | 614 | 0.16 | $ 382,517 | 705 | 0.18 | $ 365,873 | 772 | 0.21 |
| Savings and money market | 451,030 | 1,056 | 0.23 | 414,953 | 1,133 | 0.27 | 383,697 | 1,090 | 0.28 |
| Certificates of deposit | 712,411 | 9,764 | 1.37 | 726,330 | 13,015 | 1.79 | 685,259 | 17,228 | 2.51 |
| Total interest-bearing deposits | 1,546,563 | 11,434 | 0.74 | 1,523,800 | 14,853 | 0.97 | 1,434,829 | 19,090 | 1.33 |
| Short-term borrowings | 99,122 | 500 | 0.50 | 49,104 | 365 | 0.74 | 43,092 | 270 | 0.63 |
| Long-term borrowings | 15,905 | 1,321 | 8.31 | 37,043 | 2,502 | 6.75 | 46,913 | 2,857 | 6.09 |
| Total borrowings | 115,027 | 1,821 | 1.58 | 86,147 | 2,867 | 3.33 | 90,005 | 3,127 | 3.47 |
| Total interest-bearing liabilities | 1,661,590 | 13,255 | 0.80 | 1,609,947 | 17,720 | 1.10 | 1,524,834 | 22,217 | 1.46 |
| Noninterest-bearing deposits | 368,268 | | | 329,853 | | | 293,852 | | |
| Other liabilities | 15,041 | | | 15,485 | | | 20,890 | | |
| Shareholders' equity | 232,250 | | | 211,311 | | | 194,340 | | |
| Total liabilities and shareholders' equity | $2,277,149 | | | $2,166,596 | | | $2,033,916 | | |
| Net interest income (tax-equivalent) | | $ 83,925 | | | $ 80,684 | | | $ 74,957 | |
| Interest rate spread | | | 3.87% | | | 3.87% | | | 3.77% |
| Net earning assets | $ 418,143 | | | $ 371,229 | | | $ 331,998 | | |
| Net interest margin (tax-equivalent) | | | 4.04% | | | 4.07% | | | 4.04% |
| Ratio of average interest-earning assets to average interest-bearing liabilities | 125.17% | | | 123.06% | | | 121.77% | | |

**Rate /Volume Analysis**

The following table presents, on a tax-equivalent basis, the relative contribution of changes in volumes and changes in rates to changes in net interest income for the periods indicated. The change in interest not solely due to changes in volume or rate has been allocated in proportion to the absolute dollar amounts of the change in each (in thousands):

| | Change from 2011 to 2010 | | | Change from 2010 to 2009 | | |
|---|---|---|---|---|---|---|
| | Volume | Rate | Total | Volume | Rate | Total |
| **Increase (decrease) in:** | | | | | | |
| **Interest income:** | | | | | | |
| Federal funds sold and other interest-earning deposits | $ (5) | $ (5) | $ (10) | $ (65) | $ (7) | $ (72) |
| Investment securities: | | | | | | |
| Taxable | (772) | (2,144) | (2,916) | 3,807 | (3,172) | 635 |
| Tax-exempt | 1,418 | (944) | 474 | (2,300) | (204) | (2,504) |
| Total investment securities | 646 | (3,088) | (2,442) | 1,507 | (3,376) | (1,869) |
| Loans: | | | | | | |
| Commercial business | 452 | (80) | 372 | 92 | 235 | 327 |
| Commercial mortgage | 1,905 | (1,078) | 827 | 1,916 | (836) | 1,080 |
| Residential mortgage | (980) | (309) | (1,289) | (1,302) | (242) | (1,544) |
| Home equity | 636 | (288) | 348 | 382 | (279) | 103 |
| Consumer indirect | 3,829 | (2,659) | 1,170 | 4,665 | (1,124) | 3,541 |
| Other consumer | (237) | 37 | (200) | (396) | 60 | (336) |
| Total loans | 5,605 | (4,377) | 1,228 | 5,357 | (2,186) | 3,171 |
| **Total interest income** | **6,246** | **(7,470)** | **(1,224)** | **6,799** | **(5,569)** | **1,230** |
| **Interest expense:** | | | | | | |
| Deposits: | | | | | | |
| Interest-bearing demand | 1 | (92) | (91) | 34 | (101) | (67) |
| Savings and money market | 93 | (170) | (77) | 86 | (43) | 43 |
| Certificates of deposit | (245) | (3,006) | (3,251) | 982 | (5,195) | (4,213) |
| Total interest-bearing deposits | (151) | (3,268) | (3,419) | 1,102 | (5,339) | (4,237) |
| Short-term borrowings | 281 | (146) | 135 | 41 | 54 | 95 |
| Long-term borrowings | (1,662) | 481 | (1,181) | (644) | 289 | (355) |
| Total borrowings | (1,381) | 335 | (1,046) | (603) | 343 | (260) |
| **Total interest expense** | **(1,532)** | **(2,933)** | **(4,465)** | **499** | **(4,996)** | **(4,497)** |
| **Net interest income** | **$ 7,778** | **$ (4,537)** | **$ 3,241** | **$ 6,300** | **$ (573)** | **$ 5,727** |

**Provision for Loan Losses**

The provision for loan losses is based upon credit loss experience, growth or contraction of specific segments of the loan portfolio, and the estimate of losses inherent in the current loan portfolio. The provision for loan losses was $7.8 million for the year ended December 31, 2011 compared with $6.7 million for 2010. See the "Allowance for Loan Losses" section of this Management's Discussion and Analysis for further discussion.

**Noninterest Income**

The following table summarizes our noninterest income for the years ended December 31 (in thousands):

| | 2011 | 2010 | 2009 |
|---|---|---|---|
| Service charges on deposits | $ 8,679 | $ 9,585 | $ 10,065 |
| ATM and debit card | 4,359 | 3,995 | 3,610 |
| Broker-dealer fees and commissions | 1,829 | 1,283 | 1,022 |
| Company owned life insurance | 1,424 | 1,107 | 1,096 |
| Loan servicing | 835 | 1,124 | 1,308 |
| Net gain on sale of loans held for sale | 880 | 650 | 699 |
| Net gain on sales and calls of investment securities | 3,003 | 169 | 3,429 |
| Impairment charges on investment securities | (18) | (594) | (4,666) |
| Net gain (loss) on sale and disposal of other assets | 67 | (203) | 180 |
| Other | 2,867 | 2,338 | 2,052 |
| Total noninterest income | $ 23,925 | $ 19,454 | $ 18,795 |

The components of noninterest income fluctuated as discussed below.

Service charges on deposits were $8.7 million in 2011, which was $906 thousand or 9% lower than 2010. The decrease was primarily due to changes in customer behavior and recent regulatory changes that include requirements for customers to opt in for overdraft coverage for certain types of electronic banking activities.

ATM and debit card income was $4.4 million for 2011, an increase of $364 thousand or 9%, compared to 2010. The increased popularity of electronic banking and transaction processing has resulted in higher ATM and debit card point-of-sale usage income.

Broker-dealer fees and commissions were up $546 thousand or 43%, compared to 2010. Broker-dealer fees and commissions fluctuate mainly due to sales volume, which increased during 2011 as a result of improving market and economic conditions and our renewed focus on this line of business.

Company owned life insurance income was up $317 thousand or 29% for the year ended December 31, 2011 compared to the same period in 2010. The increase was the result of an additional $18.0 million investment in company owned life insurance during the third quarter of 2011.

Loan servicing income represents fees earned for servicing mortgage and indirect auto loans sold to third parties, net of amortization expense and impairment losses, if any, associated with capitalized loan servicing assets. Loan servicing income was down $289 thousand or 26% the year ended December 31, 2011 compared to 2010. Loan servicing income decreased as a result of more rapid amortization of servicing rights due to loans paying off, lower fees collected due to a decrease in the sold and serviced portfolio and write-downs on capitalized mortgage servicing assets.

Net gain on loans held for sale was $880 thousand in 2011, an increase of $230 thousand or 35%, compared to 2010, mainly due to the $153 thousand gain relating to the servicing retained sale of $13.0 million of indirect auto loans during the third quarter of 2011.

Net gains from the sales of investment securities were $3.0 million for the year ended December 31, 2011, compared to $169 thousand in 2010. The current year includes net gains of $2.3 million from the sale of four pooled trust-preferred securities that had been written down in prior periods and included in non-performing assets. We continue to monitor the market for the trust-preferred securities and evaluate the potential for future dispositions. Net gains of $730 thousand from the sale of eight mortgage-backed securities were also recognized during 2011. The amount and timing of our sale of investments securities is dependent on a number of factors, including our prudent efforts to realize gains while managing duration, premium and credit risk.

Other noninterest income increased $529 thousand or 23% for the year ended December 31, 2011, compared to 2010. Other noninterest income for 2011 includes $152 thousand related to insurance proceeds received for losses relating to an irregular instance of fraudulent debit card activity recorded in the fourth quarter of 2010. Merchant services fees paid by customers for account management and electronic processing of transactions and income from our capital investment in several limited partnerships also contributed to the 2011 increases.

**Noninterest Expense**

The following table summarizes our noninterest expense for the years ended December 31 (in thousands):

| | 2011 | 2010 | 2009 |
|---|---|---|---|
| Salaries and employee benefits | $ 35,439 | $ 32,811 | $ 33,634 |
| Occupancy and equipment | 10,868 | 10,818 | 11,062 |
| Computer and data processing | 2,437 | 2,487 | 2,340 |
| Professional services | 2,617 | 2,197 | 2,524 |
| Supplies and postage | 1,778 | 1,772 | 1,846 |
| FDIC assessments | 1,513 | 2,507 | 3,651 |
| Advertising and promotions | 1,259 | 1,121 | 949 |
| Loss on extinguishment of debt | 1,083 | — | — |
| Other | 6,800 | 7,204 | 6,771 |
| Total noninterest expense | $ 63,794 | $ 60,917 | $ 62,777 |

The components of noninterest expense fluctuated as discussed below.

Salaries and employee benefits (which includes salary-related expenses and fringe benefit expenses) was $35.4 million for 2011, up $2.6 million or 8% from 2010. Average full-time equivalent employees (“FTEs”) were 576 for 2011, about the same as 577 for last year. Salary-related expenses increased $2.0 million for the year ended December 31, 2011, compared to 2010, reflecting an increase in estimated incentive compensation, which was previously limited under the TARP Capital Purchase Program. Fringe benefit expenses increased $672 thousand or 9%, primarily attributable to higher medical expenses.

Professional services expense of $2.6 million in 2011 increased $420 thousand or 19% from 2010. Professional fees increased primarily due to legal and shareholder expenses related to our common stock offering and redemption of both our Series A preferred stock and junior subordinated debentures.

FDIC assessments decreased $1.0 million for the year ended December 31, 2011, compared to 2010, primarily a result of changes implemented by the FDIC in the method of calculating assessment rates which became effective in the second quarter of 2011.

Advertising and promotions expenses were $138 thousand or 12% higher in 2011 compared to 2010 due to increases in business development expenses and the opening of a new branch in suburban Rochester in the third quarter of 2011.

We redeemed all of the 10.20% junior subordinated debentures during 2011. As a result of the redemption, we recognized a loss on extinguishment of debt of $1.1 million, consisting of a redemption premium of $852 thousand and a write-off of the remaining unamortized issuance costs of $231 thousand.

Other noninterest expense decreased $404 thousand or 6% during 2011 compared to 2010. The 2010 expense includes a loss of approximately $1.0 million relating to irregular instances of fraudulent debit card activity.

The efficiency ratio for the year ended December 31, 2011 was 60.55% compared with 60.36% for 2010. The efficiency ratio is a supplemental financial measure utilized in management’s internal evaluations and is not defined under generally accepted accounting principles. The efficiency ratio is calculated by dividing total noninterest expense, excluding other real estate expense, by net revenue, defined as the sum of tax-equivalent net interest income and noninterest income before net gains and impairment charges on investment securities. Taxes are not part of this calculation. An increase in the efficiency ratio indicates that more resources are being utilized to generate the same volume of income, while a decrease would indicate a more efficient allocation of resources.

**Income Taxes**

We recognized income tax expense of $11.4 million for 2011 compared to $9.4 million for 2010. The change was due in part to a $3.6 million increase in pretax income between the years. In addition, during 2010, we recorded non-recurring tax benefits of $1.2 million related to valuation of our deferred tax assets as a result of the NYS repeal of the experience method for determining bad debts and re-valuing at the highest Federal statutory rate of 35%. Our effective tax rates were 33.4% in 2011 and 30.5% in 2010. Effective tax rates are affected by income and expense items that are not subject to Federal or state taxation. Our income tax provision reflects the impact of such items, including tax-exempt interest income from municipal securities, tax-exempt earnings on bank-owned life insurance and the effect of certain state tax credits.

## *RESULTS OF OPERATIONS FOR THE YEARS ENDED DECEMBER 31, 2010 AND DECEMBER 31, 2009*

### Net Interest Income and Net Interest Margin

Net interest income in the consolidated statements of income (which excludes the taxable equivalent adjustment) was $78.8 million in 2010, compared to $72.3 million in 2009. The taxable equivalent adjustments (the adjustments to bring tax-exempt interest to a level that would yield the same after-tax income had that income been subject to a taxation using a tax rate of 35% for 2010 and 34% for 2009) of $1.9 million and $2.7 million for 2010 and 2009, respectively, resulted in fully taxable equivalent net interest income of $80.7 million in 2010 and $75.0 million in 2009.

Taxable equivalent net interest income of $80.7 million for 2010 was $5.7 million or 8% higher than 2009. While the average yields on our loans and assets declined, the impact was far exceeded by the benefit of substantial loan production and asset growth. The average balance of loans rose $85.4 million to $1.295 billion, reflecting growth in the commercial and consumer indirect loan portfolios, as we have focused business development efforts in those areas, and the average balance of interest-earning assets rose $124.3 million to $1.981 billion, both increases of 7%.

The increase in taxable equivalent net interest income was a function of a favorable volume variance (because balance sheet changes in both volume and mix increased taxable equivalent net interest income by $6.3 million), partially offset by an unfavorable rate variance (decreasing taxable equivalent net interest income by $573 thousand). The change in mix and volume of earning assets increased taxable equivalent interest income by $6.8 million, while the change in volume and composition of interest-bearing liabilities increased interest expense by $499 thousand, for a net favorable volume impact of $6.3 million on taxable equivalent net interest income. Rate changes on earning assets reduced interest income by $5.6 million, while changes in rates on interest-bearing liabilities lowered interest expense by $5.0 million, for a net unfavorable rate impact of $573 thousand.

The net interest margin for 2010 was 4.07% compared to 4.04% in 2009. The 3 basis point improvement in net interest margin was attributable to a 10 basis point increase in interest rate spread (the net of a 36 basis point decrease in the cost of interest-bearing liabilities and a 26 basis decrease in the yield on earning assets), partially offset by a 7 basis point lower contribution from net free funds (primarily attributable to lower rates on interest-bearing liabilities reducing the relative value of noninterest-bearing deposits and other net free funds).

The Federal Reserve left the Federal funds rate unchanged at 0.25% during 2010 and 2009.

For 2010, the yield on average earning assets of 4.97% was 26 basis points lower than 2009. Loan yields decreased 15 basis points to 5.86%. Commercial mortgage and consumer indirect loans in particular, down 26 and 34 basis points, respectively, experienced lower yields given the competitive pricing pressures in a low interest rate environment. The yield on investment securities dropped 69 basis points to 3.31%, also impacted by the lower interest rate environment and prepayments of mortgage-related investment securities. Overall, earning asset rate changes reduced interest income by $5.6 million.

The cost of average interest-bearing liabilities of 1.10% in 2010 was 36 basis points lower than 2009. The average cost of interest-bearing deposits was 0.97% in 2010, 36 basis points lower than 2009, reflecting the lower rate environment, mitigated by a focus on product pricing to retain balances. The cost of wholesale funding (comprised of short-term borrowings and long-term borrowings) decreased 14 basis points to 3.33% for 2010. The interest-bearing liability rate changes resulted in $5.0 million lower interest expense.

Average interest-earning assets of $1.981 billion in 2010 were $124.3 million or 7% higher than 2009. Average investment securities increased $71.2 million, mostly in high quality U.S. Government agency securities. Average loans increased $85.4 million or 7%, with a $33.3 million increase in commercial loans and a $74.2 million increase in consumer loans, offset by a $22.1 million decrease in residential mortgage loans.

Average interest-bearing liabilities of $1.610 billion in 2010 were up $85.1 million or 6% versus 2009, mainly attributable to higher average retail deposit balances. The impacts of the recent recession have had a positive impact on our deposit balances, as consumers tend to save more conservatively when consumer confidence is low. On average, interest-bearing deposits grew $89.0 million, while average noninterest-bearing demand deposits (a principal component of net free funds) increased by $36.0 million. Average borrowings decreased $3.9 million, net of the $6.0 million increase and $9.9 million decrease in short-term and long-term borrowings, respectively.

### Provision for Loan Losses

The provision for loan losses was $6.7 million for the year ended December 31, 2010 compared with $7.7 million for 2009.

**Noninterest Income**

Service charges on deposits were $9.6 million in 2010, which was $480 thousand or 5% lower than 2009. The decrease was primarily attributable to lower nonsufficient funds fees in 2010, which were down $407 thousand to $7.9 million. In November 2009, the FRB issued a final rule that, effective July 1, 2010, prohibited financial institutions from charging consumers fees for paying overdrafts on automated teller machine and one-time debit card transactions, unless a consumer consents, or opts in, to the overdraft service for those types of transactions, commonly referred to as "Reg.-E". Consumers must be provided a notice that explains the financial institution's overdraft services, including the fees associated with the service, and the consumer's choices.

ATM and debit card income was $4.0 million for 2010, an increase of $385 thousand or 11%, compared to 2009, due to higher interchange fees resulting from an increase in the number of cardholders and an increase in customer transactions.

Broker-dealer fees and commissions were up $261 thousand or 26%, compared to 2009. Broker-dealer fees and commissions fluctuate mainly due to sales volume, which increased during 2010 as a result of improving market and economic conditions.

Loan servicing income decreased $184 thousand for the year ended December 31, 2010 compared to 2009, mainly as a result of more rapid amortization of servicing rights due to loans paying off prior to maturity and lower fees collected due to a decrease in the sold and serviced portfolio.

We recognized $425 thousand in net losses on investment securities during the year ended December 31, 2010 as compared to $1.2 million of net losses during the same period in 2009. The investment security net losses for 2010 resulted from other-than-temporary impairment charges of $594 thousand, partly offset by $169 thousand of gains from sales and calls of investment securities. The 2010 OTTI charges primarily related to pooled trust preferred securities that were designated as impaired in the first quarter of that year due to credit quality. The $1.2 million of investment security losses for 2009 are a result of $4.7 million of other-than-temporary impairment charges, partly offset by $3.4 million of gains on the sale of securities.

**Noninterest Expense**

Salaries and employee benefits was $32.8 million for 2010, down $823 thousand or 2% from 2009. Average full-time equivalent employees ("FTEs") were 577 for 2010, down 2% from 586 for 2009. Salary-related expenses were relatively unchanged at $25.3 million for 2010 and $25.2 million for 2009. Fringe benefit expenses decreased $876 thousand or 10%, primarily attributable to lower pension costs.

FDIC assessments, comprised mostly of deposit insurance paid to the FDIC, decreased $1.1 million for the year ended December 31, 2010, due primarily to the one-time special assessment of $923 thousand incurred in the second quarter of 2009. FDIC assessment rates have also declined as a result of our improved financial ratios, upon which the assessment rate is based.

Professional services expense of $2.2 million in 2010 decreased $327 thousand or 13% from 2009, primarily due to lower legal costs associated with loan workouts and other corporate activities.

Advertising and promotions expenses were $172 thousand or 18% higher in 2010 compared to 2009 due to increases in business development expenses.

Other noninterest expense increased $433 thousand or 6% during 2010 compared to 2009. This increase was primarily due to a loss of approximately $1.0 million relating to irregular instances of fraudulent debit card activity that we recorded in the fourth quarter of 2010.

The efficiency ratio for the year ended December 31, 2010 improved to 60.36% compared with 65.52% for 2009.

**Income Taxes**

We recognized income tax expense of $9.4 million for 2010 compared to $6.1 million for 2009. The change in income tax expense was primarily due to a $10.1 million increase in pretax income between the years. We also recorded non-recurring tax benefits during 2010 of $1.2 million related to valuation of our deferred tax assets as a result of the NYS repeal of the experience method for determining bad debts and re-valuing at the highest Federal statutory rate of 35%. Our effective tax rates were 30.5% in 2010 and 29.8% in 2009.

*ANALYSIS OF FINANCIAL CONDITION*

**OVERVIEW**

At December 31, 2011, we had total assets of $2.336 billion, an increase of 6% from $2.214 billion as of December 31, 2010, primarily a result of the continued core business growth in both loans and deposits. Net loans were $1.462 billion as of December 31, 2011, up $136.0 million, or 10%, when compared to $1.326 billion as of December 31, 2010. The increase in net loans was primarily attributed to the continued expansion of the indirect lending program in existing and new markets and commercial business development efforts. Non-performing assets totaled $9.2 million as of December 31, 2011, up $292 thousand from a year ago. An increase in non-performing investment securities for which we have stopped accruing interest was partly offset by a decrease in non-performing loans and a decrease in foreclosed assets. Total deposits amounted to $1.932 billion and $1.883 billion as of December 31, 2011 and 2010, respectively. As of December 31, 2011, borrowed funds totaled $150.7 million, compared to $103.9 million as of December 31, 2010. Book value per common share was $15.92 and $14.48 as of December 31, 2011 and 2010, respectively. As of December 31, 2011 our total shareholders' equity was $237.2 million compared to $212.1 million a year earlier.

**INVESTING ACTIVITIES**

The following table summarizes the composition of the available for sale and held to maturity security portfolios (in thousands).

| | Investment Securities Portfolio Composition At December 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2011 | | 2010 | | 2009 | |
| | Amortized Cost | Fair Value | Amortized Cost | Fair Value | Amortized Cost | Fair Value |
| **Securities available for sale:** | | | | | | |
| U.S. Government agency and government-sponsored enterprise securities | $ 94,947 | $ 97,712 | $ 141,591 | $ 140,784 | $ 134,564 | $ 134,105 |
| State and political subdivisions | 119,099 | 124,424 | 105,622 | 105,666 | 80,812 | 83,659 |
| Mortgage-backed securities: | | | | | | |
| Agency mortgage-backed securities | 390,375 | 401,596 | 414,502 | 417,709 | 356,044 | 356,355 |
| Non-Agency mortgage-backed securities | 327 | 2,089 | 981 | 1,572 | 5,087 | 5,160 |
| Asset-backed securities | 297 | 1,697 | 564 | 637 | 1,295 | 1,222 |
| Total available for sale securities | 605,045 | 627,518 | 663,260 | 666,368 | 577,802 | 580,501 |
| **Securities held to maturity:** | | | | | | |
| State and political subdivisions | 23,297 | 23,964 | 28,162 | 28,849 | 39,573 | 40,629 |
| Total investment securities | $ 628,342 | $ 651,482 | $ 691,422 | $ 695,217 | $ 617,375 | $ 621,130 |

Our investment policy is contained within our overall Asset-Liability Management and Investment Policy. This policy dictates that investment decisions will be made based on the safety of the investment, liquidity requirements, potential returns, cash flow targets, need for collateral and desired risk parameters. In pursuing these objectives, we consider the ability of an investment to provide earnings consistent with factors of quality, maturity, marketability, pledgeable nature and risk diversification. Our Treasurer, guided by ALCO, is responsible for investment portfolio decisions within the established policies.

**Impairment Assessment**

We review investment securities on an ongoing basis for the presence of OTTI with formal reviews performed quarterly. Declines in the fair value of held-to-maturity and available-for-sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses to the extent the impairment is related to credit losses or the security is intended to be sold or will be required to be sold. The amount of the impairment related to non-credit related factors is recognized in other comprehensive income. Evaluating whether the impairment of a debt security is other than temporary involves assessing i.) the intent to sell the debt security or ii.) the likelihood of being required to sell the security before the recovery of its amortized cost basis. In determining whether the other-than-temporary impairment includes a credit loss, we use our best estimate of the present value of cash flows expected to be collected from the debt security considering factors such as: a.) the length of time and the extent to which the fair value has been less than the amortized cost basis, b.) adverse conditions specifically related to the security, an industry, or a geographic area, c.) the historical and implied volatility of the fair value of the security, d.) the payment structure of the debt security and the likelihood of the issuer being able to make payments that increase in the future, e.) failure of the issuer of the security to make scheduled interest or principal payments, f.) any changes to the rating of the security by a rating agency, and g.) recoveries or additional declines in fair value subsequent to the balance sheet date.

As of December 31, 2011, management does not have the intent to sell any of the securities in a loss position and believes that it is not likely that it will be required to sell any such securities before the anticipated recovery of amortized cost. The unrealized losses are largely due to increases in market interest rates over the yields available at the time the underlying securities were purchased. The fair value is expected to recover as the bonds approach their maturity date, repricing date or if market yields for such investments decline. Management does not believe any of the securities in a loss position are impaired due to reasons of credit quality. Accordingly, as of December 31, 2011, management has concluded that unrealized losses on its investment securities are temporary and no further impairment loss has been realized in our consolidated statements of income. The following discussion provides further details of our assessment of the securities portfolio by investment category.

The table below summarizes unrealized losses in each category of the securities portfolio at the end of the periods indicated (in thousands).

| | Unrealized Losses on Investment Securities At December 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2011 | | 2010 | | 2009 | |
| | Unrealized Losses | % of Total | Unrealized Losses | % of Total | Unrealized Losses | % of Total |
| **Securities available for sale:** | | | | | | |
| U.S. Government agency and government-sponsored enterprise securities | $ 5 | 11.9% | $ 1,965 | 31.6% | $ 545 | 19.8% |
| State and political subdivisions | 11 | 26.2 | 1,472 | 23.6 | 3 | 0.1 |
| Mortgage-backed securities: | | | | | | |
| Agency mortgage-backed securities | 26 | 61.9 | 2,655 | 42.7 | 1,638 | 59.3 |
| Non-Agency mortgage-backed securities | — | — | — | — | 330 | 12.0 |
| Asset-backed securities | — | — | 131 | 2.1 | 244 | 8.8 |
| Total investment securities | $ 42 | 100.0% | $ 6,223 | 100.0% | $ 2,760 | 100.0% |

There were no unrealized losses on investment securities classified as held to maturity as of December 31, 2011, 2010 and 2009.

**U.S. Government Agencies and Government Sponsored Enterprises ("GSE").** As of December 31, 2011, there were five securities in the U.S. Government agencies and GSE portfolio with unrealized losses totaling $5 thousand. Of these, four were in an unrealized loss position for 12 months or longer and had an aggregate amortized cost of $5.3 million and unrealized losses of $4 thousand. The decline in fair value is attributable to changes in interest rates, and not credit quality, and because we do not have the intent to sell these securities and it is likely that we will not be required to sell the securities before their anticipated recovery, we do not consider these securities to be other-than-temporarily impaired at December 31, 2011.

**State and Political Subdivisions.** As of December 31, 2011, the state and political subdivisions ("municipals") portfolio totaled $147.7 million, of which $124.4 million was classified as available for sale. As of that date, $23.3 million was classified as held to maturity with a fair value of $24.0 million. As of December 31, 2011, there were three municipals in an unrealized loss position, all of which were available for sale. Of these, one was in an unrealized loss position for 12 months or longer, and had an aggregate amortized cost of $655 thousand and an unrealized loss of $9 thousand.

Although there has been a considerable amount of negative information regarding municipal entities in certain states in the U.S., our portfolio is concentrated in municipalities within our geographic footprint and there is currently no indication that the underlying credit issuers (counties, towns, villages, cities, schools, etc.) are likely to default on their debt. Additionally, most of the available for sale bonds are General Obligation issues that require the taxing authority to increase taxes as needed to repay the bond holders.

Because the decline in fair value is attributable to changes in interest rates, and not credit quality, and because we do not have the intent to sell these securities and it is not likely that we will be required to sell the securities before their anticipated recovery, we do not consider these securities to be other-than-temporarily impaired at December 31, 2011.

**Agency Mortgage-backed Securities.** With the exception of the non-Agency mortgage-backed securities ("non-Agency MBS") discussed below, all of the mortgage-backed securities held by us as of December 31, 2011, were issued by U.S. Government sponsored entities and agencies ("Agency MBS"), primarily GNMA. The contractual cash flows of our Agency MBS are guaranteed by FNMA, FHLMC or GNMA. The GNMA mortgage-backed securities are backed by the full faith and credit of the U.S. Government.

As of December 31, 2011, there were six securities in the U.S. Government agencies and GSE portfolio that were in an unrealized loss position. Of these, only four were in an unrealized loss position for 12 months or longer and had an aggregate amortized cost of $2.2 million and unrealized losses of $8 thousand. Given the high credit quality inherent in Agency MBS, we do not consider any of the unrealized losses as of December 31, 2011, on such MBS to be credit related or other-than-temporary. As of December 31, 2011, we did not intend to sell any of Agency MBS that were in an unrealized loss position, all of which were performing in accordance with their terms.

**Non-Agency Mortgage-backed Securities.** Our non-Agency MBS portfolio consists of positions in three privately issued whole loan collateralized mortgage obligations with a fair value of $2.1 million and net unrealized gains of $1.8 million as of December 31, 2011. As of that date, each of the three non-Agency MBS were rated below investment grade. None of these securities were in an unrealized loss position. During the fourth quarter of 2011 we recognized an OTTI charge of $18 thousand against one of the non-Agency MBS.

**Asset-backed Securities ("ABS").** As of December 31, 2011, the fair value of the ABS portfolio totaled $1.7 million and consisted of positions in eleven securities, the majority of which are pooled trust preferred securities ("TPS") issued primarily by financial institutions and, to a lesser extent, insurance companies located throughout the United States. As a result of some issuers defaulting and others electing to defer interest payments, we considered the TPS to be non-performing and stopped accruing interest on the investments during 2009.

Since the second quarter of 2008, we have written down each of the securities in the ABS portfolio, resulting in aggregate OTTI charges of $22.5 million through December 31, 2011. We expect to recover the remaining amortized cost of $297 thousand on the securities. As of December 31, 2011, each of the securities in the ABS portfolio was rated below investment grade. None of these securities were in an unrealized loss position.

The market for these securities began to improve during the second quarter of 2011, resulting in substantial increases to their fair value since the beginning of the year. During that time, there were no additions to the portfolio as the increase relates solely to an increase in the fair value of the securities in the portfolio. During 2011, we recognized gains totaling $2.3 million from the sale of four ABS securities. The four securities had a fair value of $251 thousand at December 31, 2010. We continue to monitor the market for these securities and evaluate the potential for future dispositions.

**Other Investments.** As a member of the FHLB the Bank is required to hold FHLB stock. The amount of required FHLB stock is based on the Bank's asset size and the amount of borrowings from the FHLB. We have assessed the ultimate recoverability of our FHLB stock and believe that no impairment currently exists. As a member of the FRB system, we are required to maintain a specified investment in FRB stock based on a ratio relative to our capital. At December 31, 2011, our ownership of FHLB and FRB stock totaled $6.8 million and $3.9 million, respectively and is included in other assets and recorded at cost.

## LENDING ACTIVITIES

Total loans were $1.485 billion at December 31, 2011, an increase of $138.8 million or 10% from December 31, 2010. Commercial loans increased $63.1 million or 11% and represented 42.2% of total loans at the end of 2011. Residential mortgage loans were $113.9 million, down $15.7 million or 12% and represented 7.7% of total loans compared to 9.6% at December 31, 2010 while consumer loans increased $91.3 million to represent 50.1% of total loans at December 31, 2011 and 48.5% at December 31, 2010. The composition of our loan portfolio, excluding loans held for sale and including net unearned income and net deferred fees and costs, is summarized as follows (in thousands):

| | Loan Portfolio Composition At December 31, | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | 2011 | | 2010 | | 2009 | | 2008 | | 2007 | |
| | Amount | Percent | Amount | Percent | Amount | Percent | Amount | Percent | Amount | Percent |
| Commercial business | $ 233,836 | 15.7% | $ 211,031 | 15.7% | $ 206,383 | 16.3% | $ 180,100 | 16.1% | $ 157,550 | 16.3% |
| Commercial mortgage | 393,244 | 26.5 | 352,930 | 26.2 | 330,748 | 26.2 | 285,383 | 25.5 | 272,394 | 28.3 |
| Total commercial | 627,080 | 42.2 | 563,961 | 41.9 | 537,131 | 42.5 | 465,483 | 41.6 | 429,944 | 44.6 |
| Residential mortgage | 113,911 | 7.7 | 129,580 | 9.6 | 144,215 | 11.4 | 177,683 | 15.8 | 166,863 | 17.3 |
| Home equity | 231,766 | 15.6 | 208,327 | 15.5 | 200,684 | 15.9 | 189,794 | 16.9 | 194,144 | 20.1 |
| Consumer indirect | 487,713 | 32.9 | 418,016 | 31.1 | 352,611 | 27.9 | 255,054 | 22.8 | 134,977 | 14.0 |
| Other consumer | 24,306 | 1.6 | 26,106 | 1.9 | 29,365 | 2.3 | 33,065 | 2.9 | 38,245 | 4.0 |
| Total consumer | 743,785 | 50.1 | 652,449 | 48.5 | 582,660 | 46.1 | 477,913 | 42.6 | 367,366 | 38.1 |
| Total loans | 1,484,776 | 100.0% | 1,345,990 | 100.0% | 1,264,006 | 100.0% | 1,121,079 | 100.0% | 964,173 | 100.0% |
| Allowance for loan losses | 23,260 | | 20,466 | | 20,741 | | 18,749 | | 15,521 | |
| Total loans, net | $1,461,516 | | $1,325,524 | | $1,243,265 | | $1,102,330 | | $ 948,652 | |

The decrease in residential mortgage loans from $144.2 million to $129.6 million to $113.9 million for the periods ending December 31, 2009, 2010 and 2011, respectively, and the increase in consumer indirect loans from $352.6 million to $418.0 million to $487.7 million for the same periods reflects a strategic shift to increase our consumer indirect loan portfolio, while placing less emphasis on expanding our residential mortgage loan portfolio, coupled with our practice of selling the majority of our fixed-rate residential mortgages in the secondary market with servicing rights retained.

Commercial loans are generally viewed as having more inherent risk of default than residential mortgage or consumer loans. Also, the commercial loan balance per borrower is typically larger than that for residential mortgage and consumer loans, inferring higher potential losses on an individual customer basis. Commercial loans increased during 2011 as we continued our commercial business development efforts. The credit risk related to commercial loans is largely influenced by general economic conditions and the resulting impact on a borrower's operations or on the value of underlying collateral, if any.

The Company participates in various lending programs in which guarantees are supplied by U.S. government agencies, such as the SBA, U.S. Department of Agriculture, Rural Economic and Community Development and Farm Service Agency, among others. As of December 31, 2011, the principal balance of such loans (included in commercial loans) was $60.1 million and the guaranteed portion amounted to $42.5 million. Most of these loans were guaranteed by the SBA.

Commercial business loans were $233.8 million at the end of 2011, up $22.8 million or 11% since year-end 2010, and comprised 15.7% of total loans outstanding at December 31, 2011 and 2010. We typically originate business loans of up to $15.0 million for small to mid-sized businesses in our market area for working capital, equipment financing, inventory financing, accounts receivable financing, or other general business purposes. Loans of this type are in a diverse range of industries. Within the commercial business classification, loans to finance agricultural production totaled approximately 1% of commercial business loans as of December 31, 2011. As of December 31, 2011, commercial business SBA loans accounted for a total of $32.9 million or 14% of our commercial business loan portfolio.

Commercial mortgage loans totaled $393.2 million at December 31, 2011, up $40.3 million or 11% from December 31, 2010, and comprised 26.5% of total loans, compared to 26.2% at December 31, 2010. Commercial mortgage includes both owner occupied and non-owner occupied commercial real estate loans. Approximately 45% and 51% of the commercial mortgage portfolio at December 31, 2011 and 2010, respectively, was owner occupied commercial real estate. The majority of our commercial real estate loans are secured by office buildings, manufacturing facilities, distribution/warehouse facilities, and retail centers, which are generally located in our local market area. As of December 31, 2011, commercial mortgage SBA loans accounted for a total of $20.5 million or 5% of our commercial mortgage loan portfolio.

Our current lending standards for commercial real estate and real estate construction lending are determined by property type and specifically address many criteria, including: maximum loan amounts, maximum loan-to-value ("LTV"), requirements for pre-leasing and / or pre-sales, minimum debt-service coverage ratios, minimum borrower equity, and maximum loan to cost. Currently, the maximum standard for LTV is 85%, with lower limits established for certain higher risk types, such as raw land which has a 65% LTV maximum. Our LTV guidelines are in compliance with regulatory supervisory limits.

Residential mortgage loans totaled $113.9 million at the end of 2011, down $15.7 million or 12% from the prior year and comprised 7.7% of total loans outstanding at December 31, 2011 and 9.6% at December 31, 2010. Residential mortgage loans include conventional first lien home mortgages and we generally limit the maximum loan to 85% of collateral value without credit enhancement (e.g. PMI insurance). As part of management's historical practice of originating and servicing residential mortgage loans, the majority of our fixed-rate residential mortgage loans are sold in the secondary market with servicing rights retained.

Our underwriting guidelines for consumer-related real estate loans include a combination of borrower FICO (credit score), the LTV of the property securing the loan and evidence of the borrower having sufficient income to repay the loan. Currently, for home equity products, the maximum acceptable LTV is 90%. The average FICO score for new home equity production in 2011 was 755 comparable to 759 in 2010. Residential mortgage products continue to be underwritten using FHLMC and FNMA secondary marketing guidelines.

Consumer loans totaled $743.8 million at December 31, 2011, up $91.3 million or 14% compared to 2010, and represented 50.1% of the 2011 year-end loan portfolio versus 48.5% at year-end 2010. Loans in this classification include indirect consumer, home equity and other consumer installment loans. Credit risk for these types of loans is generally influenced by general economic conditions, the characteristics of individual borrowers, and the nature of the loan collateral. Risks of loss are generally on smaller average balances per loan spread over many borrowers. Once charged off, there is usually less opportunity for recovery on these smaller retail loans. Credit risk is primarily controlled by reviewing the creditworthiness of the borrowers, monitoring payment histories, and taking appropriate collateral and guaranty positions.

Consumer indirect loans amounted to $487.7 million at December 31, 2011 up $69.7 million or 17% compared to 2010, and represented 32.9% of the 2011 year-end loan portfolio versus 31.1% at year-end 2010. The loans are primarily for the purchase of automobiles (both new and used) and light duty trucks primarily to individuals, but also to corporations and other organizations. The loans are originated through dealerships and assigned to us with terms that typically range from 36 to 84 months. During the year ended December 31, 2011, we originated $266.7 million in indirect loans with a mix of approximately 46% new auto and 54% used vehicles. This compares with $204.4 million in indirect loans with a mix of approximately 33% new auto and 67% used vehicles for the same period in 2010. The increase in loans for new autos reflects changes in market conditions in 2011. We do business with nearly 400 franchised auto dealers located in Western and Central New York, the Capital District of New York and Northern Pennsylvania.

Home equity consists of home equity lines, as well as home equity loans, some of which are first lien positions. Home equities amounted to $231.8 million at December 31, 2011 up $23.4 million or 11% compared to 2010, and represented 15.6% of the 2011 year-end loan portfolio versus 15.5% at year-end 2010. The portfolio had a weighted average LTV at origination of approximately 53% and 52% at December 31, 2011 and 2010, respectively. Approximately 69% of the loans in the home equity portfolio are first lien positions at December 31, 2011, compared to 63% at December 31, 2010.

Other consumer loans totaled $24.3 million at December 31, 2011, down $1.8 million or 7% compared to 2010, and represented 1.6% of the 2011 year-end loan portfolio versus 1.9% at year-end 2010. Other consumer consists of personal loans (collateralized and uncollateralized) and deposit account collateralized loans.

Factors that are important to managing overall credit quality are sound loan underwriting and administration, systematic monitoring of existing loans and commitments, effective loan review on an ongoing basis, early identification of potential problems, an appropriate allowance for loan losses, and sound nonaccrual and charge off policies.

An active credit risk management process is used for commercial loans to further ensure that sound and consistent credit decisions are made. Credit risk is controlled by detailed underwriting procedures, comprehensive loan administration, and periodic review of borrowers' outstanding loans and commitments. Borrower relationships are formally reviewed and graded on an ongoing basis for early identification of potential problems. Further analyses by customer, industry, and geographic location are performed to monitor trends, financial performance, and concentrations.

The loan portfolio is widely diversified by types of borrowers, industry groups, and market areas within our core footprint. Significant loan concentrations are considered to exist for a financial institution when there are amounts loaned to numerous borrowers engaged in similar activities that would cause them to be similarly impacted by economic or other conditions. At December 31, 2011, no significant concentrations, as defined above, existed in our portfolio in excess of 10% of total loans.

**Loans Held for Sale and Loan Servicing Rights.** Loans held for sale (not included in the loan portfolio composition table) were entirely comprised of residential real estate mortgages and totaled $2.4 million and $3.1 million as of December 31, 2011 and 2010, respectively.

We sell certain qualifying newly originated or refinanced residential real estate mortgages on the secondary market. Residential real estate mortgages serviced for others, which are not included in the consolidated statements of financial condition, amounted to $297.8 million and $328.9 million as of December 31, 2011 and 2010, respectively.

During 2011, we sold $13.0 million of indirect auto loans, recognizing a gain of $153 thousand. The loans were reclassified from portfolio to loans held for sale during the second quarter of 2011. As of December 31, 2011, a loan servicing asset for the sold and serviced indirect auto loans of $574 thousand is included in other assets in the consolidated statements of financial condition.

**Allowance for Loan Losses**

The following table summarizes the activity in the allowance for loan losses (in thousands).

| | Loan Loss Analysis Year Ended December 31, | | | | |
|---|---|---|---|---|---|
| | 2011 | 2010 | 2009 | 2008 | 2007 |
| Allowance for loan losses, beginning of year | $ 20,466 | $ 20,741 | $ 18,749 | $ 15,521 | $ 17,048 |
| Charge-offs: | | | | | |
| Commercial business | 1,346 | 3,426 | 2,360 | 720 | 618 |
| Commercial mortgage | 751 | 263 | 355 | 1,192 | 439 |
| Residential mortgage | 152 | 290 | 225 | 320 | 319 |
| Home equity | 449 | 259 | 195 | 110 | 255 |
| Consumer indirect | 4,713 | 4,669 | 3,637 | 2,011 | 988 |
| Other consumer | 877 | 909 | 1,058 | 1,106 | 1,276 |
| Total charge-offs | 8,288 | 9,816 | 7,830 | 5,459 | 3,895 |
| Recoveries: | | | | | |
| Commercial business | 401 | 326 | 428 | 684 | 1,140 |
| Commercial mortgage | 245 | 501 | 150 | 315 | 216 |
| Residential mortgage | 90 | 21 | 12 | 26 | 50 |
| Home equity | 44 | 36 | 20 | 19 | 12 |
| Consumer indirect | 2,066 | 1,485 | 1,030 | 548 | 235 |
| Other consumer | 456 | 485 | 480 | 544 | 599 |
| Total recoveries | 3,302 | 2,854 | 2,120 | 2,136 | 2,252 |
| Net charge-offs | 4,986 | 6,962 | 5,710 | 3,323 | 1,643 |
| Provision for loan losses | 7,780 | 6,687 | 7,702 | 6,551 | 116 |
| Allowance for loan losses, end of year | $ 23,260 | $ 20,466 | $ 20,741 | $ 18,749 | $ 15,521 |
| | | | | | |
| Net charge-offs to average loans | 0.36% | 0.54% | 0.47% | 0.32% | 0.18% |
| Allowance to end of period loans | 1.57% | 1.52% | 1.64% | 1.67% | 1.61% |
| Allowance to end of period non-performing loans | 329% | 270% | 239% | 229% | 192% |

The following table sets forth the allocation of the allowance for loan losses by loan category as of the dates indicated. The allocation is made for analytical purposes and is not necessarily indicative of the categories in which actual losses may occur. The total allowance is available to absorb losses from any segment of the loan portfolio (in thousands).

| | Allowance for Loan Losses by Loan Category At December 31, | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | 2011 | | 2010 | | 2009 | | 2008 | | 2007 | |
| | Loan Loss Allowance | Percentage of loans by category to total loans | Loan Loss Allowance | Percentage of loans by category to total loans | Loan Loss Allowance | Percentage of loans by category to total loans | Loan Loss Allowance | Percentage of loans by category to total loans | Loan Loss Allowance | Percentage of loans by category to total loans |
| Commercial business | $ 4,036 | 15.7% | $ 3,712 | 15.7% | $ 4,407 | 16.3% | $ 3,300 | 16.1% | $ 2,505 | 16.3% |
| Commercial mortgage | 6,418 | 26.5 | 6,431 | 26.2 | 6,638 | 26.2 | 4,635 | 25.5 | 4,640 | 28.3 |
| Residential mortgage | 858 | 7.7 | 1,013 | 9.6 | 1,251 | 11.4 | 2,516 | 15.8 | 1,763 | 17.3 |
| Home equity | 1,242 | 15.6 | 972 | 15.5 | 1,043 | 15.9 | 2,374 | 16.9 | 1,869 | 20.1 |
| Consumer indirect | 10,189 | 32.9 | 7,754 | 31.1 | 6,837 | 27.9 | 5,152 | 22.8 | 2,284 | 14.0 |
| Other consumer | 517 | 1.6 | 584 | 1.9 | 565 | 2.3 | 772 | 2.9 | 798 | 4.0 |
| Unallocated [1] | — | — | — | — | — | — | — | — | 1,662 | — |
| Total | $23,260 | 100.0% | $20,466 | 100.0% | $20,741 | 100.0% | $18,749 | 100.0% | $15,521 | 100.0% |

[1] During 2008, management revised estimation techniques related to allocation of the allowance to specific loan segments. The result was the elimination of the unallocated portion of the allowance for loan losses and allocation of the entire balance to specific loan segments.

Management believes that the allowance for loan losses at December 31, 2011 is adequate to cover probable losses in the loan portfolio at that date. Factors beyond our control, however, such as general national and local economic conditions, can adversely impact the adequacy of the allowance for loan losses. As a result, no assurance can be given that adverse economic conditions or other circumstances will not result in increased losses in the portfolio or that the allowance for loan losses will be sufficient to meet actual loan losses. See Part I, Item 1A “Risk Factors” for the risks impacting this estimate. Management presents a quarterly review of the adequacy of the allowance for loan losses to our Board of Directors based on the methodology that is described in further detail in Part I, Item I “Business” under the section titled “Lending Activities”. See also “Critical Accounting Estimates” for additional information on the allowance for loan losses.

**Non-performing Assets and Potential Problem Loans**

The following table sets forth information regarding non-performing assets (in thousands):

| | Non-performing Assets At December 31, | | | | |
|---|---|---|---|---|---|
| | 2011 | 2010 | 2009 | 2008 | 2007 |
| Non-accruing loans: | | | | | |
| Commercial business | $ 1,259 | $ 947 | $ 650 | $ 510 | $ 839 |
| Commercial mortgage | 2,928 | 3,100 | 2,288 | 2,670 | 3,294 |
| Residential mortgage | 1,644 | 2,102 | 2,376 | 3,365 | 2,987 |
| Home equity | 682 | 875 | 880 | 1,143 | 661 |
| Consumer indirect | 558 | 514 | 621 | 445 | 278 |
| Other consumer | — | 41 | 7 | 56 | 16 |
| Total non-accruing loans | 7,071 | 7,579 | 6,822 | 8,189 | 8,075 |
| Restructured accruing loans | — | — | — | — | — |
| Accruing loans contractually past due over 90 days | 5 | 3 | 1,859 | 7 | 2 |
| Total non-performing loans | 7,076 | 7,582 | 8,681 | 8,196 | 8,077 |
| Foreclosed assets | 475 | 741 | 746 | 1,007 | 1,421 |
| Non-performing investment securities | 1,636 | 572 | 1,015 | 49 | — |
| Total non-performing assets | $ 9,187 | $ 8,895 | $ 10,442 | $ 9,252 | $ 9,498 |
| Non-performing loans to total loans | 0.48% | 0.56% | 0.69% | 0.73% | 0.84% |
| Non-performing assets to total assets | 0.39% | 0.40% | 0.51% | 0.48% | 0.51% |

Non-performing assets include non-performing loans, foreclosed assets and non-performing investment securities. Non-performing assets at December 31, 2011 were $9.2 million, an increase of $292 thousand from the $8.9 million balance at December 31, 2010. The primary component of non-performing assets is non-performing loans, which were $7.1 million at December 31, 2011, a decrease of $508 thousand from the $7.6 million balance at December 31, 2010.

Approximately $3.1 million, or 44%, of the $7.1 million in non-performing loans as of December 31, 2011 were current with respect to payment of principal and interest, but were classified as non-accruing because repayment in full of principal and/or interest was uncertain. For non-accruing loans outstanding as of December 31, 2011, the amount of interest income forgone totaled $438 thousand. Included in nonaccrual loans are troubled debt restructurings ("TDRs") of $90 thousand at December 31, 2011. We had no TDRs that were accruing interest as of December 31, 2011.

The ratio of non-performing loans to total loans was 0.48% at December 31, 2011, compared to 0.56% at December 31, 2010. This ratio continues to compare favorably to the average of our peer group, which was 3.26% of total loans at September 30, 2011, the most recent period for which information is available (Source: Federal Financial Institutions Examination Council—Bank Holding Company Performance Report as of September 30, 2011—Top-tier bank holding companies having consolidated assets between $1 billion and $3 billion).

Foreclosed assets consist of real property formerly pledged as collateral to loans, which we have acquired through foreclosure proceedings or acceptance of a deed in lieu of foreclosure. Foreclosed asset holdings represented 8 properties totaling $475 thousand at December 31, 2011 and 13 properties totaling $741 thousand at December 31, 2010.

Non-performing investment securities for which we have stopped accruing interest were $1.6 million at December 31, 2011, compared to $572 thousand at December 31, 2010. Non-performing investment securities are included in non-performing assets at fair value and represent pooled trust preferred securities. The market for these securities began to improve during the second quarter of 2011, resulting in substantial increases to their fair value since the beginning of the year. There have been no securities transferred to non-performing status since the first quarter of 2009. During 2011, we recognized gains of $2.3 million from the sale of four of the 14 securities classified as non-performing at December 31, 2010. The securities had a fair value of $251 thousand at December 31, 2010.

Potential problem loans are loans that are currently performing, but information known about possible credit problems of the borrowers causes management to have concern as to the ability of such borrowers to comply with the present loan payment terms and may result in disclosure of such loans as nonperforming at some time in the future. These loans remain in a performing status due to a variety of factors, including payment history, the value of collateral supporting the credits, and/or personal or government guarantees. Management considers loans classified as substandard, which continue to accrue interest, to be potential problem loans. We identified $8.6 million and $11.5 million in loans that continued to accrue interest which were classified as substandard as of December 31, 2011 and 2010, respectively.

## FUNDING ACTIVITIES

### Deposits

The following table summarizes the composition of our deposits (dollars in thousands).

| | At December 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2011 | | 2010 | | 2009 | |
| | Amount | Percent | Amount | Percent | Amount | Percent |
| Noninterest-bearing demand | $ 393,421 | 20.3% | $ 350,877 | 18.6% | $ 324,303 | 18.6% |
| Interest-bearing demand | 362,555 | 18.8 | 374,900 | 19.9 | 363,698 | 20.9 |
| Savings and money market | 474,947 | 24.6 | 417,359 | 22.2 | 368,603 | 21.1 |
| Certificates of deposit < $100,000 | 486,496 | 25.2 | 555,840 | 29.5 | 512,969 | 29.5 |
| Certificates of deposit of $100,000 or more | 214,180 | 11.1 | 183,914 | 9.8 | 173,382 | 9.9 |
| Total deposits | $ 1,931,599 | 100.0% | $ 1,882,890 | 100.0% | $ 1,742,955 | 100.0% |

We offer a variety of deposit products designed to attract and retain customers, with the primary focus on building and expanding long-term relationships. At December 31, 2011, total deposits were $1.932 billion, representing an increase of $48.7 million for the year. Certificates of deposit were approximately 36% and 39% of total deposits at December 31, 2011 and 2010, respectively. Depositors were hesitant to invest in certificates of deposit for long periods due to the low rate environment and, as a result, reduced both the amount they placed in time deposits and the maturity terms.

Nonpublic deposits, the largest component of our funding sources, represented 80% of total deposits and totaled $1.541 billion and $1.501 billion as of December 31, 2011 and 2010, respectively. We have managed this segment of funding through a strategy of competitive pricing that minimizes the number of customer relationships that have only a single service high cost deposit account.

We had no traditional brokered deposits at December 31, 2011 or 2010, however, we do participate in the Certificate of Deposit Account Registry Service (“CDARS”) program, which enables depositors to receive FDIC insurance coverage for deposits otherwise exceeding the maximum insurable amount. Through the CDARS program, deposits in excess of the maximum insurable amount are placed with multiple participating financial institutions. Reciprocal CDARS deposits totaled $46.5 million at December 31, 2011.

As an additional source of funding, we offer a variety of public deposit products to the many towns, villages, counties and school districts within our market. Public deposits generally range from 20% to 25% of our total deposits. There is a high degree of seasonality in this component of funding, because the level of deposits varies with the seasonal cash flows for these public customers. We maintain the necessary levels of short-term liquid assets to accommodate the seasonality associated with public deposits. As of December 31, 2011, total public deposits were $390.2 million or 20% of total deposits, compared to $382.2 million or 20% of total deposits, as of December 31, 2010. In general, the number of public relationships remained stable in comparison to the prior year.

### Borrowings

Outstanding borrowings are summarized as follows as of December 31 (in thousands):

| | 2011 | 2010 |
|---|---|---|
| Short-term borrowings: | | |
| Federal funds purchased | $ 11,597 | $ 38,200 |
| Repurchase agreements | 36,301 | 38,910 |
| Short-term FHLB borrowings | 102,800 | — |
| Total short-term borrowings | 150,698 | 77,110 |
| Long-term borrowings: | | |
| FHLB advances and repurchase agreements | — | 10,065 |
| Junior subordinated debentures | — | 16,702 |
| Total long-term borrowings | — | 26,767 |
| Total borrowings | $ 150,698 | $ 103,877 |

We classify borrowings as short-term or long-term in accordance with the original terms of the agreement.

We have credit capacity with the FHLB and can borrow through facilities that include amortizing and term advances or repurchase agreements. We had approximately $36 million of immediate credit capacity with FHLB as of December 31, 2011. We had approximately $387 million in secured borrowing capacity at the Federal Reserve Bank ("FRB") Discount Window, none of which was outstanding at December 31, 2011. The FHLB and FRB credit capacity are collateralized by securities from our investment portfolio and certain qualifying loans. We had approximately $107 million of credit available under unsecured federal funds purchased lines with various banks as of December 31, 2011.

Funds are borrowed on an overnight basis through retail repurchase agreements with bank customers and federal funds purchased from other financial institutions. Retail repurchase agreement borrowings are collateralized by securities of U.S. Government agencies. Federal funds purchased are short-term borrowings that typically mature within one to ninety days. Federal funds purchased totaled $11.6 million and $38.2 million at December 31, 2011 and 2010, respectively. Repurchase agreements are secured overnight borrowings with customers. These short-term repurchase agreements amounted to $36.3 million and $38.9 million as of December 31, 2011 and 2010, respectively. Short-term FHLB borrowings have original maturities of less than one year and include overnight borrowings which we typically utilizes to address short term funding needs as they arise. Short-term FHLB borrowings at December 31, 2011 consisted of $65.0 million in overnight borrowings and $37.8 million in short-term advances.

The following table summarizes information relating to our short-term borrowings (dollars in thousands).

| | At or for the Year Ended December 31, | | |
|---|---|---|---|
| | 2011 | 2010 | 2009 |
| Year-end balance | $ 150,698 | $ 77,110 | $ 59,543 |
| Year-end weighted average interest rate | 0.39% | 0.21% | 0.59% |
| Maximum outstanding at any month-end | $ 188,355 | $ 77,110 | $ 85,912 |
| Average balance during the year | $ 99,122 | $ 49,104 | $ 43,092 |
| Average interest rate for the year | 0.50% | 0.74% | 0.63% |

Long-term borrowings totaled $26.8 million at December 31, 2010 and consisted of $10.0 million in FHLB repurchase agreements, $65 thousand of FHLB amortizing advances and $16.7 million in 10.20% junior subordinated debentures. The $10.1 million of outstanding FHLB advances and repurchase agreements at December 31, 2010 were repaid upon maturity during 2011. During the third quarter of 2011, we redeemed all of the junior subordinated debentures and recognized a $1.1 million loss on the extinguishment of debt.

**Shareholders' Equity**

Total shareholders' equity was $237.2 million at December 31, 2011, an increase of $25.1 million from $212.1 million at December 31, 2010. During February 2011, we redeemed $12.5 million of Series A preferred stock issued to the U.S. Treasury. During March 2011, we successfully completed a follow-on common equity offering, issuing 2,813,475 shares of common stock at a price of $16.35 per share before associated offering expenses. After deducting underwriting and other offering costs, we received net proceeds of approximately $43.1 million. Prior to the end of the first quarter of 2011, we utilized a portion of the net proceeds to redeem the remaining $25.0 million in Series A preferred stock. The warrant issued to the Treasury was repurchased for $2.1 million during the second quarter of 2011 and recorded as a reduction of additional paid-in capital. For detailed information on shareholders' equity, see Note 11, Shareholders' Equity, of the notes to consolidated financial statements.

The Company and Bank are subject to various regulatory capital requirements. At December 31, 2011, both the Company and the Bank exceeded all regulatory requirements. For detailed information on regulatory capital, see Note 10, Regulatory Matters, of the notes to consolidated financial statements.

**GOODWILL**

The carrying amount of goodwill totaled $37.4 million as of December 31, 2011 and 2010. The goodwill relates to our primary subsidiary and reporting unit, Five Star Bank. We perform a goodwill impairment test on an annual basis or more frequently if events and circumstances warrant. We performed the annual goodwill impairment test as of September 30, 2011 and determined the estimated fair value of our reporting unit to be in excess of its carrying amount. Accordingly, as of the annual impairment test date, there was no indication of goodwill impairment. We test goodwill for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of our reporting unit below its carrying amount.

Declines in the market value of our publicly traded stock price or declines in our ability to generate future cash flows may increase the potential that goodwill recorded on our consolidated statements of financial condition be designated as impaired and that we may incur a goodwill write-down in the future.

## LIQUIDITY AND CAPITAL RESOURCES

The objective of maintaining adequate liquidity is to assure that we meet our financial obligations. These obligations include the withdrawal of deposits on demand or at their contractual maturity, the repayment of matured borrowings, the ability to fund new and existing loan commitments and the ability to take advantage of new business opportunities. We achieve liquidity by maintaining a strong base of core customer funds, maturing short-term assets, our ability to sell or pledge securities, lines-of-credit, and access to the financial and capital markets.

Liquidity for the Bank is managed through the monitoring of anticipated changes in loans, the investment portfolio, core deposits and wholesale funds. The strength of the Bank's liquidity position is a result of its base of core customer deposits. These core deposits are supplemented by wholesale funding sources that include credit lines with the other banking institutions, the FHLB and the FRB.

The primary sources of liquidity for FII are dividends from the Bank and access to financial and capital markets. Dividends from the Bank are limited by various regulatory requirements related to capital adequacy and earnings trends. The Bank relies on cash flows from operations, core deposits, borrowings and short-term liquid assets. FSIS relies on cash flows from operations and funds from FII when necessary.

Our cash and cash equivalents were $57.6 million as of December 31, 2011, up from $39.1 million as of December 31, 2010. Our net cash provided by operating activities totaled $32.0 million and the principal source of operating activity cash flow was net income adjusted for noncash income and expense items. Net cash used in investing activities totaled $104.9 million, which included outflows for net loan origination funding of $157.1 million and inflows from net securities transactions of $60.3 million. Net cash provided by financing activities of $91.4 million was attributed to a $48.7 million increase in deposits, a $73.6 million increase in short-term borrowings and $43.1 million in net proceeds from the issuance of common stock, partly offset by the $37.5 million payment to redeem the Series A preferred stock, $26.8 million of long-term debt repayments and $7.6 million in dividend payments.

### Contractual Obligations and Other Commitments

The following table summarizes the maturities of various contractual obligations and other commitments (in thousands):

| | At December 31, 2011 | | | | |
|---|---|---|---|---|---|
| | Within 1 year | Over 1 to 3 years | Over 3 to 5 Years | Over 5 years | Total |
| **On-Balance sheet:** | | | | | |
| Certificates of deposit [1] | $ 547,874 | $ 102,661 | $ 50,000 | $ 141 | $ 700,676 |
| Supplemental executive retirement plans | 159 | 318 | 318 | 549 | 1,344 |
| **Off-Balance sheet:** | | | | | |
| Limited partnership investments [2] | $ 594 | $ 1,187 | $ 593 | $ — | $ 2,374 |
| Commitments to extend credit [3] | 374,266 | — | — | — | 374,266 |
| Standby letters of credit [3] | 5,488 | 2,512 | 855 | — | 8,855 |
| Operating leases | 1,242 | 2,066 | 1,889 | 4,963 | 10,160 |

[1] Includes the maturity of certificates of deposit amounting to $100 thousand or more as follows: $77.7 million in three months or less; $32.4 million between three months and six months; $57.7 million between six months and one year; and $46.4 million over one year.

[2] We have committed to capital investments in several limited partnerships of up to $6.1 million, of which we have contributed $3.7 million as of December 31, 2011, including $407 thousand during 2011.

[3] We do not expect all of the commitments to extend credit and standby letters of credit to be funded. Thus, the total commitment amounts do not necessarily represent our future cash requirements.

### Off-Balance Sheet Arrangements

With the exception of obligations in connection with our irrevocable loan commitments, operating leases and limited partnership investments, we had no other off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to investors. For additional information on off-balance sheet arrangements, see Note 1, Summary of Significant Accounting Policies and Note 9, Commitments and Contingencies, in the notes to the accompanying consolidated financial statements.

### Security Yields and Maturities Schedule

The following table sets forth certain information regarding the amortized cost ("Cost"), weighted average yields ("Yield") and contractual maturities of our debt securities portfolio as of December 31, 2011. Mortgage-backed securities are included in maturity categories based on their stated maturity date. Actual maturities may differ from the contractual maturities presented because borrowers may have the right to call or prepay certain investments. We have stopped accruing interest on our asset-backed securities. No tax-equivalent adjustments were made to the weighted average yields (in thousands).

| | Due in one year or less | | Due from one to five years | | Due after five years through ten years | | Due after ten years | | Total | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Cost | Yield | Cost | Yield | Cost | Yield | Cost | Yield | Cost | Yield |
| **Available for sale debt securities:** | | | | | | | | | | |
| U.S. Government agencies and government-sponsored enterprises | $ 13,574 | 1.42% | $ 32,137 | 2.21% | $ 34,289 | 2.32% | $ 14,947 | 0.86% | $ 94,947 | 1.93% |
| State and political subdivisions | 9,573 | 3.57 | 43,534 | 2.67 | 65,992 | 2.44 | — | — | 119,099 | 2.62 |
| Mortgage-backed securities | 878 | 4.52 | 5,812 | 3.82 | 83,358 | 1.77 | 300,654 | 3.49 | 390,702 | 3.13 |
| Asset-backed securities | — | — | — | — | — | — | 297 | — | 297 | — |
| | 24,025 | 2.39 | 81,483 | 2.57 | 183,639 | 2.11 | 315,898 | 3.49 | 605,045 | 2.91 |
| **Held to maturity debt securities:** | | | | | | | | | | |
| State and political subdivisions | 18,496 | 2.35 | 3,763 | 4.26 | 905 | 4.90 | 133 | 5.53 | 23,297 | 2.77 |
| | $ 42,521 | 2.37% | $ 85,246 | 2.64% | $ 184,544 | 2.13% | $ 316,031 | 3.49% | $ 628,342 | 2.90% |

### Contractual Loan Maturity Schedule

The following table summarizes the contractual maturities of our loan portfolio at December 31, 2011. Loans, net of deferred loan origination costs, include principal amortization and non-accruing loans. Demand loans having no stated schedule of repayment or maturity and overdrafts are reported as due in one year or less (in thousands).

| | Due in less than one year | Due from one to five years | Due after five years | Total |
|---|---|---|---|---|
| Commercial business | $ 135,627 | $ 82,926 | $ 15,283 | $ 233,836 |
| Commercial mortgage | 109,782 | 187,205 | 96,257 | 393,244 |
| Residential mortgage | 28,673 | 56,585 | 28,653 | 113,911 |
| Home equity | 46,468 | 105,726 | 79,572 | 231,766 |
| Consumer indirect | 161,053 | 310,214 | 16,446 | 487,713 |
| Other consumer | 10,375 | 12,509 | 1,422 | 24,306 |
| Total loans | $ 491,978 | $ 755,165 | $ 237,633 | $ 1,484,776 |
| | | | | |
| Loans maturing after one year: | | | | |
| With a predetermined interest rate | | $ 225,553 | $ 157,596 | $ 383,149 |
| With a floating or adjustable rate | | 529,612 | 80,037 | 609,649 |
| Total loans maturing after one year | | $ 755,165 | $ 237,633 | $ 992,798 |

**Capital Resources**

The FRB has adopted a system using risk-based capital guidelines to evaluate the capital adequacy of bank holding companies on a consolidated basis. The guidelines require a minimum Tier 1 leverage ratio of 4.00%, a minimum Tier 1 capital ratio of 4.00% and a minimum total risk-based capital ratio of 8.00%. The following table reflects the ratios and their components (in thousands):

| | 2011 | 2010 |
|---|---|---|
| Total shareholders' equity | $ 237,194 | $ 212,144 |
| Less: Unrealized gain on securities available for sale, net of tax | 13,570 | 1,877 |
| Unrecognized net periodic pension & postretirement benefits (costs), net of tax | (12,625) | (6,599) |
| Disallowed goodwill and other intangible assets | 37,369 | 37,369 |
| Disallowed deferred tax assets | 1,794 | 14,608 |
| Plus: Qualifying trust preferred securities | — | 16,200 |
| Tier 1 capital | $ 197,086 | $ 181,089 |
| Adjusted average total assets (for leverage capital purposes) | $ 2,282,755 | $ 2,177,911 |
| Tier 1 leverage ratio (Tier 1 capital to adjusted average total assets) | 8.63% | 8.31% |
| Total Tier 1 capital | $ 197,086 | $ 181,089 |
| Plus: Qualifying allowance for loan losses | 20,239 | 18,363 |
| Total risk-based capital | $ 217,325 | $ 199,452 |
| Net risk-weighted assets | $ 1,616,119 | $ 1,466,957 |
| Tier 1 capital ratio (Tier 1 capital to net risk-weighted assets) | 12.20% | 12.34% |
| Total risk-based capital ratio (Total risk-based capital to net risk-weighted assets) | 13.45% | 13.60% |

**CRITICAL ACCOUNTING ESTIMATES**

Our consolidated financial statements are prepared in accordance with GAAP and are consistent with predominant practices in the financial services industry. Application of critical accounting policies, which are those policies that management believes are the most important to our financial position and results, requires management to make estimates, assumptions, and judgments that affect the amounts reported in the consolidated financial statements and accompanying notes and are based on information available as of the date of the financial statements. Future changes in information may affect these estimates, assumptions and judgments, which, in turn, may affect amounts reported in the financial statements.

We have numerous accounting policies, of which the most significant are presented in Note 1, Summary of Significant Accounting Policies, of the notes to consolidated financial statements. These policies, along with the disclosures presented in the other financial statement notes and in this discussion, provide information on how significant assets, liabilities, revenues and expenses are reported in the consolidated financial statements and how those reported amounts are determined. Based on the sensitivity of financial statement amounts to the methods, assumptions, and estimates underlying those amounts, management has determined that the accounting policies with respect to the allowance for loan losses, valuation of goodwill and deferred tax assets, the valuation of securities and determination of OTTI, and accounting for defined benefit plans require particularly subjective or complex judgments important to our financial position and results of operations, and, as such, are considered to be critical accounting policies as discussed below. These estimates and assumptions are based on management's best estimates and judgment and are evaluated on an ongoing basis using historical experience and other factors, including the current economic environment. We adjust these estimates and assumptions when facts and circumstances dictate. Illiquid credit markets and volatile equity have combined with declines in consumer spending to increase the uncertainty inherent in these estimates and assumptions. As future events cannot be determined with precision, actual results could differ significantly from our estimates.

**Adequacy of the Allowance for Loan Losses**

The allowance for loan losses represents management's estimate of probable credit losses inherent in the loan portfolio. Determining the amount of the allowance for loan losses is considered a critical accounting estimate because it requires significant judgment and the use of subjective measurements including management's assessment of the internal risk classifications of loans, changes in the nature of the loan portfolio, industry concentrations, existing economic conditions, the fair value of underlying collateral, and other qualitative and quantitative factors which could affect probable credit losses. Because current economic conditions can change and future events are inherently difficult to predict, the anticipated amount of estimated loan losses, and therefore the appropriateness of the allowance for loan losses, could change significantly. As an integral part of their examination process, various regulatory agencies also review the allowance for loan losses. Such agencies may require additions to the allowance for loan losses or may require that certain loan balances be charged off or downgraded into criticized loan categories when their credit evaluations differ from those of management, based on their judgments about information available to them at the time of their examination. We believe the level of the allowance for loan losses is appropriate as recorded in the consolidated financial statements.

For additional discussion related to our accounting policies for the allowance for loan losses, see the sections titled "Allowance for Loan Losses" in Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" and Note 1, Summary of Significant Accounting Policies, of the notes to consolidated financial statements.

**Valuation of Goodwill**

Goodwill represents the excess of the purchase price over the fair value of net assets acquired in accordance with the purchase method of accounting for business combinations. Goodwill is not amortized but, instead, is subject to impairment tests on at least an annual basis or more frequently if an event occurs or circumstances change that reduce the fair value of a reporting unit below its carrying amount. We complete our annual goodwill impairment test as of September 30 of each year. The impairment testing process is conducted by assigning net assets and goodwill to each reporting unit. Currently, our goodwill is evaluated at the entity level as there is only one reporting unit. The fair value of each reporting unit is compared to the recorded book value "step one". If the fair value of the reporting unit exceeds its carrying value, goodwill is not considered impaired and "step two" is not considered necessary. If the carrying value of a reporting unit exceeds its fair value, the impairment test continues ("step two") by comparing the carrying value of the reporting unit's goodwill to the implied fair value of goodwill. The implied fair value is computed by adjusting all assets and liabilities of the reporting unit to current fair value with the offset adjustment to goodwill. The adjusted goodwill balance is the implied fair value of the goodwill. An impairment charge is recognized if the carrying fair value of goodwill exceeds the implied fair value of goodwill.

**Valuation of Deferred Tax Assets**

The determination of deferred tax expense or benefit is based on changes in the carrying amounts of assets and liabilities that generate temporary differences. The carrying value of our net deferred tax assets assumes that we will be able to generate sufficient future taxable income based on estimates and assumptions (after consideration of historical taxable income as well as tax planning strategies). If these estimates and related assumptions change, we may be required to record valuation allowances against our deferred tax assets resulting in additional income tax expense in the consolidated statements of income. Management evaluates deferred tax assets on a quarterly basis and assesses the need for a valuation allowance, if any. A valuation allowance is established when management believes that it is more likely than not that some portion of its deferred tax assets will not be realized. Changes in valuation allowance from period to period are included in our tax provision in the period of change. For additional discussion related to our accounting policy for income taxes see Note 14, Income Taxes, of the notes to consolidated financial statements.

**Valuation and Other Than Temporary Impairment of Securities**

We record all of our securities that are classified as available for sale at fair value. The fair value of equity securities are determined using public quotations, when available. Where quoted market prices are not available, fair values are estimated based on dealer quotes, pricing models, discounted cash flow methodologies, or similar techniques for which the determination of fair value may require significant judgment or estimation. Fair values of public bonds and those private securities that are actively traded in the secondary market have been determined through the use of third-party pricing services using market observable inputs. Private placement securities and other corporate fixed maturities for which we do not receive a public quotation are valued using a variety of acceptable valuation methods. Market rates used are applicable to the yield, credit quality and average maturity of each security. Private equity securities may also utilize internal valuation methodologies appropriate for the specific asset. Fair values might also be determined using broker quotes or through the use of internal models or analysis.

Securities are evaluated quarterly to determine whether a decline in their fair value is other than temporary. Management utilizes criteria such as, the current intent or requirement to hold or sell the security, the magnitude and duration of the decline and, when appropriate, consideration of negative changes in expected cash flows, creditworthiness, near term prospects of issuers, the level of credit subordination, estimated loss severity, and delinquencies, to determine whether a loss in value is other than temporary. The term “other than temporary” is not intended to indicate that the decline is permanent, but indicates that the prospect for a near-term recovery of value is not necessarily favorable. Declines in the fair value of investment securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses to the extent the impairment is related to credit issues or concerns, or the security is intended to be sold. The amount of impairment related to non-credit related factors on securities not intended to be sold is recognized in other comprehensive income.

**Defined Benefit Pension Plan**

Management is required to make various assumptions in valuing its defined benefit pension plan assets and liabilities. These assumptions include, but are not limited to, the expected long-term rate of return on plan assets, the weighted average discount rate used to value certain liabilities and the rate of compensation increase. We use a third-party specialist to assist in making these estimates and assumptions. Changes in these estimates and assumptions are reasonably possible and may have a material impact on our consolidated financial statements, results of income or liquidity.

**RECENT ACCOUNTING PRONOUNCEMENTS**

See Note 1, Summary of Significant Accounting Policies—Recent Accounting Pronouncements, in the notes to consolidated financial statements for a discussion of recent accounting pronouncements.

## ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

### Asset-Liability Management

The principal objective of our interest rate risk management is to evaluate the interest rate risk inherent in assets and liabilities, determine the appropriate level of risk to us given our business strategy, operating environment, capital and liquidity requirements and performance objectives, and manage the risk consistent with the guidelines approved by our Board of Directors. Management is responsible for reviewing with the Board of Directors our activities and strategies, the effect of those strategies on the net interest margin, the fair value of the portfolio and the effect that changes in interest rates will have on the portfolio and exposure limits. Management has developed an Asset-Liability Policy that meets strategic objectives and regularly reviews the activities of the Bank.

### Net Interest Income at Risk Analysis

The primary tool we use to manage interest rate risk is a "rate shock" simulation to measure the rate sensitivity of the statement of financial condition. Rate shock simulation is a modeling technique used to estimate the impact of changes in rates on net interest income and economic value of equity. The following table sets forth the results of the modeling analysis as of December 31, 2011 (dollars in thousands):

| Changes in interest rate | Net Interest Income | | | Economic Value of Equity | | |
|---|---|---|---|---|---|---|
| | Amount | Change | | Amount | Change | |
| + 300 basis points | $ 85,243 | $ 2,621 | 3.17% | $ 343,691 | $ (19,853) | (5.46)% |
| + 200 basis points | 84,298 | 1,676 | 2.03 | 354,626 | (8,918) | (2.45) |
| + 100 basis points | 83,050 | 429 | 0.52 | 361,887 | (1,656) | (0.46) |
| - 100 basis points | 80,484 | (2,138) | (2.59) | 385,220 | 21,677 | 5.96 |

We measure net interest income at risk by estimating the changes in net interest income resulting from instantaneous and sustained parallel shifts in interest rates of different magnitudes over a period of 12 months. As of December 31, 2011, a 100 basis point increase in rates would increase net interest income by $429 thousand, or 0.5%, over the next twelve-month period. A 100 basis point decrease in rates would decrease net interest income by $2.1 million, or 2.6%, over a twelve-month period. As of December 31, 2011, a 100 basis point increase in rates would decrease the economic value of equity by $1.7 million, or 0.5%, over the next twelve-month period. A 100 basis point decrease in rates would increase the economic value of equity by $21.7 million, or 6.0%, over a twelve-month period. This simulation is based on management's assumption as to the effect of interest rate changes on assets and liabilities and assumes a parallel shift of the yield curve. It also includes certain assumptions about the future pricing of loans and deposits in response to changes in interest rates. Further, it assumes that delinquency rates would not change as a result of changes in interest rates, although there can be no assurance that this will be the case. While this simulation is a useful measure as to net interest income at risk due to a change in interest rates, it is not a forecast of the future results and is based on many assumptions that, if changed, could cause a different outcome.

In addition to the changes in interest rate scenarios listed above, we typically run other scenarios to measure interest rate risk, which vary depending on the economic and interest rate environments.

The following table presents an analysis of our interest rate sensitivity gap position at December 31, 2011. All interest-earning assets and interest-bearing liabilities are shown based on the earlier of their contractual maturity or re-pricing date. The expected maturities are presented on a contractual basis or, if more relevant, based on projected call dates. Investment securities are at amortized cost for both securities available for sale and securities held to maturity. Loans, net of deferred loan origination costs, include principal amortization adjusted for estimated prepayments (principal payments in excess of contractual amounts) and non-accruing loans. Because the interest rate sensitivity levels shown in the table could be changed by external factors such as loan prepayments and liability decay rates or by factors controllable by us, such as asset sales, it is not an absolute reflection of our potential interest rate risk profile (in thousands).

| | At December 31, 2011 | | | | |
|---|---|---|---|---|---|
| | Three Months or Less | Over Three Months Through One Year | Over One Year Through Five Years | Over Five Years | Total |
| INTEREST-EARNING ASSETS: | | | | | |
| Federal funds sold and interest-earning deposits in other banks | $ — | $ 94 | $ — | $ — | $ 94 |
| Investment securities | 117,520 | 144,472 | 254,640 | 111,710 | 628,342 |
| Loans | 469,602 | 257,217 | 667,411 | 92,956 | 1,487,186 |
| Total interest-earning assets | $ 587,122 | $ 401,783 | $ 922,051 | $ 204,666 | 2,115,622 |
| Cash and due from banks | | | | | 57,489 |
| Other assets [1] | | | | | 163,242 |
| Total assets | | | | | $ 2,336,353 |
| INTEREST-BEARING LIABILITIES: | | | | | |
| Interest-bearing demand, savings and money market | $ 837,502 | $ — | $ — | $ — | $ 837,502 |
| Certificates of deposit | 183,321 | 364,553 | 152,661 | 141 | 700,676 |
| Borrowings | 130,698 | 20,000 | — | — | 150,698 |
| Total interest-bearing liabilities | $ 1,151,521 | $ 384,553 | $ 152,661 | $ 141 | 1,688,876 |
| Noninterest-bearing deposits | | | | | 393,421 |
| Other liabilities | | | | | 16,862 |
| Total liabilities | | | | | 2,099,159 |
| Shareholders' equity | | | | | 237,194 |
| Total liabilities and shareholders' equity | | | | | $ 2,336,353 |
| Interest sensitivity gap | $ (564,399) | $ 17,230 | $ 769,390 | $ 204,525 | $ 426,746 |
| Cumulative gap | $ (564,399) | $ (547,169) | $ 222,221 | $ 426,746 | |
| Cumulative gap ratio [2] | 51.0% | 64.4% | 113.2% | 125.3% | |
| Cumulative gap as a percentage of total assets | (24.2)% | (23.4)% | 9.5% | 18.3% | |

[1] Includes net unrealized gain on securities available for sale and allowance for loan losses.

[2] Cumulative total interest-earning assets divided by cumulative total interest-bearing liabilities.

For purposes of interest rate risk management, we direct more attention on simulation modeling, such as "net interest income at risk" as previously discussed, rather than gap analysis. The net interest income at risk simulation modeling is considered by management to be more informative in forecasting future income at risk.

## ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

**FINANCIAL INSTITUTIONS, INC. AND SUBSIDIARIES**
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## Management's Report on Internal Control over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting for Financial Institutions, Inc. and its subsidiaries (the "Company"), as such term is defined in Exchange Act Rules 13a-15(f). The Company's system of internal control over financial reporting has been designed to provide reasonable assurance to the Company's management and board of directors regarding the reliability of financial reporting and the preparation and fair presentation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles.

Any system of internal control over financial reporting, no matter how well designed, has inherent limitations, including the possibility that a control can be circumvented or overridden and misstatements due to error or fraud may occur and not be detected. Also, because of changes in conditions, internal control effectiveness may vary over time. Accordingly, even an effective system of internal control will provide only reasonable assurance with respect to financial statement preparation and presentation.

The Company's management has assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2011. To make this assessment, we used the criteria for effective internal control over financial reporting described in *Internal Control—Integrated Framework* , issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on our assessment and based on such criteria, we believe that, as of December 31, 2011, the Company's internal control over financial reporting was effective.

The Company's independent registered public accounting firm that audited the Company's consolidated financial statements has issued an attestation report on internal control over financial reporting as of December 31, 2011. That report appears herein.

***/s/ Peter G. Humphrey***
President and Chief Executive Officer
March 9, 2012

***/s/ Karl F. Krebs***
Executive Vice President and Chief Financial Officer
March 9, 2012

## Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders
Financial Institutions, Inc.:

We have audited Financial Institutions, Inc. and subsidiaries' (the Company) internal control over financial reporting as of December 31, 2011, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also includes performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2011, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated statements of financial condition of the Company as of December 31, 2011 and 2010, and the related consolidated statements of income, changes in shareholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2011, and our report dated March 9, 2012 expressed an unqualified opinion on those consolidated financial statements.

***/s/ KPMG LLP***

Rochester, New York
March 9, 2012

## Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders
Financial Institutions, Inc.:

We have audited the accompanying consolidated statements of financial condition of Financial Institutions, Inc. and subsidiaries (the Company) as of December 31, 2011 and 2010, and the related consolidated statements of income, changes in shareholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2011. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company as of December 31, 2011 and 2010, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2011, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of December 31, 2011, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated March 9, 2012 expressed an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

***/s/ KPMG LLP***

Rochester, New York
March 9, 2012

**FINANCIAL INSTITUTIONS, INC. AND SUBSIDIARIES**
**Consolidated Statements of Financial Condition**

| (Dollars in thousands, except share and per share data) | December 31, 2011 | 2010 |
|---|---|---|
| **ASSETS** | | |
| Cash and cash equivalents: | | |
| Cash and due from banks | $ 57,489 | $ 38,964 |
| Federal funds sold and interest-bearing deposits in other banks | 94 | 94 |
| Total cash and cash equivalents | 57,583 | 39,058 |
| Securities available for sale, at fair value | 627,518 | 666,368 |
| Securities held to maturity, at amortized cost (fair value of $23,964 and $28,849, respectively) | 23,297 | 28,162 |
| Loans held for sale | 2,410 | 3,138 |
| Loans (net of allowance for loan losses of $23,260 and $20,466, respectively) | 1,461,516 | 1,325,524 |
| Company owned life insurance | 45,556 | 26,053 |
| Premises and equipment, net | 33,085 | 33,263 |
| Goodwill | 37,369 | 37,369 |
| Other assets | 48,019 | 55,372 |
| Total assets | $ 2,336,353 | $ 2,214,307 |
| **LIABILITIES AND SHAREHOLDERS' EQUITY** | | |
| Deposits: | | |
| Noninterest-bearing demand | $ 393,421 | $ 350,877 |
| Interest-bearing demand | 362,555 | 374,900 |
| Savings and money market | 474,947 | 417,359 |
| Certificates of deposit | 700,676 | 739,754 |
| Total deposits | 1,931,599 | 1,882,890 |
| Short-term borrowings | 150,698 | 77,110 |
| Long-term borrowings | — | 26,767 |
| Other liabilities | 16,862 | 15,396 |
| Total liabilities | 2,099,159 | 2,002,163 |
| Commitments and contingencies (Note 9) | | |
| Shareholders' equity: | | |
| Series A 3% preferred stock, $100 par value; 1,533 shares authorized; 1,500 and 1,533 shares issued, respectively | 150 | 153 |
| Series A preferred stock, $5,000 liquidation preference per share, 7,503 shares authorized; 7,503 shares issued at December 31, 2010 | — | 36,210 |
| Series B-1 8.48% preferred stock, $100 par value, 200,000 shares authorized; 173,235 and 174,223 shares issued, respectively | 17,323 | 17,422 |
| Total preferred equity | 17,473 | 53,785 |
| Common stock, $0.01 par value, 50,000,000 shares authorized; 14,161,597 and 11,348,122 shares issued, respectively | 142 | 113 |
| Additional paid-in capital | 67,247 | 26,029 |
| Retained earnings | 158,079 | 144,599 |
| Accumulated other comprehensive income (loss) | 945 | (4,722) |
| Treasury stock, at cost – 358,481 and 410,616 shares, respectively | (6,692) | (7,660) |
| Total shareholders' equity | 237,194 | 212,144 |
| Total liabilities and shareholders' equity | $ 2,336,353 | $ 2,214,307 |

See accompanying notes to the consolidated financial statements.

**FINANCIAL INSTITUTIONS, INC. AND SUBSIDIARIES**
**Consolidated Statements of Income**

| (Dollars in thousands, except per share amounts) | Years ended December 31, 2011 | 2010 | 2009 |
|---|---|---|---|
| Interest income: | | | |
| Interest and fees on loans | $ 77,105 | $ 75,877 | $ 72,706 |
| Interest and dividends on investment securities | 18,013 | 20,622 | 21,694 |
| Other interest income | — | 10 | 82 |
| Total interest income | 95,118 | 96,509 | 94,482 |
| Interest expense: | | | |
| Deposits | 11,434 | 14,853 | 19,090 |
| Short-term borrowings | 500 | 365 | 270 |
| Long-term borrowings | 1,321 | 2,502 | 2,857 |
| Total interest expense | 13,255 | 17,720 | 22,217 |
| Net interest income | 81,863 | 78,789 | 72,265 |
| Provision for loan losses | 7,780 | 6,687 | 7,702 |
| Net interest income after provision for loan losses | 74,083 | 72,102 | 64,563 |
| Noninterest income: | | | |
| Service charges on deposits | 8,679 | 9,585 | 10,065 |
| ATM and debit card | 4,359 | 3,995 | 3,610 |
| Broker-dealer fees and commissions | 1,829 | 1,283 | 1,022 |
| Company owned life insurance | 1,424 | 1,107 | 1,096 |
| Loan servicing | 835 | 1,124 | 1,308 |
| Net gain on sale of loans held for sale | 880 | 650 | 699 |
| Net gain on sales and calls of investment securities | 3,003 | 169 | 3,429 |
| Impairment charges on investment securities | (18) | (594) | (4,666) |
| Net gain (loss) on sale and disposal of other assets | 67 | (203) | 180 |
| Other | 2,867 | 2,338 | 2,052 |
| Total noninterest income | 23,925 | 19,454 | 18,795 |
| Noninterest expense: | | | |
| Salaries and employee benefits | 35,439 | 32,811 | 33,634 |
| Occupancy and equipment | 10,868 | 10,818 | 11,062 |
| Computer and data processing | 2,437 | 2,487 | 2,340 |
| Professional services | 2,617 | 2,197 | 2,524 |
| Supplies and postage | 1,778 | 1,772 | 1,846 |
| FDIC assessments | 1,513 | 2,507 | 3,651 |
| Advertising and promotions | 1,259 | 1,121 | 949 |
| Loss on extinguishment of debt | 1,083 | — | — |
| Other | 6,800 | 7,204 | 6,771 |
| Total noninterest expense | 63,794 | 60,917 | 62,777 |
| Income before income taxes | 34,214 | 30,639 | 20,581 |
| Income tax expense | 11,415 | 9,352 | 6,140 |
| Net income | $ 22,799 | $ 21,287 | $ 14,441 |
| Preferred stock dividends | 1,877 | 3,358 | 3,160 |
| Accretion of discount on Series A preferred stock | 1,305 | 367 | 537 |
| Net income available to common shareholders | $ 19,617 | $ 17,562 | $ 10,744 |
| Earnings per common share (Note 15): | | | |
| Basic | $ 1.50 | $ 1.62 | $ 0.99 |
| Diluted | $ 1.49 | $ 1.61 | $ 0.99 |
| Cash dividends declared per common share | $ 0.47 | $ 0.40 | $ 0.40 |
| Weighted average common shares outstanding: | | | |
| Basic | 13,067 | 10,767 | 10,730 |
| Diluted | 13,157 | 10,845 | 10,769 |

See accompanying notes to the consolidated financial statements.

**FINANCIAL INSTITUTIONS, INC. AND SUBSIDIARIES**
**Consolidated Statements of Changes in Shareholders' Equity**
**Years ended December 31, 2011, 2010 and 2009**

| (Dollars in thousands, except per share data) | Preferred Equity | Common Stock | Additional Paid-in Capital | Retained Earnings | Accumulated Other Comprehensive Income (Loss) | Treasury Stock | Total Shareholders' Equity |
|---|---|---|---|---|---|---|---|
| **Balance at January 1, 2009** | **$ 53,074** | **$ 113** | **$ 26,397** | **$ 124,952** | **$ (4,013)** | **$ (10,223)** | **$ 190,300** |
| Comprehensive income: | | | | | | | |
| Net income | — | — | — | 14,441 | — | — | 14,441 |
| Other comprehensive income, net of tax | — | — | — | — | 311 | — | 311 |
| Total comprehensive income | | | | | | | 14,752 |
| Issuance costs of Series A preferred stock | — | — | (68) | — | — | — | (68) |
| Share-based compensation plans: | | | | | | | |
| Share-based compensation | — | — | 852 | 2 | — | — | 854 |
| Stock options exercised | — | — | (4) | — | — | 19 | 15 |
| Restricted stock awards issued, net | — | — | (207) | — | — | 207 | — |
| Directors' retainer | — | — | (30) | — | — | 151 | 121 |
| Accrued undeclared cumulative dividend on Series A preferred stock, net of accretion | 344 | — | — | (537) | — | — | (193) |
| Cash dividends declared: | | | | | | | |
| Series A 3% preferred-$3.00 per share | — | — | — | (5) | — | — | (5) |
| Series A preferred-$223.61 per share | — | — | — | (1,678) | — | — | (1,678) |
| Series B-1 8.48% preferred-$8.48 per share | — | — | — | (1,477) | — | — | (1,477) |
| Common-$0.40 per share | — | — | — | (4,327) | — | — | (4,327) |
| **Balance at December 31, 2009** | **$ 53,418** | **$ 113** | **$ 26,940** | **$ 131,371** | **$ (3,702)** | **$ (9,846)** | **$ 198,294** |
| Comprehensive income: | | | | | | | |
| Net income | — | — | — | 21,287 | — | — | 21,287 |
| Other comprehensive loss, net of tax | — | — | — | — | (1,020) | — | (1,020) |
| Total comprehensive income | | | | | | | 20,267 |
| Purchases of treasury stock | — | — | — | — | — | (69) | (69) |
| Share-based compensation plans: | | | | | | | |
| Share-based compensation | — | — | 1,031 | — | — | — | 1,031 |
| Stock options exercised | — | — | (74) | — | — | 290 | 216 |
| Restricted stock awards issued, net | — | — | (1,853) | — | — | 1,853 | — |
| Directors' retainer | — | — | (15) | — | — | 112 | 97 |
| Accrued undeclared cumulative dividend on Series A preferred stock, net of accretion | 367 | — | — | (367) | — | — | — |
| Cash dividends declared: | | | | | | | |
| Series A 3% preferred-$3.00 per share | — | — | — | (5) | — | — | (5) |
| Series A preferred-$250.00 per share | — | — | — | (1,876) | — | — | (1,876) |
| Series B-1 8.48% preferred-$8.48 per share | — | — | — | (1,477) | — | — | (1,477) |
| Common-$0.40 per share | — | — | — | (4,334) | — | — | (4,334) |
| **Balance at December 31, 2010** | **$ 53,785** | **$ 113** | **$ 26,029** | **$ 144,599** | **$ (4,722)** | **$ (7,660)** | **$ 212,144** |

***Continued on next page***

See accompanying notes to the consolidated financial statements.

**FINANCIAL INSTITUTIONS, INC. AND SUBSIDIARIES**
**Consolidated Statements of Changes in Shareholders' Equity (Continued)**
**Years ended December 31, 2011, 2010 and 2009**

| (Dollars in thousands, except per share data) | Preferred Equity | Common Stock | Additional Paid-in Capital | Retained Earnings | Accumulated Other Comprehensive Income (Loss) | Treasury Stock | Total Shareholders' Equity |
|---|---|---|---|---|---|---|---|
| **Balance at December 31, 2010** | **$ 53,785** | **$ 113** | **$ 26,029** | **$ 144,599** | **$ (4,722)** | **$ (7,660)** | **$ 212,144** |
| ***Balance carried forward*** | | | | | | | |
| Comprehensive income: | | | | | | | |
| Net income | — | — | — | 22,799 | — | — | 22,799 |
| Other comprehensive income, net of tax | — | — | — | — | 5,667 | — | 5,667 |
| Total comprehensive income | | | | | | | 28,466 |
| Issuance of common stock | — | 29 | 43,098 | — | — | — | 43,127 |
| Purchases of treasury stock | — | — | — | — | — | (215) | (215) |
| Repurchase of Series A 3% preferred stock | (3) | — | — | — | — | — | (3) |
| Repurchase of warrant issued to U.S. Treasury | — | — | (2,080) | — | — | — | (2,080) |
| Redemption of Series A preferred stock | (37,515) | — | 68 | — | — | — | (37,447) |
| Repurchase of Series B-1 8.48% preferred stock | (99) | — | — | — | — | — | (99) |
| Share-based compensation plans: | | | | | | | |
| Share-based compensation | — | — | 1,105 | — | — | — | 1,105 |
| Stock options exercised | — | — | (28) | — | — | 119 | 91 |
| Restricted stock awards issued, net | — | — | (954) | — | — | 954 | — |
| Excess tax benefit on share-based compensation | — | — | 21 | — | — | — | 21 |
| Directors' retainer | — | — | (12) | | | 110 | 98 |
| Accretion of discount on Series A preferred stock | 1,305 | — | — | (1,305) | — | — | — |
| Cash dividends declared: | | | | | | | |
| Series A 3% preferred-$3.00 per share | — | — | — | (5) | — | — | (5) |
| Series A preferred-$53.24 per share | — | — | — | (399) | — | — | (399) |
| Series B-1 8.48% preferred-$8.48 per share | — | — | — | (1,473) | — | — | (1,473) |
| Common-$0.47 per share | — | — | — | (6,137) | — | — | (6,137) |
| **Balance at December 31, 2011** | **$ 17,473** | **$ 142** | **$ 67,247** | **$ 158,079** | **$ 945** | **$ (6,692)** | **$ 237,194** |

See accompanying notes to the consolidated financial statements.

**FINANCIAL INSTITUTIONS, INC. AND SUBSIDIARIES**
**Consolidated Statements of Cash Flows**

| (Dollars in thousands) | Years ended December 31, 2011 | 2010 | 2009 |
|---|---|---|---|
| Cash flows from operating activities: | | | |
| Net income | $ 22,799 | $ 21,287 | $ 14,441 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Depreciation and amortization | 3,466 | 3,537 | 4,067 |
| Net amortization of premiums on securities | 5,722 | 3,005 | 2,587 |
| Provision for loan losses | 7,780 | 6,687 | 7,702 |
| Share-based compensation | 1,105 | 1,031 | 854 |
| Deferred income tax expense | 6,510 | 2,468 | 7,470 |
| Proceeds from sale of loans held for sale | 32,839 | 42,195 | 90,290 |
| Originations of loans held for sale | (31,231) | (44,262) | (88,999) |
| Net gain on sale of loans held for sale | (880) | (650) | (699) |
| Increase in company owned life insurance | (1,424) | (1,107) | (1,096) |
| Net gain on sales and calls of investment securities | (3,003) | (169) | (3,429) |
| Impairment charges on investment securities | 18 | 594 | 4,666 |
| Net (gain) loss on sale and disposal of other assets | (67) | 203 | (180) |
| Loss on extinguishment of debt | 1,083 | — | — |
| Increase in other assets | (7,756) | (353) | (8,773) |
| (Decrease) increase in other liabilities | (4,943) | 961 | (6,633) |
| Net cash provided by operating activities | 32,018 | 35,427 | 22,268 |
| Cash flows from investing activities: | | | |
| Purchases of investment securities: | | | |
| Available for sale | (158,013) | (430,952) | (602,259) |
| Held to maturity | (17,188) | (19,791) | (29,280) |
| Proceeds from principal payments, maturities and calls on investment securities: | | | |
| Available for sale | 168,976 | 219,974 | 353,545 |
| Held to maturity | 21,986 | 30,885 | 46,891 |
| Proceeds from sales and calls of securities available for sale | 44,514 | 122,090 | 224,928 |
| Net increase in loans, excluding sales | (157,110) | (89,507) | (165,716) |
| Loans sold | 13,033 | — | — |
| Purchases of company owned life insurance | (18,079) | (79) | (79) |
| Proceeds from sales of other assets | 705 | 611 | 1,709 |
| Purchases of premises and equipment | (3,678) | (2,438) | (1,959) |
| Net cash used in investing activities | (104,854) | (169,207) | (172,220) |
| Cash flows from financing activities: | | | |
| Net increase in deposits | 48,709 | 139,935 | 109,692 |
| Net increase in short-term borrowings | 73,588 | 17,567 | 36,078 |
| Repayments of long-term borrowings | (26,767) | (20,080) | (508) |
| Proceeds from issuance of common stock, net of issuance costs | 43,127 | — | — |
| Purchases of common stock for treasury | (215) | (69) | — |
| Repurchase of Series A 3% preferred stock | (3) | — | — |
| Issuance costs of Series A preferred stock | — | — | (68) |
| Repurchase of warrant issued to U.S. Treasury | (2,080) | — | — |
| Redemption of Series A preferred stock | (37,447) | — | — |
| Repurchase of Series B-1 8.48% preferred stock | (99) | — | — |
| Proceeds from stock options exercised | 91 | 216 | 15 |
| Excess tax benefit on share-based compensation | 21 | — | — |
| Cash dividends paid to preferred shareholders | (2,118) | (3,358) | (3,160) |
| Cash dividends paid to common shareholders | (5,446) | (4,332) | (4,325) |
| Net cash provided by financing activities | 91,361 | 129,879 | 137,724 |
| Net increase (decrease) in cash and cash equivalents | 18,525 | (3,901) | (12,228) |
| Cash and cash equivalents, beginning of period | 39,058 | 42,959 | 55,187 |
| Cash and cash equivalents, end of period | $ 57,583 | $ 39,058 | $ 42,959 |

See accompanying notes to the consolidated financial statements.

## (1.) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Financial Institutions, Inc., a financial holding company organized under the laws of New York State ("New York" or "NYS"), and its subsidiaries provide deposit, lending and other financial services to individuals and businesses in Central and Western New York. The Company has also expanded its indirect lending network to include relationships with franchised automobile dealers in the Capital District of New York and Northern Pennsylvania. The Company owns all of the capital stock of Five Star Bank, a New York State chartered bank, and Five Star Investment Services, Inc., a broker-dealer and investment advisor subsidiary offering noninsured investment products. References to "the Company" mean the consolidated reporting entities and references to "the Bank" mean Five Star Bank.

The accounting and reporting policies conform to general practices within the banking industry and to U.S. generally accepted accounting principles ("GAAP"). Prior years' consolidated financial statements are re-classified whenever necessary to conform to the current year's presentation.

The Company has evaluated events and transactions for potential recognition or disclosure through the day the financial statements were issued.

The following is a description of the Company's significant accounting policies.

### *(a.) Principles of Consolidation*

The consolidated financial statements include the accounts of the Company and its subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

### *(b.) Use of Estimates*

In preparing the consolidated financial statements in conformity with GAAP, management is required to make estimates and assumptions that affect the reported amount of assets and liabilities as of the date of the statement of financial condition and reported amounts of revenue and expenses during the reporting period. Material estimates relate to the determination of the allowance for loan losses, the carrying value of goodwill and deferred tax assets, the valuation and other than temporary impairment ("OTTI") considerations related to the securities portfolio, and assumptions used in the defined benefit pension plan accounting,. These estimates and assumptions are based on management's best estimates and judgment and are evaluated on an ongoing basis using historical experience and other factors, including the current economic environment. The Company adjusts these estimates and assumptions when facts and circumstances dictate. As future events cannot be determined with precision, actual results could differ significantly from the Company's estimates.

### *(c.) Cash Flow Reporting*

Cash and cash equivalents include cash and due from banks, federal funds sold and interest-bearing deposits in other banks. Net cash flows are reported for loans, deposit transactions and short-term borrowings.

Supplemental cash flow information is summarized as follows for the years ended December 31 (in thousands):

| | 2011 | 2010 | 2009 |
|---|---|---|---|
| Cash paid (received) during the year for: | | | |
| Interest expense | $ 15,668 | $ 17,676 | $ 21,682 |
| Income taxes, net of income tax refunds | 5,191 | 6,923 | (1,312) |
| Non-cash activity: | | | |
| Real estate and other assets acquired in settlement of loans | $ 305 | $ 561 | $ 1,096 |
| Dividends declared and unpaid | 2,144 | 1,694 | 1,692 |
| Decrease in net unsettled security purchases | (67) | (317) | (1,348) |
| Loans securitized | — | — | 15,983 |

**(1.) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

***(d.) Investment Securities***

Investment securities are classified as either available for sale or held to maturity. Debt securities that management has the positive intent and ability to hold to maturity are classified as held to maturity and are recorded at amortized cost. Other investment securities are classified as available for sale and recorded at fair value, with unrealized gains and losses excluded from earnings and reported as a component of shareholders' equity.

Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Securities are evaluated periodically to determine whether a decline in their fair value is other than temporary. Management utilizes criteria such as, the current intent to hold or sell the security, the magnitude and duration of the decline and, when appropriate, consideration of negative changes in expected cash flows, creditworthiness, near term prospects of issuers, the level of credit subordination, estimated loss severity, and delinquencies, to determine whether a loss in value is other than temporary. The term "other than temporary" is not intended to indicate that the decline is permanent, but indicates that the prospect for a near-term recovery of value is not necessarily favorable. Declines in the fair value of investment securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses to the extent the impairment is related to credit issues or concerns, or the security is intended to be sold. The amount of impairment related to non-credit related factors is recognized in other comprehensive income. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

***(e.) Loans Held for Sale and Mortgage Servicing Rights***

The Company generally makes the determination of whether to identify a mortgage as held for sale at the time the loan is closed based on the Company's intent and ability to hold the loan. Loans held for sale are recorded at the lower of cost or market computed on the aggregate portfolio basis. The amount, by which cost exceeds market value, if any, is accounted for as a valuation allowance with changes included in the determination of results of operations for the period in which the change occurs. The amount of loan origination cost and fees are deferred at origination of the loans and recognized as part of the gain and loss on sale of the loans, determined using the specific identification method, in the consolidated statement of income.

The Company originates and sells certain residential real estate loans in the secondary market. The Company typically retains the right to service the mortgages upon sale. Mortgage-servicing rights ("MSRs") represent the cost of acquiring the contractual rights to service loans for others. MSRs are recorded at their fair value at the time a loan is sold and servicing rights are retained. MSRs are reported in other assets in the consolidated statements of financial position and are amortized to noninterest income in the consolidated statements of income in proportion to and over the period of estimated net servicing income. The Company uses a valuation model that calculates the present value of future cash flows to determine the fair value of servicing rights. In using this valuation method, the Company incorporates assumptions to estimate future net servicing income, which include estimates of the cost to service the loan, the discount rate, an inflation rate and prepayment speeds. On a quarterly basis, the Company evaluates its MSRs for impairment and charges any such impairment to current period earnings. In order to evaluate its MSRs the Company stratifies the related mortgage loans on the basis of their predominant risk characteristics, such as interest rates, year of origination and term, using discounted cash flows and market-based assumptions. Impairment of MSRs is recognized through a valuation allowance, determined by estimating the fair value of each stratum and comparing it to its carrying value. Subsequent increases in fair value are adjusted through the valuation allowance, but only to the extent of the valuation allowance. The Company recognized an impairment loss of $35 thousand during the year ended December 31, 2011. No impairment loss was recognized during the years ended December 31, 2010 or 2009.

Mortgage loan servicing includes collecting monthly mortgagor payments, forwarding payments and related accounting reports to investors, collecting escrow deposits for the payment of mortgagor property taxes and insurance, and paying taxes and insurance from escrow funds when due. Loan servicing income (a component of noninterest income in the consolidated statements of income) consists of fees earned for servicing mortgage loans sold to third parties, net of amortization expense and impairment losses associated with capitalized mortgage servicing assets.

**(1.) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

***(f.) Loans***

Loans are classified as held for investment when management has both the intent and ability to hold the loan for the foreseeable future, or until maturity or payoff. Loans are carried at the principal amount outstanding, net of any unearned income and unamortized deferred fees and costs on originated loans. Loan origination fees and certain direct loan origination costs are deferred, and the net amount is amortized into net interest income over the contractual life of the related loans or over the commitment period as an adjustment of yield. Interest income on loans is based on the principal balance outstanding computed using the effective interest method.

A loan is considered delinquent when a payment has not been received in accordance with the contractual terms. The accrual of interest income for commercial loans is discontinued when there is a clear indication that the borrower's cash flow may not be sufficient to meet payments as they become due, while the accrual of interest income for retail loans is discontinued when loans reach specific delinquency levels. Loans are generally placed on nonaccrual status when contractually past due 90 days or more as to interest or principal payments, unless the loan is well secured and in the process of collection. Additionally, whenever management becomes aware of facts or circumstances that may adversely impact the collectability of principal or interest on loans, it is management's practice to place such loans on a nonaccrual status immediately, rather than delaying such action until the loans become 90 days past due. When a loan is placed on nonaccrual status, previously accrued and uncollected interest is reversed, amortization of related deferred loan fees or costs is suspended, and income is recorded only to the extent that interest payments are subsequently received in cash and a determination has been made that the principal balance of the loan is collectible. If collectability of the principal is in doubt, payments received are applied to loan principal. A nonaccrual loan may be returned to accrual status when all delinquent principal and interest payments become current in accordance with the terms of the loan agreement, the borrower has demonstrated a period of sustained performance (generally a minimum of six months) and the ultimate collectability of the total contractual principal and interest is no longer in doubt.

The Company's loan policy dictates the guidelines to be followed in determining when a loan is charged-off. All charge offs are approved by the Bank's senior loan officers or loan committees, depending on the amount of the charge off, and are reported in aggregate to the Bank's Board of Directors. Commercial business and commercial mortgage loans are charged-off when a determination is made that the financial condition of the borrower indicates that the loan will not be collectible in the ordinary course of business. Residential mortgage loans and home equities are generally charged-off or written down when the credit becomes severely delinquent and the balance exceeds the fair value of the property less costs to sell. Indirect and other consumer loans, both secured and unsecured, are generally charged-off in full during the month in which the loan becomes 120 days past due, unless the collateral is in the process of repossession in accordance with the Company's policy.

A loan is accounted for as a troubled debt restructuring if the Company, for economic or legal reasons related to the borrower's financial condition, grants a significant concession to the borrower that it would not otherwise consider. A troubled debt restructuring may involve the receipt of assets from the debtor in partial or full satisfaction of the loan, or a modification of terms such as a reduction of the stated interest rate or face amount of the loan, a reduction of accrued interest, an extension of the maturity date at a stated interest rate lower than the current market rate for a new loan with similar risk, or some combination of these concessions. Troubled debt restructurings generally remain on nonaccrual status until there is a sustained period of payment performance (usually six months or longer) and there is a reasonable assurance that the payments will continue. See Allowance for Loan Losses below for further policy discussion and see Note 4 for additional information on loans.

***(g.) Off-Balance Sheet Financial Instruments***

In the ordinary course of business, the Company enters into off-balance sheet financial instruments consisting of commitments to extend credit, standby letters of credit and financial guarantees. Such financial instruments are recorded in the consolidated financial statements when they are funded or when related fees are incurred or received. The Company periodically evaluates the credit risks inherent in these commitments and establishes loss allowances for such risks if and when these are deemed necessary.

The Company recognizes as liabilities the fair value of the obligations undertaken in issuing the guarantees under the standby letters of credit, net of the related amortization at inception. The fair value approximates the unamortized fees received from the customers for issuing the standby letters of credit. The fees are deferred and recognized on a straight-line basis over the commitment period. Standby letters of credit outstanding at December 31, 2011 had original terms ranging from one to five years.

**(1.) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

Fees received for providing loan commitments and letters of credit that result in loans are typically deferred and amortized to interest income over the life of the related loan, beginning with the initial borrowing. Fees on commitments and letters of credit are amortized to other income as banking fees and commissions over the commitment period when funding is not expected.

***(h.) Allowance for Loan Losses***

The allowance for loan losses is established through charges to earnings in the form of a provision for loan losses. When a loan or portion of a loan is determined to be uncollectible, the portion deemed uncollectible is charged against the allowance and subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis and is based upon periodic review of the collectability of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral, and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance consists of specific and general components. Specific allowances are established for impaired loans. Impaired commercial business and commercial mortgage loans are individually evaluated and measured for impairment based on the present value of expected future cash flows discounted at the loan's effective interest rate, a loan's observable market price, or the fair value of the collateral if the loan is collateral dependent. Regardless of the measurement method, impairment is based on the fair value of the collateral when foreclosure is probable. If the recorded investment in impaired loans exceeds the measure of estimated fair value, a specific allowance is established as a component of the allowance for loan losses. Interest payments on impaired loans are typically applied to principal unless collectability of the principal amount is reasonably assured, in which case interest is recognized on a cash basis. Impaired loans, or portions thereof, are charged off when deemed uncollectible.

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered in determining impairment include payment status and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. The Company determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan by loan basis by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loans obtainable market price, or the fair value of the collateral if the loan is collateral dependent. Large groups of homogeneous loans are collectively evaluated for impairment. Accordingly, the Company does not separately identify individual consumer and residential loans for impairment disclosures unless the loan has been subject to a troubled debt restructure.

General allowances are established for loan losses on a portfolio basis for loans that do not meet the definition of impaired. The portfolio is grouped into similar risk characteristics, primarily loan type. The Company applies an estimated loss rate to each loan group. The loss rate is based on historical experience and as a result can differ from actual losses incurred in the future. The historical loss rate is adjusted for qualitative factors such as levels and trends of delinquent and non-accruing loans, trends in volume and terms, effects of changes in lending policy, the experience, ability and depth of management, national and local economic trends and conditions, concentrations of credit risk, interest rates, highly leveraged borrowers, information risk and collateral risk. The qualitative factors are reviewed at least quarterly and adjustments are made as needed.

While management evaluates currently available information in establishing the allowance for loan losses, future adjustments to the allowance may be necessary if conditions differ substantially from the assumptions used in making the evaluations. In addition, various regulatory agencies, as an integral part of their examination process, periodically review a financial institution's allowance for loan losses. Such agencies may require the financial institution to recognize additions to the allowance based on their judgments about information available to them at the time of their examination.

**(1.) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

***(i.) Other Real Estate Owned***

Other real estate owned consists of properties acquired through foreclosure or by acceptance of a deed in lieu of foreclosure. These assets are recorded at the lower of fair value of the asset acquired less estimated costs to sell or "cost" (defined as the fair value at initial foreclosure). At the time of foreclosure, or when foreclosure occurs in-substance, the excess, if any, of the loan over the fair market value of the assets received, less estimated selling costs, is charged to the allowance for loan losses and any subsequent valuation write-downs are charged to other expense. In connection with the determination of the allowance for loan losses and the valuation of other real estate owned, management obtains appraisals for properties. Operating costs associated with the properties are charged to expense as incurred. Gains on the sale of other real estate owned are included in income when title has passed and the sale has met the minimum down payment requirements prescribed by GAAP. The balance of other real estate owned at December 31, 2011 was $475 thousand.

***(j.) Company Owned Life Insurance***

The Company holds life insurance policies on certain current and former employees. The Company is the owner and beneficiary of the policies. The cash surrender value of these policies is included as an asset on the consolidated statements of financial condition, and any increase in cash surrender value is recorded as noninterest income on the consolidated statements of income. In the event of the death of an insured individual under these policies, the Company would receive a death benefit which would be recorded as noninterest income.

***(k.) Premises and Equipment***

Premises and equipment are stated at cost, less accumulated depreciation and amortization. Depreciation is computed on the straight-line method over the estimated useful lives of the assets. The Company generally amortizes buildings and building improvements over a period of 15 to 39 years and software, furniture and equipment over a period of 3 to 10 years. Leasehold improvements are amortized over the shorter of the lease term or the useful life of the improvements. Premises and equipment are periodically reviewed for impairment or when circumstances present indicators of impairment.

***(l.) Goodwill and Other Intangible Assets***

Goodwill represents the excess of the purchase price over the fair value of net assets acquired in accordance with the purchase method of accounting for business combinations. Goodwill is not amortized but, instead, is subject to impairment tests on at least an annual basis or more frequently if an event occurs or circumstances change that reduce the fair value of a reporting unit below its carrying amount. The Company completes the annual goodwill impairment test as of September 30 of each year. The impairment testing process is conducted by assigning net assets and goodwill to each reporting unit. Currently, the Company's goodwill is evaluated at the entity level as there is only one reporting unit. The fair value of each reporting unit is compared to the recorded book value "step one". If the fair value of the reporting unit exceeds its carrying value, goodwill is not considered impaired and "step two" is not considered necessary. If the carrying value of a reporting unit exceeds its fair value, the impairment test continues ("step two") by comparing the carrying value of the reporting unit's goodwill to the implied fair value of goodwill. The implied fair value is computed by adjusting all assets and liabilities of the reporting unit to current fair value with the offset adjustment to goodwill. The adjusted goodwill balance is the implied fair value of the goodwill. An impairment charge is recognized if the carrying fair value of goodwill exceeds the implied fair value of goodwill.

The company had other intangible assets, consisting entirely of core deposit intangibles, which were fully amortized as of December 31, 2009. Amortization expense for these other intangible assets for the year ended December 31, 2009 was $280 thousand. Amortization of other intangible assets was computed using the straight-line method over the estimated lives of the respective assets (primarily 5 and 7 years).

**(1.) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

***(m.) Federal Home Loan Bank ("FHLB") and Federal Reserve Bank ("FRB") Stock***

The non-marketable investments in FHLB and FRB stock are included in other assets in the consolidated statements of financial condition at par value or cost and are periodically reviewed for impairment. The dividends received relative to these investments are included in other noninterest income in the consolidated statements of income.

As a member of the FHLB system, the Company is required to maintain a specified investment in FHLB of New York ("FHLBNY") stock in proportion to its volume of certain transactions with the FHLB. FHLBNY stock totaled $6.8 million and $2.5 million as of December 31, 2011 and 2010, respectively.

As a member of the FRB system, the Company is required to maintain a specified investment in FRB stock based on a ratio relative to the Company's capital. FRB stock totaled $3.9 million as of December 31, 2011 and 2010.

***(n.) Equity Method Investments***

The Company has investments in limited partnerships and accounts for these investments under the equity method. These investments are included in other assets in the consolidated statements of financial condition and totaled $4.0 million and $3.6 million as of December 31, 2011 and 2010, respectively.

***(o.) Treasury Stock***

Acquisitions of treasury stock are recorded at cost. The reissuance of shares in treasury is recorded at weighted-average cost.

***(p.) Employee Benefits***

The Company participates in a non-contributory defined benefit pension plan for certain employees who previously met participation requirements. The Company also provides post-retirement benefits, principally health and dental care, to employees of a previously acquired entity. The Company has closed the pension and post-retirement plans to new participants. The actuarially determined pension benefit is based on years of service and the employee's highest average compensation during five consecutive years of employment. The Company's policy is to at least fund the minimum amount required by the Employment Retirement Income Security Act of 1974. The cost of the pension and post-retirement plans are based on actuarial computations of current and future benefits for employees, and is charged to noninterest expense in the consolidated statements of income.

The Company recognizes an asset or a liability for a plans' overfunded status or underfunded status, respectively, in the consolidated financial statements and reports changes in the funded status as a component of other comprehensive income, net of applicable taxes, in the year in which changes occur.

***(q.) Share-Based Compensation Plans***

Compensation expense for stock options and restricted stock awards is based on the fair value of the award on the measurement date, which, for the Company, is the date of grant and is recognized ratably over the service period of the award. The fair value of stock options is estimated using the Black-Scholes option-pricing model. The fair value of restricted stock awards is generally the market price of the Company's stock on the date of grant.

Share-based compensation expense is included in the consolidated statements of income under salaries and employee benefits for awards granted to management and in other noninterest expense for awards granted to directors.

***(r.) Income Taxes***

Income taxes are accounted for using the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates in effect for the year in which those temporary differences are expected to be recovered or settled. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enactment date. A valuation allowance is recognized on deferred tax assets if, based upon the weight of available evidence, it is more likely than not that some or all of the assets may not be realized. The Company recognizes interest and/or penalties related to income tax matters in income tax expense.

**(1.) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

***(s.) Earnings Per Common Share***

The Company calculates earnings per common share ("EPS") using the two-class method in accordance with Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 260, "Earnings Per Share". The two-class method requires the Company to present EPS as if all of the earnings for the period are distributed to common shareholders and any participating securities, regardless of whether any actual dividends or distributions are made. All outstanding unvested share-based payment awards that contain rights to nonforfeitable dividends are considered participating securities. Certain of the restricted shares issued under the Company's share-based compensation plan are entitled to dividends at the same rate as common stock. The Company has determined that these outstanding non-vested stock awards qualify as participating securities.

Basic EPS is computed by dividing distributed and undistributed earnings available to common shareholders by the weighted average number of common shares outstanding for the period. Distributed and undistributed earnings available to common shareholders represent net income reduced by preferred stock dividends and distributed and undistributed earnings available to participating securities. Common shares outstanding include common stock and vested restricted stock awards. Diluted EPS reflects the assumed conversion of all potential dilutive securities. A reconciliation of the weighted-average shares used in calculating basic earnings per common share and the weighted average common shares used in calculating diluted earnings per common share for the reported periods is provided in Note 15—Earnings Per Common Share.

***(t.) Recent Accounting Pronouncements***

In December 2011, the Financial Accounting Standard Board ("FASB") issued Accounting Standards Update ("ASU") 2011-12 "*Comprehensive Income (Topic 220)—Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05.*" ASU 2011-12 defers changes in ASU No. 2011-05 that relate to the presentation of reclassification adjustments to allow the FASB time to reconsider whether to require presentation of such adjustments on the face of the financial statements to show the effects of reclassifications out of accumulated other comprehensive income on the components of net income and other comprehensive income. ASU 2011-12 allows entities to continue to report reclassifications out of accumulated other comprehensive income consistent with the presentation requirements in effect before ASU No. 2011-05. All other requirements in ASU No. 2011-05 are not affected by ASU No. 2011-12. ASU 2011-12 is effective for annual and interim periods beginning after December 15, 2011 and is not expected to have a material impact on the Company's consolidated financial statements.

In November 2011, the FASB issued ASU 2011-11 "*Balance Sheet (Topic 210)—"Disclosures about Offsetting Assets and Liabilities."* ASU 2011-11 amends Topic 210, "*Balance Sheet,"* to require an entity to disclose both gross and net information about financial instruments, such as sales and repurchase agreements and reverse sale and repurchase agreements and securities borrowing/lending arrangements, and derivative instruments that are eligible for offset in the statement of financial position and/or subject to a master netting arrangement or similar agreement. ASU 2011-11 is effective for annual and interim periods beginning on January 1, 2013, and is not expected to have a material impact on the Company's consolidated financial statements.

In September 2011, the FASB issued ASU No. 2011-08 "*Testing Goodwill for Impairment."* The provisions of ASU 2011-08 permit an entity the option to first perform a qualitative assessment to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If an entity believes, as a result of its qualitative assessment, that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, the quantitative impairment test is required. Otherwise, no further impairment testing is required. ASU No. 2011-08 includes examples of events and circumstances that may indicate that a reporting unit's fair value is less than its carrying amount. The provisions of ASU No. 2011-08 are effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Early adoption is permitted provided that the entity has not yet performed its annual impairment test for goodwill. The Company performs its annual impairment test for goodwill as of September 30 of each year. The adoption of ASU No. 2011-08 is not expected to have a material impact on the Company's consolidated financial statements.

**(1.) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

In June 2011, the FASB issued ASU 2011-05 *"Comprehensive Income (Topic 220)—Presentation of Comprehensive Income."* ASU 2011-05 amends Topic 220, "Comprehensive Income," to require that all non-owner changes in stockholders' equity be presented in either a single continuous statement of comprehensive income or in two separate but consecutive statements. Additionally, ASU 2011-05 requires entities to present, on the face of the financial statements, reclassification adjustments for items that are reclassified from other comprehensive income to net income in the statement or statements where the components of net income and the components of other comprehensive income are presented. The option to present components of other comprehensive income as part of the statement of changes in stockholders' equity was eliminated. ASU 2011-05 is effective for annual and interim periods beginning after December 15, 2011; however, certain provisions related to the presentation of reclassification adjustments have been deferred by ASU 2011-12 "Comprehensive Income (Topic 220)—Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05," as further discussed above. The adoption of ASU 2011-05 is not expected to have a significant impact on the Company's consolidated financial statements.

In May 2011, the FASB issued ASU 2011-04 *"Fair Value Measurement (Topic 820)—Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs."* ASU 2011-04 changes the wording used to describe many of the requirements in GAAP for measuring fair value and for disclosing information about fair value measurements. Consequently, the amendments in this update result in common fair value measurement and disclosure requirements in GAAP and IFRSs (International Financial Reporting Standards). ASU 2011-04 is effective prospectively during interim and annual periods beginning on or after December 15, 2011. Early adoption by public entities is not permitted. The adoption of ASU 2011-04 is not expected to have a significant impact on the Company's consolidated financial statements.

In April 2011, the FASB issued ASU 2011-03 *"Transfers and Servicing (Topic 860)—Reconsideration of Effective Control for Repurchase Agreement."* ASU 2011-03 removes from the assessment of effective control the criterion relating to the transferor's ability to repurchase or redeem financial assets on substantially the agreed terms, even in the event of default by the transferee. ASU 2011-03 is effective for the first interim or annual period beginning on or after December 15, 2011. The guidance should be applied prospectively to transactions or modifications of existing transactions that occur on or after the effective date. Early adoption is not permitted. The adoption of ASU 2011-03 is not expected to have a significant impact on the Company's consolidated financial statements.

In April 2011, the FASB issued ASU 2011-02 *"A Creditor's Determination of Whether a Restructuring is a Troubled Debt Restructuring"* , which clarifies when creditors should classify loan modifications as troubled debt restructurings. The guidance is effective for interim and annual periods beginning on or after June 15, 2011, and applies retrospectively to restructurings occurring on or after the beginning of the year. The guidance on measuring the impairment of a receivable restructured in a troubled debt restructuring, as clarified, is effective on a prospective basis. A provision in ASU No. 2011-02 also ends the FASB's deferral of the additional disclosures related to troubled debt restructurings as required by ASU No. 2010-20. The Company adopted the provisions of ASU No. 2010-20 retrospectively to all modifications and restructuring activities that have occurred from January 1, 2011. See Note 4 to the Consolidated Financial Statements for the disclosures required by ASU No. 2010-20.

## (2.) INVESTMENT SECURITIES

The amortized cost and estimated fair value of investment securities are summarized below (in thousands).

| | December 31, 2011 | | | |
|---|---|---|---|---|
| | Amortized Cost | Unrealized Gains | Unrealized Losses | Fair Value |
| **Securities available for sale:** | | | | |
| U.S. Government agencies and government sponsored enterprises | $ 94,947 | $ 2,770 | $ 5 | $ 97,712 |
| State and political subdivisions | 119,099 | 5,336 | 11 | 124,424 |
| Mortgage-backed securities: | | | | |
| Federal National Mortgage Association | 98,679 | 2,944 | — | 101,623 |
| Federal Home Loan Mortgage Corporation | 63,838 | 1,017 | — | 64,855 |
| Government National Mortgage Association | 73,226 | 3,376 | — | 76,602 |
| Collateralized mortgage obligations: | | | | |
| Federal National Mortgage Association | 28,339 | 581 | 7 | 28,913 |
| Federal Home Loan Mortgage Corporation | 22,318 | 675 | 1 | 22,992 |
| Government National Mortgage Association | 103,975 | 2,654 | 18 | 106,611 |
| Privately issued | 327 | 1,762 | — | 2,089 |
| Total collateralized mortgage obligations | 154,959 | 5,672 | 26 | 160,605 |
| Total mortgage-backed securities | 390,702 | 13,009 | 26 | 403,685 |
| Asset-backed securities | 297 | 1,400 | — | 1,697 |
| Total available for sale securities | $ 605,045 | $ 22,515 | $ 42 | $ 627,518 |
| **Securities held to maturity:** | | | | |
| State and political subdivisions | $ 23,297 | $ 667 | $ — | $ 23,964 |

| | December 31, 2010 | | | |
|---|---|---|---|---|
| | Amortized Cost | Unrealized Gains | Unrealized Losses | Fair Value |
| **Securities available for sale:** | | | | |
| U.S. Government agencies and government sponsored enterprises | $ 141,591 | $ 1,158 | $ 1,965 | $ 140,784 |
| State and political subdivisions | 105,622 | 1,516 | 1,472 | 105,666 |
| Mortgage-backed securities: | | | | |
| Federal National Mortgage Association | 96,300 | 798 | 1,030 | 96,068 |
| Federal Home Loan Mortgage Corporation | 83,745 | 321 | 1,317 | 82,749 |
| Government National Mortgage Association | 102,633 | 2,422 | 7 | 105,048 |
| Collateralized mortgage obligations: | | | | |
| Federal National Mortgage Association | 8,938 | 231 | 11 | 9,158 |
| Federal Home Loan Mortgage Corporation | 15,917 | 329 | 1 | 16,245 |
| Government National Mortgage Association | 106,969 | 1,761 | 289 | 108,441 |
| Privately issued | 981 | 591 | — | 1,572 |
| Total collateralized mortgage obligations | 132,805 | 2,912 | 301 | 135,416 |
| Total mortgage-backed securities | 415,483 | 6,453 | 2,655 | 419,281 |
| Asset-backed securities | 564 | 204 | 131 | 637 |
| Total available for sale securities | $ 663,260 | $ 9,331 | $ 6,223 | $ 666,368 |
| **Securities held to maturity:** | | | | |
| State and political subdivisions | $ 28,162 | $ 687 | $ — | $ 28,849 |

**(2.) INVESTMENT SECURITIES (Continued)**

Interest and dividends on securities for the years ended December 31 are summarized as follows (in thousands):

| | 2011 | 2010 | 2009 |
|---|---|---|---|
| Taxable interest and dividends | $ 14,185 | $ 17,101 | $ 16,466 |
| Tax-exempt interest and dividends | 3,828 | 3,521 | 5,228 |
| Total interest and dividends on securities | $ 18,013 | $ 20,622 | $ 21,694 |

Sales and calls of securities available for sale for the years ended December 31 were as follows (in thousands):

| | 2011 | 2010 | 2009 |
|---|---|---|---|
| Proceeds from sales and calls | $ 44,514 | $ 122,090 | $ 224,928 |
| Gross realized gains | 3,051 | 173 | 6,826 |
| Gross realized losses | 48 | 4 | 3,397 |

The scheduled maturities of securities available for sale and securities held to maturity at December 31, 2011 are shown below. Actual expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations (in thousands).

| | Amortized Cost | Fair Value |
|---|---|---|
| **Debt securities available for sale:** | | |
| Due in one year or less | $ 24,025 | $ 24,166 |
| Due from one to five years | 81,483 | 84,008 |
| Due after five years through ten years | 183,639 | 190,461 |
| Due after ten years | 315,898 | 328,883 |
| | $ 605,045 | $ 627,518 |
| **Debt securities held to maturity:** | | |
| Due in one year or less | $ 18,496 | $ 18,631 |
| Due from one to five years | 3,763 | 4,062 |
| Due after five years through ten years | 905 | 1,096 |
| Due after ten years | 133 | 175 |
| | $ 23,297 | $ 23,964 |

**(2.) INVESTMENT SECURITIES (Continued)**

There were no unrealized losses in held to maturity securities at December 31, 2011 or December 31, 2010. Unrealized losses on investment securities available for sale and the fair value of the related securities, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position as of December 31 are summarized as follows (in thousands):

| | December 31, 2011 | | | | | |
|---|---|---|---|---|---|---|
| | Less than 12 months | | 12 months or longer | | Total | |
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| **Securities available for sale:** | | | | | | |
| U.S. Government agencies and government sponsored enterprises | $ 2,177 | $ 1 | $ 5,246 | $ 4 | $ 7,423 | $ 5 |
| State and political subdivisions | 452 | 2 | 646 | 9 | 1,098 | 11 |
| Mortgage-backed securities: | | | | | | |
| Collateralized mortgage obligations: | | | | | | |
| Federal National Mortgage Association | — | — | 1,817 | 7 | 1,817 | 7 |
| Federal Home Loan Mortgage Corporation | — | — | 388 | 1 | 388 | 1 |
| Government National Mortgage Association | 6,138 | 18 | — | — | 6,138 | 18 |
| Total collateralized mortgage obligations | 6,138 | 18 | 2,205 | 8 | 8,343 | 26 |
| Total mortgage-backed securities | 6,138 | 18 | 2,205 | 8 | 8,343 | 26 |
| **Total temporarily impaired securities** | $ 8,767 | $ 21 | $ 8,097 | $ 21 | $ 16,864 | $ 42 |

| | December 31, 2010 | | | | | |
|---|---|---|---|---|---|---|
| | Less than 12 months | | 12 months or longer | | Total | |
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| **Securities available for sale:** | | | | | | |
| U.S. Government agencies and government sponsored enterprises | $ 47,752 | $ 1,911 | $ 8,821 | $ 54 | $ 56,573 | $ 1,965 |
| State and political subdivisions | 38,398 | 1,472 | — | — | 38,398 | 1,472 |
| Mortgage-backed securities: | | | | | | |
| Federal National Mortgage Association | 46,777 | 1,030 | — | — | 46,777 | 1,030 |
| Federal Home Loan Mortgage Corporation | 60,707 | 1,317 | — | — | 60,707 | 1,317 |
| Government National Mortgage Association | 5,135 | 7 | — | — | 5,135 | 7 |
| Collateralized mortgage obligations: | | | | | | |
| Federal National Mortgage Association | — | — | 2,332 | 11 | 2,332 | 11 |
| Federal Home Loan Mortgage Corporation | 612 | 1 | — | — | 612 | 1 |
| Government National Mortgage Association | 17,798 | 289 | — | — | 17,798 | 289 |
| Total collateralized mortgage obligations | 18,410 | 290 | 2,332 | 11 | 20,742 | 301 |
| Total mortgage-backed securities | 131,029 | 2,644 | 2,332 | 11 | 133,361 | 2,655 |
| Asset-backed securities | 111 | 61 | 96 | 70 | 207 | 131 |
| **Total temporarily impaired securities** | $ 217,290 | $ 6,088 | $ 11,249 | $ 135 | $ 228,539 | $ 6,223 |

**(2.) INVESTMENT SECURITIES (Continued)**

The following summarizes the amounts of OTTI recognized during the years ended December 31 by investment category (in thousands).

| | 2011 | 2010 | 2009 |
|---|---|---|---|
| Mortgage-backed securities—Privately issued whole loan CMOs | $ 18 | $ — | $ 2,353 |
| Asset-backed securities—Trust preferred securities | — | 526 | 1,787 |
| Asset-backed securities—Other | — | 68 | 526 |
| Total OTTI | $ 18 | $ 594 | $ 4,666 |

The Company reviews investment securities on an ongoing basis for the presence of OTTI with formal reviews performed quarterly. When evaluating debt securities for OTTI, management considers many factors, including: (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, (3) whether the market decline was affected by macroeconomic conditions, and (4) whether the Company has the intention to sell the debt security or whether it is more likely than not that it will be required to sell the debt security before its anticipated recovery. The assessment of whether OTTI exists involves a high degree of subjectivity and judgment and is based on the information available to management at a point in time.

The total number of security positions in the investment portfolio in an unrealized loss position at December 31, 2011 was 14 compared to 156 at December 31, 2010. At December 31, 2011, the Company had positions in 9 investment securities with an amortized cost of $8.1 million and an unrealized loss of $21 thousand that have been in a continuous unrealized loss position for more than 12 months. There were a total of 5 securities positions in the Company's investment portfolio, with an amortized cost of $8.8 million and a total unrealized loss of $21 thousand at December 31, 2011, that have been in a continuous unrealized loss position for less than 12 months. The unrealized loss on these investment securities was predominantly caused by changes in market interest rates, average life or credit spreads subsequent to purchase. The fair value of most of the investment securities in the Company's portfolio fluctuates as market interest rates change.

Based on management's review and evaluation of the Company's debt securities as of December 31, 2011, the debt securities with unrealized losses were not considered to be OTTI. As of December 31, 2011, the Company does not intend to sell any debt securities which have an unrealized loss, it is unlikely the Company will be required to sell these securities before recovery and the Company expects to recover the entire amortized cost of these impaired securities. Accordingly, as of December 31, 2011, management has concluded that unrealized losses on its investment securities are temporary and no further impairment loss has been realized in the Company's consolidated statements of income.

## (3.) LOANS HELD FOR SALE AND LOAN SERVICING RIGHTS

Loans held for sale were entirely comprised of residential real estate mortgages and totaled $2.4 million and $3.1 million as of December 31, 2011 and 2010, respectively.

The Company sells certain qualifying newly originated or refinanced residential real estate mortgages on the secondary market. Residential real estate mortgages serviced for others, which are not included in the consolidated statements of financial condition, amounted to $297.8 million and $328.9 million as of December 31, 2011 and 2010, respectively. In connection with these mortgage-servicing activities, the Company administered escrow and other custodial funds which amounted to approximately $5.9 million and $6.2 million as of December 31, 2011 and 2010, respectively.

The activity in capitalized mortgage servicing assets is summarized as follows for the years ended December 31 (in thousands):

| | 2011 | 2010 | 2009 |
|---|---|---|---|
| Mortgage servicing assets, beginning of year | $ 1,642 | $ 1,534 | $ 925 |
| Originations | 319 | 408 | 952 |
| Amortization | (352) | (300) | (343) |
| Mortgage servicing assets, end of year | 1,609 | 1,642 | 1,534 |
| Valuation allowance | (210) | (175) | (185) |
| Mortgage servicing assets, net, end of year | $ 1,399 | $ 1,467 | $ 1,349 |

The Company did not securitize any residential mortgage loans in 2011 or 2010. During 2009, the Company pooled $16.0 million of one-to-four family residential mortgage loans and converted the loans to FHLMC securities. The Company retained servicing responsibilities for this securitization. The mortgage-backed securities received in exchange for the loans were classified as available-for-sale and subsequently sold. The $564 thousand gain recognized on the sale of the securities is included in the consolidated statements of income under net gain on sales and calls of investment securities.

Automobile loan servicing rights are accounted for using the amortization method. A servicing asset is established at fair value at the time of the sale. The servicing asset is reported in other assets in the consolidated statements of financial position and amortized to noninterest income in the consolidated statements of income in proportion to and over the period of estimated net servicing income. Impairment, if any, is recognized when carrying value exceeds the fair value as determined by calculating the present value of expected net future cash flows. The primary risk characteristic for measuring servicing assets is payoff rates of the underlying loan pools. Valuation calculations rely on the predicted payoff assumption and, if actual payoff is quicker than expected, then future value would be impaired.

During 2011, the Company sold $13.0 million of indirect auto loans under a 90%/10% participation agreement, recognizing a gain of $153 thousand. The loans were reclassified from portfolio to loans held for sale during the second quarter of 2011. As of December 31, 2011, a loan servicing asset for these loans of $574 thousand is included in other assets in the consolidated statements of financial condition. Management reviewed the servicing asset for impairment as of December 31, 2011 and determined that no valuation allowance was necessary. The Company will continue to service the loans for a fee in accordance with the participation agreement.

## (4.) LOANS

The Company's loan portfolio consisted of the following at December 31 (in thousands):

| | Loans, Gross | Net Deferred Loan (Fees) Costs | Loans, Net |
|---|---|---|---|
| **2011** | | | |
| Commercial business | $ 233,727 | $ 109 | $ 233,836 |
| Commercial mortgage | 394,034 | (790) | 393,244 |
| Residential mortgage | 113,865 | 46 | 113,911 |
| Home equity | 227,853 | 3,913 | 231,766 |
| Consumer indirect | 465,807 | 21,906 | 487,713 |
| Other consumer | 24,138 | 168 | 24,306 |
| Total | $ 1,459,424 | $ 25,352 | 1,484,776 |
| Allowance for loan losses | | | (23,260) |
| Total loans, net | | | $ 1,461,516 |
| **2010** | | | |
| Commercial business | $ 210,948 | $ 83 | $ 211,031 |
| Commercial mortgage | 353,537 | (607) | 352,930 |
| Residential mortgage | 129,553 | 27 | 129,580 |
| Home equity | 205,070 | 3,257 | 208,327 |
| Consumer indirect | 400,221 | 17,795 | 418,016 |
| Other consumer | 25,937 | 169 | 26,106 |
| Total | $ 1,325,266 | $ 20,724 | 1,345,990 |
| Allowance for loan losses | | | (20,466) |
| Total loans, net | | | $ 1,325,524 |

The Company's significant concentrations of credit risk in the loan portfolio relate to a geographic concentration in the communities that the Company serves.

Certain executive officers, directors and their business interests are customers of the Company. Transactions with these parties are based on substantially the same terms as similar transactions with unrelated third parties and do not carry more than normal credit risk. Borrowings by these related parties amounted to $378 thousand and $609 thousand at December 31, 2011 and 2010, respectively. During 2011, new borrowings amounted to $4 thousand (including borrowings of executive officers and directors that were outstanding at the time of their election), and repayments and other reductions were $235 thousand.

**(4.) LOANS (Continued)**

**Past Due Loans Aging**

The following table provides an analysis, by loan class, of the Company's delinquent and nonaccrual loans as of December 31 (in thousands):

| | 30-59 Days Past Due | 60-89 Days Past Due | Greater Than 90 Days | Total Past Due | Nonaccrual | Current | Total Loans |
|---|---|---|---|---|---|---|---|
| **2011** | | | | | | | |
| Commercial business | $ 35 | $ — | $ — | $ 35 | $ 1,259 | $ 232,433 | $ 233,727 |
| Commercial mortgage | 165 | — | — | 165 | 2,928 | 390,941 | 394,034 |
| Residential mortgage | 517 | — | — | 517 | 1,644 | 111,704 | 113,865 |
| Home equity | 749 | 68 | — | 817 | 682 | 226,354 | 227,853 |
| Consumer indirect | 984 | 92 | — | 1,076 | 558 | 464,173 | 465,807 |
| Other consumer | 106 | 10 | 5 | 121 | — | 24,017 | 24,138 |
| Total loans, gross | $ 2,556 | $ 170 | $ 5 | $ 2,731 | $ 7,071 | $ 1,449,622 | $ 1,459,424 |
| **2010** | | | | | | | |
| Commercial business | $ 172 | $ 92 | $ — | $ 264 | $ 947 | $ 209,737 | $ 210,948 |
| Commercial mortgage | 163 | — | — | 163 | 3,100 | 350,274 | 353,537 |
| Residential mortgage | 492 | 6 | — | 498 | 2,102 | 126,953 | 129,553 |
| Home equity | 428 | 47 | — | 475 | 875 | 203,720 | 205,070 |
| Consumer indirect | 656 | 107 | — | 763 | 514 | 398,944 | 400,221 |
| Other consumer | 82 | 1 | 3 | 86 | 41 | 25,810 | 25,937 |
| Total loans, gross | $ 1,993 | $ 253 | $ 3 | $ 2,249 | $ 7,579 | $ 1,315,438 | $ 1,325,266 |

There were no loans past due greater than 90 days and still accruing interest as of December 31, 2011 and December 31, 2010. There were $5 thousand and $3 thousand in consumer overdrafts which were past due greater than 90 days as of December 31, 2011 and December 31, 2010, respectively. Consumer overdrafts are overdrawn deposit accounts which have been reclassified as loans but by their terms do not accrue interest.

Interest income on nonaccrual loans, if recognized, is recorded using the cash basis method of accounting. There was no interest income recognized on nonaccrual loans during the years ended December 31, 2011, 2010 and 2009. For the years ended December 31, 2011, 2010 and 2009, estimated interest income of $438 thousand, $474 thousand, and $388 thousand, respectively, would have been recorded if all such loans had been accruing interest according to their original contractual terms.

**Troubled Debt Restructurings**

A modification of a loan constitutes a troubled debt restructuring ("TDR") when a borrower is experiencing financial difficulty and the modification constitutes a concession. The Company offers various types of concessions when modifying loans, however, forgiveness of principal is rarely granted. Commercial loans modified in a TDR may involve temporary interest-only payments, term extensions, reducing the interest rate for the remaining term of the loan, extending the maturity date at an interest rate lower than the current market rate for new debt with similar risk, requesting additional collateral, releasing collateral for consideration, or substituting or adding a new borrower or guarantor. The following presents, by loan class, information related to loans modified in a TDR during the year ended December 31, 2011 (in thousands).

| | Number of Contracts | Pre-Modification Outstanding Recorded Investment | Post-Modification Outstanding Recorded Investment |
|---|---|---|---|
| Commercial business | 6 | $ 142 | $ 142 |
| Commercial mortgage | 1 | 280 | 280 |
| Total | 7 | $ 422 | $ 422 |

**(4.) LOANS (Continued)**

All of the loans identified as TDRs by the Company were previously on nonaccrual status and reported as impaired loans prior to restructuring. The modifications primarily related to extending the amortization periods of the loans. All loans restructured during the year ended December 31, 2011 are on nonaccrual status as of December 31, 2011. Nonaccrual loans that are restructured remain on nonaccrual status, but may move to accrual status after they have performed according to the restructured terms for a period of time. The TDR classification did not have a material impact on the Company's determination of the allowance for loan losses because the modified loans were impaired and evaluated for a specific reserve both before and after restructuring.

For purposes of this disclosure, a loan modified as a TDR is considered to have defaulted when the borrower becomes 90 days past due. As of December 31, 2011, one commercial real estate loan restructured in 2011 with a balance of $261 thousand at December 31, 2011 was in default. This default did not significantly impact the Company's determination of the allowance for loan losses.

**Impaired Loans**

Management has determined that specific commercial loans on nonaccrual status and all loans that have had their terms restructured in a troubled debt restructuring are impaired loans. The following table presents data on impaired loans at December 31 (in thousands):

| | Recorded Investment | Unpaid Principal Balance | Related Allowance | Average Recorded Investment | Interest Income Recognized |
|---|---|---|---|---|---|
| **2011** | | | | | |
| With no related allowance recorded: | | | | | |
| Commercial business | $ 342 | $ 1,266 | $ — | $ 361 | $ — |
| Commercial mortgage | 605 | 696 | — | 583 | — |
| | 947 | 1,962 | — | 944 | — |
| With an allowance recorded: | | | | | |
| Commercial business | 917 | 917 | 436 | 1,033 | — |
| Commercial mortgage | 2,323 | 2,323 | 644 | 2,172 | — |
| | 3,240 | 3,240 | 1,080 | 3,205 | — |
| | $ 4,187 | $ 5,202 | $ 1,080 | $ 4,149 | $ — |
| **2010** | | | | | |
| With no related allowance recorded: | | | | | |
| Commercial business | $ 372 | $ 524 | $ — | $ 275 | $ — |
| Commercial mortgage | 187 | 187 | — | 481 | — |
| | 559 | 711 | — | 756 | — |
| With an allowance recorded: | | | | | |
| Commercial business | 576 | 576 | 149 | 1,828 | — |
| Commercial mortgage | 2,913 | 2,921 | 883 | 1,897 | — |
| | 3,489 | 3,497 | 1,032 | 3,725 | — |
| | $ 4,048 | $ 4,208 | $ 1,032 | $ 4,481 | $ — |

During the year ended December 31, 2009, the Company's average investment in impaired loans was $3.8 million. The Company recognized $69 thousand of interest income on impaired loans during the year ended December 31, 2009. At December 31, 2011, there were no commitments to lend additional funds to those borrowers whose loans were classified as impaired.

**(4.) LOANS (Continued)**

**Credit Quality Indicators**

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors such as the fair value of collateral. The Company analyzes commercial business and commercial mortgage loans individually by classifying the loans as to credit risk. Risk ratings are updated any time the situation warrants. The Company uses the following definitions for risk ratings:

**Special Mention:** Loans classified as special mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the Company's credit position at some future date.

**Substandard:** Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected.

**Doubtful:** Loans classified as doubtful have all the weaknesses inherent in those classified as Substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

Loans not meeting the criteria above that are analyzed individually as part of the process described above are considered "Uncriticized" or pass-rated loans and are included in groups of homogeneous loans with similar risk and loss characteristics.

The following table sets forth the Company's commercial loan portfolio, categorized by internally assigned asset classification, as of December 31 (in thousands):

| | Commercial Business | Commercial Mortgage |
|---|---|---|
| **2011** | | |
| Uncriticized | $ 221,477 | $ 383,700 |
| Special mention | 7,445 | 2,388 |
| Substandard | 4,805 | 7,946 |
| Doubtful | — | — |
| Total | $ 233,727 | $ 394,034 |
| | | |
| **2010** | | |
| Uncriticized | $ 194,510 | $ 338,061 |
| Special mention | 11,479 | 4,931 |
| Substandard | 4,959 | 10,545 |
| Doubtful | — | — |
| Total | $ 210,948 | $ 353,537 |

**(4.) LOANS (Continued)**

The Company utilizes payment status as a means of identifying and reporting problem and potential problem retail loans. The Company considers nonaccrual loans and loans past due greater than 90 days and still accruing interest to be non-performing. The following table sets forth the Company's retail loan portfolio, categorized by payment status, as of December 31 (in thousands):

| | Residential Mortgage | Home Equity | Consumer Indirect | Other Consumer |
|---|---|---|---|---|
| **2011** | | | | |
| Performing | $ 112,221 | $ 227,171 | $ 465,249 | $ 24,138 |
| Non-performing | 1,644 | 682 | 558 | — |
| Total | $ 113,865 | $ 227,853 | $ 465,807 | $ 24,138 |
| **2010** | | | | |
| Performing | $ 127,451 | $ 204,195 | $ 399,707 | $ 25,896 |
| Non-performing | 2,102 | 875 | 514 | 41 |
| Total | $ 129,553 | $ 205,070 | $ 400,221 | $ 25,937 |

**Allowance for Loan Losses**

The following tables set forth the changes in the allowance for loan losses for the years ended December 31 (in thousands):

| | Commercial | Commercial Mortgage | Residential Mortgage | Home Equity | Consumer Indirect | Other Consumer | Total |
|---|---|---|---|---|---|---|---|
| **2011** | | | | | | | |
| **Allowance for loan losses:** | | | | | | | |
| Beginning balance | $ 3,712 | $ 6,431 | $ 1,013 | $ 972 | $ 7,754 | $ 584 | $ 20,466 |
| Charge-offs | (1,346) | (751) | (152) | (449) | (4,713) | (877) | (8,288) |
| Recoveries | 401 | 245 | 90 | 44 | 2,066 | 456 | 3,302 |
| Provision (credit) | 1,269 | 493 | (93) | 675 | 5,082 | 354 | 7,780 |
| Ending balance | $ 4,036 | $ 6,418 | $ 858 | $ 1,242 | $ 10,189 | $ 517 | $ 23,260 |
| Evaluated for impairment: | | | | | | | |
| Individually | $ 436 | $ 644 | $ — | $ — | $ — | $ — | $ 1,080 |
| Collectively | $ 3,600 | $ 5,774 | $ 858 | $ 1,242 | $ 10,189 | $ 517 | $ 22,180 |
| **Loans:** | | | | | | | |
| Ending balance | $ 233,727 | $ 394,034 | $ 113,865 | $ 227,853 | $ 465,807 | $ 24,138 | $ 1,459,424 |
| Evaluated for impairment: | | | | | | | |
| Individually | $ 1,259 | $ 2,928 | $ — | $ — | $ — | $ — | $ 4,187 |
| Collectively | $ 232,468 | $ 391,106 | $ 113,865 | $ 227,853 | $ 465,807 | $ 24,138 | $ 1,455,237 |

**(4.) LOANS (Continued)**

| | Commercial | Commercial Mortgage | Residential Mortgage | Home Equity | Consumer Indirect | Other Consumer | Total |
|---|---|---|---|---|---|---|---|
| **2010** | | | | | | | |
| **Allowance for loan losses:** | | | | | | | |
| Beginning balance | $ 4,407 | $ 6,638 | $ 1,251 | $ 1,043 | $ 6,837 | $ 565 | $ 20,741 |
| Charge-offs | (3,426) | (263) | (290) | (259) | (4,669) | (909) | (9,816) |
| Recoveries | 326 | 501 | 21 | 36 | 1,485 | 485 | 2,854 |
| Provision (credit) | 2,405 | (445) | 31 | 152 | 4,101 | 443 | 6,687 |
| Ending balance | $ 3,712 | $ 6,431 | $ 1,013 | $ 972 | $ 7,754 | $ 584 | $ 20,466 |
| Evaluated for impairment: | | | | | | | |
| Individually | $ 149 | $ 883 | $ — | $ — | $ — | $ — | $ 1,032 |
| Collectively | $ 3,563 | $ 5,548 | $ 1,013 | $ 972 | $ 7,754 | $ 584 | $ 19,434 |
| **Loans:** | | | | | | | |
| Ending balance | $ 210,948 | $ 353,537 | $ 129,553 | $ 205,070 | $ 400,221 | $ 25,937 | $ 1,325,266 |
| Evaluated for impairment: | | | | | | | |
| Individually | $ 948 | $ 3,100 | $ — | $ — | $ — | $ — | $ 4,048 |
| Collectively | $ 210,000 | $ 350,437 | $ 129,553 | $ 205,070 | $ 400,221 | $ 25,937 | $ 1,321,218 |

| 2009 | Total |
|---|---|
| **Allowance for loan losses:** | |
| Beginning balance | $ 18,749 |
| Charge-offs | (7,830) |
| Recoveries | 2,120 |
| Provision | 7,702 |
| Ending balance | $ 20,741 |

**Risk Characteristics**

Commercial business loans primarily consist of loans to small to mid-sized businesses in our market area in a diverse range of industries. These loans are of higher risk and typically are made on the basis of the borrower's ability to make repayment from the cash flow of the borrower's business. Further, the collateral securing the loans may depreciate over time, may be difficult to appraise and may fluctuate in value. The credit risk related to commercial loans is largely influenced by general economic conditions and the resulting impact on a borrower's operations or on the value of underlying collateral, if any.

Commercial mortgage loans generally have larger balances and involve a greater degree of risk than residential mortgage loans, inferring higher potential losses on an individual customer basis. Loan repayment is often dependent on the successful operation and management of the properties, as well as on the collateral securing the loan. Economic events or conditions in the real estate market could have an adverse impact on the cash flows generated by properties securing the Company's commercial real estate loans and on the value of such properties.

Residential mortgage loans and home equities (comprised of home equity loans and home equity lines) are generally made on the basis of the borrower's ability to make repayment from his or her employment and other income, but are secured by real property whose value tends to be more easily ascertainable. Credit risk for these types of loans is generally influenced by general economic conditions, the characteristics of individual borrowers, and the nature of the loan collateral.

Consumer indirect and other consumer loans may entail greater credit risk than residential mortgage loans and home equities, particularly in the case of other consumer loans which are unsecured or, in the case of indirect consumer loans, secured by depreciable assets, such as automobiles or boats. In such cases, any repossessed collateral for a defaulted consumer loan may not provide an adequate source of repayment of the outstanding loan balance. In addition, consumer loan collections are dependent on the borrower's continuing financial stability, thus are more likely to be affected by adverse personal circumstances such as job loss, illness or personal bankruptcy. Furthermore, the application of various federal and state laws, including bankruptcy and insolvency laws, may limit the amount which can be recovered on such loans.

## (5.) PREMISES AND EQUIPMENT, NET

Major classes of premises and equipment at December 31 are summarized as follows (in thousands):

| | 2011 | 2010 |
|---|---|---|
| Land and land improvements | $ 4,330 | $ 4,335 |
| Buildings and leasehold improvements | 40,590 | 39,215 |
| Furniture, fixtures, equipment and vehicles | 23,414 | 23,645 |
| Premises and equipment | 68,334 | 67,195 |
| Accumulated depreciation and amortization | (35,249) | (33,932) |
| Premises and equipment, net | $ 33,085 | $ 33,263 |

Depreciation and amortization expense, included in occupancy and equipment expense in the consolidated statements of income, amounted to $3.5 million for the years ended December 31, 2011 and 2010, and $3.8 million for the year ended December 31, 2009.

## (6.) GOODWILL AND OTHER INTANGIBLE ASSETS

The carrying amount of goodwill totaled $37.4 million as of December 31, 2011 and 2010. The goodwill relates to the Company's primary subsidiary and reporting unit, Five Star Bank. The Company performs a goodwill impairment test on an annual basis or more frequently if events and circumstances warrant. As of September 30, 2011, the Company performed the annual goodwill impairment test and determined the estimated fair value of our reporting unit to be in excess of its carrying amount. Accordingly, as of the Company's annual impairment test date, there was no indication of goodwill impairment. The Company tests its goodwill for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of our reporting unit below its carrying amount.

Declines in the market value of the Company's publicly traded stock price or declines in the Company's ability to generate future cash flows may increase the potential that goodwill recorded on the Company's consolidated statement of financial condition be designated as impaired and that the Company may incur a goodwill write-down in the future.

## (7.) DEPOSITS

A summary of deposits as of December 31 are as follows (in thousands):

| | 2011 | 2010 |
|---|---|---|
| Noninterest-bearing demand | $ 393,421 | $ 350,877 |
| Interest-bearing demand | 362,555 | 374,900 |
| Savings and money market | 474,947 | 417,359 |
| Certificates of deposit, due: | | |
| Within one year | 547,874 | 554,104 |
| One to two years | 84,687 | 126,955 |
| Two to three years | 17,974 | 14,653 |
| Three to five years | 50,000 | 43,888 |
| Thereafter | 141 | 154 |
| Total certificates of deposit | 700,676 | 739,754 |
| Total deposits | $ 1,931,599 | $ 1,882,890 |

Certificates of deposit in denominations of $100,000 or more at December 31, 2011, 2010 and 2009 amounted to $214.2 million, $183.9 million and $173.4 million, respectively.

Interest expense by deposit type for the years ended December 31 is summarized as follows (in thousands):

| | 2011 | 2010 | 2009 |
|---|---|---|---|
| Interest-bearing demand | $ 614 | $ 705 | $ 772 |
| Savings and money market | 1,056 | 1,133 | 1,090 |
| Certificates of deposit | 9,764 | 13,015 | 17,228 |
| Total interest expense on deposits | $ 11,434 | $ 14,853 | $ 19,090 |

## (8.) BORROWINGS

Outstanding borrowings are summarized as follows as of December 31 (in thousands):

| | 2011 | 2010 |
|---|---|---|
| Short-term borrowings: | | |
| Federal funds purchased | $ 11,597 | $ 38,200 |
| Repurchase agreements | 36,301 | 38,910 |
| Short-term FHLB borrowings | 102,800 | — |
| Total short-term borrowings | 150,698 | 77,110 |
| Long-term borrowings: | | |
| FHLB advances and repurchase agreements | — | 10,065 |
| Junior subordinated debentures | — | 16,702 |
| Total long-term borrowings | — | 26,767 |
| Total borrowings | $ 150,698 | $ 103,877 |

The Company classifies borrowings as short-term or long-term in accordance with the original terms of the agreement. At December 31, 2011, the Company's short-term borrowings had a weighted average rate of 0.39%.

### Short-term Borrowings

Federal funds purchased are short-term borrowings that typically mature within one to ninety days. Federal funds purchased totaled $11.6 million and $38.2 million at December 31, 2011 and 2010, respectively. Repurchase agreements are secured overnight borrowings with customers. These short-term repurchase agreements amounted to $36.3 million and $38.9 million as of December 31, 2011 and 2010, respectively. Short-term FHLB borrowings have original maturities of less than one year and include overnight borrowings which the Company typically utilizes to address short term funding needs as they arise. Short-term FHLB borrowings at December 31, 2011 consisted of $65.0 million in overnight borrowings and $37.8 million in short-term advances.

### Long-term Borrowings

The Company has credit capacity with the FHLB and can borrow through facilities that include an overnight line of credit, amortizing and term advances, and repurchase agreements. The FHLB credit capacity is collateralized by securities from the Company's investment portfolio and certain qualifying loans. FHLB advances totaled $65 thousand as of December 31, 2010. FHLB repurchase agreements are stated at the amount of cash received in connection with the transaction. The Company may be required to provide additional collateral based on the fair value of the underlying securities. FHLB repurchase agreements totaled $10.0 million as of December 31, 2010. The $10.1 million of outstanding FHLB advances and repurchase agreements at December 31, 2010 were repaid upon maturity during 2011.

In February 2001, the Company formed Financial Institutions Statutory Trust I (the "Trust") for the sole purpose of issuing trust preferred securities. The Company's $502 thousand investment in the common equity of the Trust was classified in the consolidated statements of financial condition as other assets and $16.7 million of related 10.20% junior subordinated debentures were classified as long-term borrowings. In 2001, the Company incurred costs relating to the issuance of the debentures totaling $487 thousand. These costs, which were included in other assets on the consolidated statements of financial condition, were deferred and were being amortized to interest expense using the straight-line method over a twenty year period.

In August 2011, the Company redeemed all of the 10.20% junior subordinated debentures at a redemption price equaling 105.1% of the principal amount redeemed, plus all accrued and unpaid interest. As a result of the redemption, the Company recognized a loss on extinguishment of debt of $1.1 million, consisting of the redemption premium of $852 thousand and the write-off of the remaining unamortized issuance costs of $231 thousand.

Interest expense on borrowings for the years ended December 31 is summarized as follows (in thousands):

| | 2011 | 2010 | 2009 |
|---|---|---|---|
| Short-term borrowings | $ 500 | $ 365 | $ 270 |
| Long-term borrowings | 1,321 | 2,502 | 2,857 |
| Total interest expense on borrowings | $ 1,821 | $ 2,867 | $ 3,127 |

## (9.) COMMITMENTS AND CONTINGENCIES

### Financial Instruments with Off-Balance Sheet Risk

The Company has financial instruments with off-balance sheet risk established in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. These instruments involve, to varying degrees, elements of credit and interest rate risk extending beyond amounts recognized in the financial statements.

The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is essentially the same as that involved with extending loans to customers. The Company uses the same credit underwriting policies in making commitments and conditional obligations as for on-balance sheet instruments.

Off-balance sheet commitments as of December 31 consist of the following (in thousands):

| | 2011 | 2010 |
|---|---|---|
| Commitments to extend credit | $ 374,266 | $ 357,240 |
| Standby letters of credit | 8,855 | 6,524 |

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Commitments may expire without being drawn upon; therefore the total commitment amounts do not necessarily represent future cash requirements. Each customer's creditworthiness is evaluated on a case-by-case basis. The amount of collateral obtained, if any, is based on management's credit evaluation of the borrower. Standby letters of credit are conditional lending commitments issued by the Company to guarantee the performance of a customer to a third party. These standby letters of credit are primarily issued to support private borrowing arrangements. The credit risk involved in issuing standby letters of credit is essentially the same as that involved in extending loan facilities to customers.

The Company also extends rate lock agreements to borrowers related to the origination of residential mortgage loans. To mitigate the interest rate risk inherent in these rate lock agreements when the Company intends to sell the related loan, once originated, as well as closed residential mortgage loans held for sale, the Company enters into forward commitments to sell individual residential mortgages. Rate lock agreements and forward commitments are considered derivatives and are recorded at fair value. Forward sales commitments totaled $2.9 million and $8.0 million at December 31, 2011 and 2010, respectively. In addition, the net change in the fair values of these derivatives was recognized as other noninterest income or other noninterest expense in the consolidated statements of income.

### Lease Obligations

The Company is obligated under a number of noncancellable operating lease agreements for land, buildings and equipment. Certain of these leases provide for escalation clauses and contain renewal options calling for increased rentals if the lease is renewed. Future minimum payments by year and in the aggregate, under the noncancellable leases with initial or remaining terms of one year or more, are as follows at December 31, 2011 (in thousands):

| | |
|---|---|
| 2012 | $ 1,242 |
| 2013 | 1,049 |
| 2014 | 1,017 |
| 2015 | 962 |
| 2016 | 927 |
| Thereafter | 4,963 |
| | $ 10,160 |

Rent expense relating to these operating leases, included in occupancy and equipment expense in the statements of income, was $1.5 million, $1.4 million and $1.5 million in 2011, 2010 and 2009, respectively.

### Contingent Liabilities

In the ordinary course of business there are various threatened and pending legal proceedings against the Company. Based on consultation with outside legal counsel, management believes that the aggregate liability, if any, arising from such litigation would not have a material adverse effect on the Company's consolidated financial statements.

## (10.) REGULATORY MATTERS

### General

The supervision and regulation of financial and bank holding companies and their subsidiaries is intended primarily for the protection of depositors, the deposit insurance funds regulated by the FDIC and the banking system as a whole, and not for the protection of shareholders or creditors of bank holding companies. The various bank regulatory agencies have broad enforcement power over financial holding companies and banks, including the power to impose substantial fines, operational restrictions and other penalties for violations of laws and regulations and for safety and soundness considerations.

### Capital

Banks and financial holding companies are subject to various regulatory capital requirements administered by state and federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary, actions by regulators that, if undertaken, could have a direct material impact on the Company's consolidated financial statements. Capital adequacy guidelines and, additionally for banks, prompt corrective action regulations, involve quantitative measures of assets, liabilities, and certain off-balance sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators about components, risk weighting and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Company and the Bank to maintain minimum amounts and ratios of Total and Tier 1 capital to risk-weighted assets and of Tier 1 capital to average assets (all as defined in the regulations). These minimum amounts and ratios are included in the table below.

The Company's and the Bank's Tier 1 capital consists of shareholders' equity excluding unrealized gains and losses on securities available for sale (except for unrealized losses which have been determined to be other than temporary and recognized as expense in the consolidated statements of income), goodwill and other intangible assets and disallowed portions of deferred tax assets. As of December 31, 2011, Tier 1 capital for the Company includes, subject to limitation, $17.5 million of preferred stock. As of December 31, 2010, Tier 1 capital for the Company also includes, subject to limitation, $16.7 million of trust preferred securities issued by FISI Statutory Trust I (see Note 8, Borrowings) and $37.5 million of preferred stock issued to the U.S. Department of Treasury (the "Treasury") through the Treasury's Troubled Asset Relief Program ("TARP") (see Note 11, Shareholders' Equity). The Company and the Bank's total capital are comprised of Tier 1 capital for each entity plus a permissible portion of the allowance for loan losses.

The Tier 1 and total risk-based capital ratios are calculated by dividing the respective capital amounts by risk-weighted assets. Risk-weighted assets are calculated based on regulatory requirements and include total assets, excluding goodwill and other intangible assets and disallowed portions of deferred tax assets, allocated by risk weight category and certain off-balance-sheet items (primarily loan commitments and securities more than one level below investment grade that are subject to the low level exposure rules). The leverage ratio is calculated by dividing Tier 1 capital by adjusted quarterly average total assets, which exclude goodwill and other intangible assets and disallowed portions of deferred tax assets.

**(10.) REGULATORY MATTERS (Continued)**

The Company's and the Bank's actual and required regulatory capital ratios were as follows (in thousands):

| | | Actual | | For Capital Adequacy Purposes | | Well Capitalized | |
|---|---|---|---|---|---|---|---|
| | | Amount | Ratio | Amount | Ratio | Amount | Ratio |
| **December 31, 2011:** | | | | | | | |
| Tier 1 leverage: | Company | $ 197,086 | 8.63% | $ 91,310 | 4.00% | $ 114,138 | 5.00% |
| | Bank | 184,639 | 8.10 | 91,192 | 4.00 | 113,990 | 5.00 |
| Tier 1 capital: | Company | 197,086 | 12.20 | 64,645 | 4.00 | 96,967 | 6.00 |
| | Bank | 184,639 | 11.46 | 64,445 | 4.00 | 96,667 | 6.00 |
| Total risk-based capital: | Company | 217,325 | 13.45 | 129,290 | 8.00 | 161,612 | 10.00 |
| | Bank | 204,817 | 12.71 | 128,890 | 8.00 | 161,112 | 10.00 |
| **December 31, 2010:** | | | | | | | |
| Tier 1 leverage: | Company | $ 181,089 | 8.31% | $ 87,116 | 4.00% | $ 108,896 | 5.00% |
| | Bank | 156,957 | 7.22 | 86,958 | 4.00 | 108,697 | 5.00 |
| Tier 1 capital: | Company | 181,089 | 12.34 | 58,678 | 4.00 | 88,017 | 6.00 |
| | Bank | 156,957 | 10.74 | 58,450 | 4.00 | 87,674 | 6.00 |
| Total risk-based capital: | Company | 199,452 | 13.60 | 117,357 | 8.00 | 146,696 | 10.00 |
| | Bank | 175,250 | 11.99 | 116,899 | 8.00 | 146,124 | 10.00 |

As of December 31, 2011, the Company and Bank were considered "well capitalized" under all regulatory capital guidelines. Such determination has been made based on the Tier 1 leverage, Tier 1 capital and total risk-based capital ratios.

**Federal Reserve Requirements**

The Bank is required to maintain a reserve balance at the FRB of New York. The reserve requirement for the Bank totaled $1.0 million as of December 31, 2011 and 2010.

**Dividend Restrictions**

In the ordinary course of business, the Company is dependent upon dividends from Five Star Bank to provide funds for the payment of interest expense on the junior subordinated debentures, dividends to shareholders and to provide for other cash requirements. Banking regulations may limit the amount of dividends that may be paid. Approval by regulatory authorities is required if the effect of dividends declared would cause the regulatory capital of the Bank to fall below specified minimum levels. Approval is also required if dividends declared exceed the net profits for that year combined with the retained net profits for the preceding two years. The Company is no longer subject to the limitations prescribed by the terms of the Treasury's TARP Capital Purchase Program (see Note 11, Shareholders' Equity).

## (11.) SHAREHOLDERS' EQUITY

The Company's authorized capital stock consists of 50,210,000 shares of capital stock, 50,000,000 of which are common stock, par value $0.01 per share, and 210,000 of which are preferred stock, par value $100 per share, which is designated into two classes, Class A of which 10,000 shares are authorized, and Class B of which 200,000 shares are authorized. There are two series of Class A preferred stock: Series A 3% preferred stock and the Series A preferred stock. There is one series of Class B preferred stock: Series B-1 8.48% preferred stock. There were 174,735 shares and 183,259 shares of preferred stock issued and outstanding as of December 31, 2011 and 2010, respectively.

### Common Stock

The following table sets forth the changes in the number of shares of common stock for the years ended December 31 (in thousands):

| | Outstanding | Treasury | Issued |
|---|---|---|---|
| **2011** | | | |
| Shares outstanding at beginning of year | 10,937,506 | 410,616 | 11,348,122 |
| Shares issued in common stock offering | 2,813,475 | — | 2,813,475 |
| Restricted stock awards issued, net of forfeitures | 51,070 | (51,070) | — |
| Stock options exercised | 6,357 | (6,357) | — |
| Treasury stock purchases | (11,181) | 11,181 | — |
| Directors' retainer | 5,889 | (5,889) | — |
| Shares outstanding at end of year | 13,803,116 | 358,481 | 14,161,597 |
| | | | |
| **2010** | | | |
| Shares outstanding at beginning of year | 10,820,268 | 527,854 | 11,348,122 |
| Restricted stock awards issued, net of forfeitures | 99,324 | (99,324) | — |
| Stock options exercised | 15,563 | (15,563) | — |
| Treasury stock purchases | (3,658) | 3,658 | — |
| Directors' retainer | 6,009 | (6,009) | — |
| Shares outstanding at end of year | 10,937,506 | 410,616 | 11,348,122 |

### Issuance of Common Stock

In March 2011, the Company completed the sale of 2,813,475 shares of its common stock through an underwritten public offering at a price of $16.35 per share. The net proceeds of the offering, after deducting underwriting discounts and commissions and offering expenses, were $43.1 million. A portion of the proceeds from this offering was used to redeem the Company's Series A preferred stock and the 10.20% junior subordinated debentures.

### Preferred Stock

***Series A 3% Preferred Stock.*** There were 1,500 shares and 1,533 shares of Series A 3% preferred stock issued and outstanding as of December 31, 2011 and 2010, respectively. Holders of Series A 3% preferred stock are entitled to receive an annual dividend of $3.00 per share, which is cumulative and payable quarterly. Holders of Series A 3% preferred stock have no pre-emptive right in, or right to purchase or subscribe for, any additional shares of the Company's capital stock and have no voting rights. Dividend or dissolution payments to the Class A shareholders must be declared and paid, or set apart for payment, before any dividends or dissolution payments can be declared and paid, or set apart for payment, to the holders of Class B preferred stock or common stock. The Series A 3% preferred stock is not convertible into any other of the Company's securities.

***Series B-1 8.48% Preferred Stock.*** There were 173,235 shares and 174,223 shares of Series B-1 8.48% preferred stock issued and outstanding as of December 31, 2011 and 2010, respectively. Holders of Series B-1 8.48% preferred stock are entitled to receive an annual dividend of $8.48 per share, which is cumulative and payable quarterly. Holders of Series B-1 8.48% preferred stock have no pre-emptive right in, or right to purchase or subscribe for, any additional shares of the Company's common stock and have no voting rights. Accumulated dividends on the Series B-1 8.48% preferred stock do not bear interest, and the Series B-1 8.48% preferred stock is not subject to redemption. Dividend or dissolution payments to the Class B shareholders must be declared and paid, or set apart for payment, before any dividends or dissolution payments are declared and paid, or set apart for payment, to the holders of common stock. The Series B-1 8.48% preferred stock is not convertible into any other of the Company's securities.

**(11.) SHAREHOLDERS' EQUITY (Continued)**

**Redemption of Series A Preferred Stock and Warrant**

In December 2008, under the Treasury's TARP Capital Purchase Program, the Company entered into a Securities Purchase Agreement—Standard Terms with the Treasury pursuant to which, among other things, the Company sold to the Treasury for an aggregate purchase price of $37.5 million, 7,503 shares of fixed rate cumulative perpetual preferred stock, Series A ("Series A" preferred stock) and a warrant to purchase up to 378,175 shares of common stock, par value $0.01 per share, at an exercise price of $14.88 per share (the "Warrant"), of the Company.

Pursuant to the terms of the Purchase Agreement, the Company's ability to declare or pay dividends on any of its shares was limited. Specifically, the Company was prohibited from paying any dividend with respect to shares of common stock, other junior securities or preferred stock ranking *pari passu* with the Series A preferred stock or repurchasing or redeeming any shares of the Company's common stock, other junior securities or preferred stock ranking *pari passu* with the Series A preferred stock in any quarter unless all accrued and unpaid dividends were paid on the Series A preferred stock for all past dividend periods (including the latest completed dividend period), subject to certain limited exceptions.

The $37.5 million in proceeds was allocated to the Series A preferred stock and the Warrant based on their relative fair values at issuance ($35.5 million was allocated to the Series A preferred stock and $2.0 million to the Warrant). The resulting discount for the Series A preferred stock was to be accreted over five years through retained earnings as a preferred stock dividend. The Warrant was to remain in additional paid-in-capital at its initial book value until it was exercised or expired.

In February 2011, the Company redeemed one-third, or $12.5 million, of the Series A preferred stock. In March 2011, the remaining $25.0 million of the Series A preferred stock was redeemed. The unamortized discount related to the Series A preferred stock was charged to retained earnings upon redemption. The complete redemption of the Series A preferred stock removed the TARP restrictions pertaining to the Company's ability to declare and pay dividends and repurchase its common stock, as well as certain restrictions associated with executive compensation.

In May 2011, the Company repurchased the Warrant issued to the Treasury. The repurchase price of $2.1 million was recorded as a reduction of additional paid-in capital.

## (12.) COMPREHENSIVE INCOME

Total comprehensive income is reported in the accompanying consolidated statements of changes in shareholders' equity. Information related to comprehensive income for the years ended December 31 was as follows (in thousands):

| | Pre-tax Amount | Tax Expense (Benefit) | Net-of-tax Amount |
|---|---|---|---|
| **2011** | | | |
| Securities available for sale: | | | |
| Change in net unrealized gain/loss during the period | $ 22,350 | $ 8,855 | $ 13,495 |
| Reclassification adjustment for gains included in income | (3,003) | (1,190) | (1,813) |
| Reclassification adjustment for impairment charges included in income | 18 | 7 | 11 |
| | 19,365 | 7,672 | 11,693 |
| Change in net actuarial gain/loss and prior service benefit (cost) on defined benefit pension and post-retirement plans | (9,979) | (3,953) | (6,026) |
| Other comprehensive income | $ 9,386 | $ 3,719 | 5,667 |
| Net income | | | 22,799 |
| Comprehensive income | | | $ 28,466 |
| **2010** | | | |
| Securities available for sale: | | | |
| Change in net unrealized gain/loss during the period | $ (16) | $ 19 | $ (35) |
| Reclassification adjustment for gains included in income | (169) | (67) | (102) |
| Reclassification adjustment for impairment charges included in income | 594 | 235 | 359 |
| | 409 | 187 | 222 |
| Change in net actuarial gain/loss and prior service benefit (cost) on defined benefit pension and post-retirement plans | (2,192) | (950) | (1,242) |
| Other comprehensive loss | $ (1,783) | $ (763) | (1,020) |
| Net income | | | 21,287 |
| Comprehensive income | | | $ 20,267 |
| **2009** | | | |
| Securities available for sale: | | | |
| Change in net unrealized gain/loss during the period | $ (4,186) | $ (1,619) | $ (2,567) |
| Reclassification adjustment for gains included in income | (3,429) | (1,327) | (2,102) |
| Reclassification adjustment for impairment charges included in income | 4,666 | 1,805 | 2,861 |
| | (2,949) | (1,141) | (1,808) |
| Change in net actuarial gain/loss and prior service benefit (cost) on defined benefit pension and post-retirement plans | 3,457 | 1,338 | 2,119 |
| Other comprehensive income | $ 508 | $ 197 | 311 |
| Net income | | | 14,441 |
| Comprehensive income | | | $ 14,752 |

The components of accumulated other comprehensive income (loss), net of tax, as of December 31 were as follows (in thousands):

| | 2011 | 2010 |
|---|---|---|
| Net actuarial loss and prior service cost on defined benefit pension and post-retirement plans | $ (12,625) | $ (6,599) |
| Net unrealized gain on securities available for sale | 13,570 | 1,877 |
| | $ 945 | $ (4,722) |

## (13.) SHARE-BASED COMPENSATION

The Company maintains certain stock-based compensation plans, approved by the Company's shareholders that are administered by the Board, or the Management Development and Compensation Committee of the Board. In May 2009, the shareholders of the Company approved two share-based compensation plans, the 2009 Management Stock Incentive Plan ("Management Plan") and the 2009 Directors' Stock Incentive Plan ("Director's Plan"). An aggregate of 690,000 shares has been reserved for issuance by the Company under the terms of the Management Plan pursuant to the grant of incentive stock options (not to exceed 500,000 shares), non-qualified stock options and restricted stock grants, all which are defined in the plan. An aggregate of 250,000 shares has been reserved for issuance by the Company under the terms of the Director's Plan pursuant to the grant of non-qualified stock options and restricted stock grants, all which are defined in the plan. Under both plans, for purposes of calculating the number of shares of common stock available for issuance, each share of common stock granted pursuant to a restricted stock grant shall count as 1.64 shares of common stock. As of December 31, 2011, there were approximately 213,000 and 451,000 shares available for grant under the Director's Plan and Management Plan, respectively, of which 61% were available for issuance as restricted stock grants.

Under the Management Plan and the Director's Plan (the "Plans"), the Board (or the Compensation Committee) may establish and prescribe grant guidelines including various terms and conditions for the granting of stock-based compensation. For stock options, the exercise price of each option equals the market price of the Company's stock on the date of the grant. All options expire after a period of ten years from the date of grant and generally become fully exercisable over a period of 3 to 5 years from the grant date. When option recipients exercise their options, the Company issues shares from treasury stock and records the proceeds as additions to capital. For restricted stock, shares generally vest over 2 to 3 years from the grant date. Vesting of the shares may be based on years of service, established performance measures or both. If restricted stock grants are forfeited before they vest, the shares are reacquired into treasury stock.

The share-based compensation plans were established to allow for the granting of compensation awards to attract, motivate and retain employees, executive officers and non-employee directors who contribute to the success and profitability of the Company and to give such persons a proprietary interest in the Company, thereby enhancing their personal interest in the Company's success.

The share-based compensation expense for the years ended December 31 was as follows (in thousands):

| | 2011 | 2010 | 2009 |
|---|---|---|---|
| Stock options: | | | |
| Management Stock Incentive Plan | $ 55 | $ 110 | $ 222 |
| Director Stock Incentive Plan | 14 | 43 | 46 |
| Total stock option expense | 69 | 153 | 268 |
| Restricted stock awards: | | | |
| Management Stock Incentive Plan | 917 | 761 | 488 |
| Director Stock Incentive Plan | 119 | 117 | 98 |
| Total restricted stock award expense | 1,036 | 878 | 586 |
| Total share-based compensation | $ 1,105 | $ 1,031 | $ 854 |

The Company uses the Black-Scholes valuation method to estimate the fair value of its stock option awards. There were no stock options awarded during 2011, 2010 or 2009. The following is a summary of stock option activity for the year ended December 31, 2011 (dollars in thousands, except per share amounts):

| | Number of Options | Weighted Average Exercise Price | Weighted Average Remaining Contractual Term | Aggregate Intrinsic Value |
|---|---|---|---|---|
| Outstanding at beginning of year | 409,893 | $ 20.64 | | |
| Granted | — | — | | |
| Exercised | (6,357) | 14.26 | | |
| Forfeited | (550) | 15.85 | | |
| Expired | (34,928) | 21.28 | | |
| Outstanding at end of year | 368,058 | $ 20.70 | 3.65 years | $ 9 |
| Exercisable at end of year | 361,033 | $ 20.79 | 3.60 years | $ 7 |

**(13.) SHARE-BASED COMPENSATION (Continued)**

As of December 31, 2011, there was $13 thousand of unrecognized compensation expense related to unvested stock options, all of which is expected to be recognized during 2012.

The aggregate intrinsic value (the amount by which the market price of the stock on the date of exercise exceeded the market price of the stock on the date of grant) of option exercises for the years ended December 31, 2011, 2010 and 2009 was $31 thousand, $59 thousand, and $1 thousand, respectively. The total cash received as a result of option exercises under stock compensation plans for the years ended December 31, 2011, 2010 and 2009 was $91 thousand, $216 thousand, and $14 thousand, respectively. The tax benefits realized in connection with these stock option exercises were not significant.

The following is a summary of restricted stock award activity for the year ended December 31, 2011:

| | Number of Shares | Weighted Average Market Price at Grant Date |
|---|---|---|
| Outstanding at beginning of year | 150,796 | $ 12.76 |
| Granted | 53,070 | 18.88 |
| Vested | (35,212) | 14.38 |
| Forfeited | (2,000) | 15.44 |
| Outstanding at end of year | 166,654 | $ 14.34 |

As of December 31, 2011, there was $804 thousand of unrecognized compensation expense related to unvested restricted stock awards that is expected to be recognized over a weighted average period of 1.48 years.

**(14.) INCOME TAXES**

Total income tax expense was allocated as follows for the years ended December 31 (in thousands):

| | 2011 | 2010 | 2009 |
|---|---|---|---|
| Income tax expense | $ 11,415 | $ 9,352 | $ 6,140 |
| Shareholder's equity | 3,718 | (763) | 197 |

The income tax expense (benefit) for the years ended December 31 consisted of the following (in thousands):

| | 2011 | 2010 | 2009 |
|---|---|---|---|
| Current tax expense (benefit): | | | |
| Federal | $ 3,747 | $ 5,781 | $ (1,355) |
| State | 1,158 | 1,103 | 25 |
| Total current tax expense (benefit) | 4,905 | 6,884 | (1,330) |
| Deferred tax expense (benefit): | | | |
| Federal | 5,584 | 2,852 | 6,189 |
| State | 926 | (384) | 1,281 |
| Total deferred tax expense | 6,510 | 2,468 | 7,470 |
| Total income tax expense | $ 11,415 | $ 9,352 | $ 6,140 |

**(14.) INCOME TAXES (Continued)**

Income tax expense differed from the statutory federal income tax rate for the years ended December 31 as follows:

| | 2011 | 2010 | 2009 |
|---|---|---|---|
| Statutory federal tax rate | 35.0% | 35.0% | 34.0% |
| Increase (decrease) resulting from: | | | |
| Tax exempt interest income | (4.3) | (4.2) | (8.6) |
| Non-taxable earnings on company owned life insurance | (1.5) | (1.3) | (1.8) |
| State taxes, net of federal tax benefit | 4.0 | 1.5 | 4.2 |
| Nondeductible expenses | 0.4 | 0.6 | 1.0 |
| Disallowed interest expense | 0.2 | 0.2 | 0.5 |
| Other, net | (0.4) | (1.3) | 0.5 |
| Effective tax rate | 33.4% | 30.5% | 29.8% |

The Company's net deferred tax asset is included in other assets in the Consolidated Statements of Condition. The tax effects of temporary differences that give rise to the deferred tax assets and deferred tax liabilities are as follows at December 31 (in thousands):

| | 2011 | 2010 |
|---|---|---|
| Deferred tax assets: | | |
| Other than temporary impairment of investment securities | $ 11,326 | $ 15,418 |
| Allowance for loan losses | 9,106 | 8,108 |
| Share-based compensation | 1,437 | 1,250 |
| Interest on non-accruing loans | 716 | 781 |
| Accrued pension costs | 538 | — |
| Tax attribute carryforward benefits | 463 | 2,033 |
| Core deposit intangible | 79 | 158 |
| Other | 1,172 | 665 |
| Gross deferred tax assets | 24,837 | 28,413 |
| Deferred tax liabilities: | | |
| Net unrealized gain on securities available for sale | 8,903 | 1,231 |
| Depreciation and amortization | 1,741 | 1,489 |
| Deferred loan origination costs | 930 | 2,263 |
| Loan servicing assets | 781 | 581 |
| Prepaid pension costs | — | 139 |
| Gross deferred tax liabilities | 12,355 | 5,703 |
| Net deferred tax asset | $ 12,482 | $ 22,710 |

The Company recognizes deferred income taxes for the estimated future tax effects of differences between the tax and financial statement bases of assets and liabilities considering enacted tax laws. These differences result in deferred tax assets and liabilities, which are included in other assets in the Company's consolidated statements of condition. The Company also assesses the likelihood that deferred tax assets will be realizable based on, among other considerations, future taxable income and establishes, if necessary, a valuation allowance for those deferred tax assets determined to not likely be realizable. A deferred tax asset valuation allowance is recognized if, based on the weight of available evidence (both positive and negative), it is more likely than not that some portion or all of the deferred tax assets will not be realized. The future realization of deferred tax benefits depends upon the existence of sufficient taxable income within the carry-back and carry-forward periods. Management's judgment is required in determining the appropriate recognition of deferred tax assets and liabilities, including projections of future taxable income.

Based upon the Company's historical and projected future levels of pre-tax and taxable income, the scheduled reversals of taxable temporary differences to offset future deductible amounts, and prudent and feasible tax planning strategies, management believes it is more likely than not that the deferred tax assets will be realized. As such, no valuation allowance has been recorded as of December 31, 2011 or 2010.

The Company and its subsidiaries are subject to federal and New York State ("NYS") income taxes. The federal income tax years currently open for audits are 2007 through 2011. The NYS income tax years currently open for audits are 2009 through 2011.

**(14.) INCOME TAXES (Continued)**

At December 31, 2011, the Company had no federal or NYS net operating loss carryforwards. The Company has federal tax credits of approximately $463 thousand which have an unlimited carryforward period.

The Company's unrecognized tax benefits and changes in unrecognized tax benefits were not significant as of or for the years ended December 31, 2011 and 2010. There were no interest or penalties recorded in the income statement in income tax expense for the year ended December 31, 2011. As of December 31, 2011, there were no amounts accrued for interest or penalties related to uncertain tax positions.

**(15.) EARNINGS PER COMMON SHARE**

The following table presents a reconciliation of the earnings and shares used in calculating basic and diluted EPS for each of the years ended December 31 (in thousands, except per share amounts).

| | 2011 | 2010 | 2009 |
|---|---|---|---|
| Net income available to common shareholders | $ 19,617 | $ 17,562 | $ 10,744 |
| Less: Earnings allocated to participating securities | 38 | 105 | 87 |
| Net income available to common shareholders for EPS | $ 19,579 | $ 17,457 | $ 10,657 |
| | | | |
| Weighted average common shares outstanding: | | | |
| Total shares issued | 13,599 | 11,348 | 11,348 |
| Unvested restricted stock awards | (166) | (154) | (92) |
| Treasury shares | (366) | (427) | (526) |
| Total basic weighted average common shares outstanding | 13,067 | 10,767 | 10,730 |
| | | | |
| Incremental shares from assumed: | | | |
| Exercise of stock options | 3 | 6 | — |
| Vesting of restricted stock awards | 65 | 27 | 39 |
| Exercise of warrant | 22 | 45 | — |
| Total diluted weighted average common shares outstanding | 13,157 | 10,845 | 10,769 |
| | | | |
| Basic earnings per common share | $ 1.50 | $ 1.62 | $ 0.99 |
| Diluted earnings per common share | $ 1.49 | $ 1.61 | $ 0.99 |

For each of the periods presented, average shares subject to the following instruments were excluded from the computation of diluted EPS because the effect would be antidilutive:

| | | | |
|---|---|---|---|
| Stock options | 339 | 353 | 459 |
| Restricted stock awards | — | — | — |
| Warrant | — | — | 378 |
| | 339 | 353 | 837 |

## (16.) EMPLOYEE BENEFIT PLANS

### Defined Benefit Pension Plan

The Company participates in The New York State Bankers Retirement System (the "Plan"), a defined benefit pension plan covering substantially all employees, subject to the limitations related to the plan closure effective December 31, 2006. The benefits are based on years of service and the employee's highest average compensation during five consecutive years of employment. The defined benefit plan was closed to new participants effective December 31, 2006. Only employees hired on or before December 31, 2006 and who met participation requirements on or before January 1, 2008 are eligible to receive benefits.

The following table provides a reconciliation of the changes in the plan's benefit obligations, fair value of assets and a statement of the funded status as of and for the year ended December 31 (in thousands):

| | 2011 | 2010 |
|---|---|---|
| Change in projected benefit obligation: | | |
| Projected benefit obligation at beginning of period | $ 38,381 | $ 33,441 |
| Service cost | 1,756 | 1,633 |
| Interest cost | 2,027 | 1,933 |
| Actuarial loss | 7,939 | 2,969 |
| Benefits paid and plan expenses | (1,800) | (1,595) |
| Projected benefit obligation at end of period | 48,303 | 38,381 |
| Change in plan assets: | | |
| Fair value of plan assets at beginning of period | 38,731 | 33,203 |
| Actual return on plan assets | 12 | 2,823 |
| Employer contributions | 10,000 | 4,300 |
| Benefits paid and plan expenses | (1,800) | (1,595) |
| Fair value of plan assets at end of period | 46,943 | 38,731 |
| Funded (unfunded) status at end of period | $ (1,360) | $ 350 |

The accumulated benefit obligation was $43.3 million and $34.3 million at December 31, 2011 and 2010, respectively.

The Company's funding policy is to contribute, at a minimum, an actuarially determined amount that will satisfy the minimum funding requirements determined under the appropriate sections of Internal Revenue Code. The Company satisfied the minimum required contribution to its pension plan of $1.7 million for the 2012 fiscal year by contributing $10.0 million prior to December 31, 2011.

Estimated benefit payments under the pension plan over the next ten years at December 31, 2011 are as follows (in thousands):

| | |
|---|---|
| 2012 | $ 1,553 |
| 2013 | 1,623 |
| 2014 | 1,733 |
| 2015 | 1,876 |
| 2016 | 2,101 |
| 2017 - 2021 | 12,782 |

Net periodic pension cost consists of the following components for the years ended December 31 (in thousands):

| | 2011 | 2010 | 2009 |
|---|---|---|---|
| Service cost | $ 1,756 | $ 1,633 | $ 1,689 |
| Interest cost on projected benefit obligation | 2,027 | 1,933 | 1,826 |
| Expected return on plan assets | (2,653) | (2,444) | (1,848) |
| Amortization of unrecognized loss | 608 | 458 | 728 |
| Amortization of unrecognized prior service cost | 19 | 11 | 11 |
| Net periodic pension cost | $ 1,757 | $ 1,591 | $ 2,406 |

**(16.) EMPLOYEE BENEFIT PLANS (Continued)**

The actuarial assumptions used to determine the net periodic pension cost were as follows:

| | 2011 | 2010 | 2009 |
|---|---|---|---|
| Weighted average discount rate | 5.38% | 5.89% | 6.03% |
| Rate of compensation increase | 3.00% | 3.50% | 3.50% |
| Expected long-term rate of return | 7.00% | 7.50% | 7.50% |

The actuarial assumptions used to determine the projected benefit obligation were as follows:

| | 2011 | 2010 | 2009 |
|---|---|---|---|
| Weighted average discount rate | 4.27% | 5.38% | 5.89% |
| Rate of compensation increase | 3.00% | 3.00% | 3.50% |

The weighted average discount rate was based upon the projected benefit cash flows and the market yields of high grade corporate bonds that are available to pay such cash flows.

The weighted average expected long term rate of return is estimated based on current trends in the Plan's assets as well as projected future rates of return on those assets and reasonable actuarial assumptions based on the guidance provided by Actuarial Standard of Practice No. 27, "Selection of Economic Assumptions for Measuring Pension Obligations", for long term inflation, and the real and nominal rate of investment return for a specific mix of asset classes. The following assumptions were used in determining the long term rate of return:

| | |
|---|---|
| Equity securities | Dividend discount model, the smoothed earnings yield model and the equity risk premium model |
| Fixed income securities | Current yield-to-maturity and forecasts of future yields |
| Other financial instruments | Comparison of the specific investment's risk to that of fixed income and equity instruments and using judgment |

The long term rate of return considers historical returns. Adjustments were made to historical returns in order to reflect expectations of future returns. These adjustments were due to factor forecasts by economists and long-term U.S. Treasury yields to forecast long-term inflation. In addition forecasts by economists and others for long-term GDP growth were factored into the development of assumptions for earnings growth and per capital income. The Plan's overall investment strategy is to achieve a mix of approximately 97% of investments for long-term growth and 3% for near-term benefit payments with a wide diversification of asset types, fund strategies, and fund managers. The target allocations for Plan assets are shown in the table below. Cash equivalents consist primarily of short term investment funds. Equity securities primarily include investments in common stock and depository receipts. Fixed income securities include corporate bonds, government issues and mortgage backed securities. Other financial instruments primarily include rights and warrants.

**(16.) EMPLOYEE BENEFIT PLANS (Continued)**

Effective September 2011, the Plan revised its investment guidelines. The Plan currently prohibits its investment managers from purchasing any security greater than 5% of the portfolio at the time of purchase or greater than 8% at market value in any one issuer. In addition, the following are prohibited:

| | |
|---|---|
| Equity securities | Short sales<br>Unregistered securities<br>Margin purchases |
| Fixed income securities | Mortgage backed derivatives that have an inverse floating rate coupon or that are interest only securities |
| | Any ABS that is not issued by the U.S. Government or its agencies or its instrumentalities |
| | Generally securities of less than Baa2/BBB quality may not be purchased |
| | Securities of less than A-quality may not in the aggregate exceed 10% of the investment manager's portfolio |
| Other financial instruments | Unhedged currency exposure in countries not defined as "high income economies" by the World Bank |

Prior to September 2011 investments in emerging countries as defined by the Morgan Stanley Emerging Markets Index and structured notes were prohibited.

All other investments not prohibited by the Plan are permitted. At December 31, 2011, the Plan holds certain investments which are no longer deemed acceptable to acquire. These positions will be liquidated when the investment managers deem that such liquidation is in the best interest of the Plan.

| | 2012 Target Allocation | Percentage of Plan Assets at December 31, | | Weighted Average Expected Long-term Rate of Return |
|---|---|---|---|---|
| | | 2011 | 2010 | |
| Asset category: | | | | |
| Cash equivalents | 0 – 20% | 10.6% | 11.2% | 0.39% |
| Equity securities | 40 – 60 | 47.9 | 48.2 | 4.62 |
| Fixed income securities | 40 – 60 | 41.5 | 40.6 | 1.85 |
| Other financial instruments | 0 – 5 | — | — | — |

**(16.) EMPLOYEE BENEFIT PLANS (Continued)**

Assets are segregated by the level of the valuation inputs within the fair value hierarchy established by ASC Topic 820 utilized to measure fair value (see Note 17—Fair Value Measurements). There were no assets classified as Level 3 assets during the years ended December 31, 2011 and 2010. The major categories of Plan assets measured at fair value on a recurring basis are presented in the following table (in thousands).

| | Level 1 Inputs | Level 2 Inputs | Level 3 Inputs | Total Fair Value |
|---|---|---|---|---|
| **December 31, 2011:** | | | | |
| Cash equivalents: | | | | |
| Foreign currencies | $ 81 | $ — | $ — | $ 81 |
| Short term investment funds | — | 4,901 | — | 4,901 |
| Total cash equivalents | 81 | 4,901 | — | 4,982 |
| Equity securities: | | | | |
| U.S. Large Cap | 13,993 | — | — | 13,993 |
| U.S. Mid Cap | 1,903 | — | — | 1,903 |
| U.S. Small Cap | 44 | — | — | 44 |
| International | 6,553 | — | — | 6,553 |
| Total equity securities | 22,493 | — | — | 22,493 |
| Fixed income securities: | | | | |
| Corporate bonds: | | | | |
| Rated single A or higher by S&P | — | 1,949 | — | 1,949 |
| Rated below single A by S&P | — | 2,281 | — | 2,281 |
| Government issues | — | 10,651 | — | 10,651 |
| Collateralized mortgage obligations: | | | | |
| Rated single A or higher by S&P | — | 4,233 | — | 4,233 |
| Rated below single A by S&P | — | 354 | — | 354 |
| Total fixed income securities | — | 19,468 | — | 19,468 |
| Total Plan investments | $ 22,574 | $ 24,369 | $ — | $ 46,943 |
| **December 31, 2010:** | | | | |
| Cash equivalents: | | | | |
| Foreign currencies | $ 84 | $ — | $ — | $ 84 |
| Short term investment funds | — | 4,266 | — | 4,266 |
| Total cash equivalents | 84 | 4,266 | — | 4,350 |
| Equity securities: | | | | |
| U.S. Large Cap | 10,800 | — | — | 10,800 |
| U.S. Mid Cap | 1,103 | — | — | 1,103 |
| U.S. Small Cap | 82 | — | — | 82 |
| International | 6,698 | — | — | 6,698 |
| Total equity securities | 18,683 | — | — | 18,683 |
| Fixed income securities: | | | | |
| Corporate bonds: | | | | |
| Rated single A or higher by S&P | — | 2,113 | — | 2,113 |
| Rated below single A by S&P | — | 1,483 | — | 1,483 |
| Government issues | — | 11,259 | — | 11,259 |
| Collateralized mortgage obligations: | | | | |
| Rated single A or higher by S&P | — | 582 | — | 582 |
| Rated below single A by S&P | — | 261 | — | 261 |
| Total fixed income securities | — | 15,698 | — | 15,698 |
| Total Plan investments | $ 18,767 | $ 19,964 | $ — | $ 38,731 |

**(16.) EMPLOYEE BENEFIT PLANS (Continued)**

At December 31, 2011 the portfolio was managed by two investment firms, with control of the portfolio split approximately 46% and 52% under the control of the investment managers with the remaining 2% under the direct control of the Plan. A portfolio concentration in the State Street Bank & Trust Co. Short Term Investment Fund of 10% and 11% existed at December 31, 2011 and 2010, respectively.

**Postretirement Benefit Plan**

An entity acquired by the Company provided health and dental care benefits to retired employees who met specified age and service requirements through a postretirement health and dental care plan in which both the acquired entity and the retirees shared the cost. The plan provided for substantially the same medical insurance coverage as for active employees until their death and was integrated with Medicare for those retirees aged 65 or older. In 2001, the plan's eligibility requirements were amended to curtail eligible benefit payments to only retired employees and active participants who were fully vested under the Plan. In 2003, retirees under age 65 began contributing to health coverage at the same cost-sharing level as that of active employees. The retirees aged 65 or older were offered new Medicare supplemental plans as alternatives to the plan historically offered. The cost sharing of medical coverage was standardized throughout the group of retirees aged 65 or older. In addition, to be consistent with the administration of the Company's dental plan for active employees, all retirees who continued dental coverage began paying the full monthly premium. The accrued liability included in other liabilities in the consolidated statements of financial condition related to this plan amounted to $122 thousand and $162 thousand as of December 31, 2011 and 2010, respectively. The postretirement expense for the plan that was included in salaries and employee benefits in the consolidated statements of income was not significant for the years ended December 31, 2011, 2010 and 2009. The plan is not funded.

The components of accumulated other comprehensive loss related to the defined benefit plan and postretirement benefit plan, on a pre-tax basis as of December 31 are summarized below (in thousands):

| | 2011 | 2010 |
|---|---|---|
| **Defined benefit plan:** | | |
| Net actuarial loss | $ (21,160) | $ (11,188) |
| Prior service cost | (113) | (132) |
| | (21,273) | (11,320) |
| **Postretirement benefit plan:** | | |
| Net actuarial loss | (210) | (252) |
| Prior service credit | 575 | 643 |
| | 365 | 391 |
| Total recognized in accumulated other comprehensive loss | $ (20,908) | $ (10,929) |

Changes in plan assets and benefit obligations recognized in other comprehensive income (loss) on a pre-tax basis during the years ended December 31 are as follows (in thousands):

| | 2011 | 2010 |
|---|---|---|
| **Defined benefit plan:** | | |
| Net actuarial loss | $ (10,580) | $ (2,590) |
| Amortization of net loss | 608 | 458 |
| Amortization of prior service cost | 19 | 11 |
| | (9,953) | (2,121) |
| **Postretirement benefit plan:** | | |
| Net actuarial gain (loss) | 42 | (4) |
| Amortization of prior service credit | (68) | (67) |
| | (26) | (71) |
| Total recognized in other comprehensive income (loss) | $ (9,979) | $ (2,192) |

For the year ending December 31, 2012, the estimated net loss and prior service cost for the plan that will be amortized from accumulated other comprehensive income into net periodic benefit cost is $1.4 million and $20 thousand, respectively.

**(16.) EMPLOYEE BENEFIT PLANS (Continued)**

**Defined Contribution Plan**

Employees that meet certain age and service requirements are eligible to participate in the Company sponsored 401(k) plan. Under the plan, participants may make contributions, in the form of salary deferrals, up to the maximum Internal Revenue Code limit. The Company matches a participant's contributions up to 4.5% of compensation, calculated as 100% of the first 3% of compensation and 50% of the next 3% of compensation deferred by the participant. The Company may also make additional discretionary matching contributions, although no such additional discretionary contributions were made in 2011, 2010 or 2009. The expense included in salaries and employee benefits in the consolidated statements of income for this plan amounted to $1.0 million, $936 thousand and $914 thousand in 2011, 2010 and 2009, respectively.

**Supplemental Executive Retirement Plans**

The Company has a non-qualified Supplemental Executive Retirement Plan ("SERP") covering three former executives. At December 31, 2011, there was a $1.0 million unfunded pension liability related to the SERP. SERP expense was $67 thousand, $262 thousand, and $648 thousand for 2011, 2010 and 2009, respectively.

**(17.) FAIR VALUE MEASUREMENTS**

**Determination of Fair Value – Assets Measured at Fair Value on a Recurring and Nonrecurring Basis**

**Valuation Hierarchy**

The fair value of an asset or liability is the price that would be received to sell that asset or paid to transfer that liability in an orderly transaction occurring in the principal market (or most advantageous market in the absence of a principal market) for such asset or liability. ASC Topic 820, "Fair Value Measurements and Disclosures," establishes a fair value hierarchy for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy is as follows:

- **Level 1** —Unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.
- **Level 2** —Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These might include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (such as interest rates, volatilities, prepayment speeds, credit risks, etc.) or inputs that are derived principally from or corroborated by market data by correlation or other means.
- **Level 3** —Unobservable inputs for determining the fair values of assets or liabilities that reflect an entity's own assumptions about the assumptions that market participants would use in pricing the assets or liabilities.

In general, fair value is based upon quoted market prices, where available. If such quoted market prices are not available, fair value is based upon internally developed models that primarily use, as inputs, observable market-based parameters. Valuation adjustments may be made to ensure that financial instruments are recorded at fair value. These adjustments may include amounts to reflect counterparty credit quality and the company's creditworthiness, among other things, as well as unobservable parameters. Any such valuation adjustments are applied consistently over time. The Company's valuation methodologies may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. While management believes the Company's valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date. Furthermore, the reported fair value amounts have not been comprehensively revalued since the presentation dates, and therefore, estimates of fair value after the balance sheet date may differ significantly from the amounts presented herein. A more detailed 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.

**(17.) FAIR VALUE MEASUREMENTS (Continued)**

**Investment securities available for sale:** Pooled trust preferred securities are reported at fair value utilizing Level 3 inputs. Fair values for these securities are determined through the use of internal valuation methodologies appropriate for the specific asset, which may include the use of a discounted expected cash flow analysis or the use of broker quotes. Other securities classified as available for sale are reported at fair value utilizing Level 2 inputs. For these securities, the Company obtains fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include 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 conditions, among other things.

**Loans held for sale:** The fair value of loans held for sale is determined using quoted secondary market prices and investor commitments. Loans held for sale are classified as Level 2 in the fair value hierarchy.

**Collateral dependent impaired loans:** The fair value of impaired loans with specific allocations of the allowance for loan losses is generally based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are typically significant and result in a Level 3 classification of the inputs for determining fair value.

**Other real estate owned (Foreclosed assets):** Nonrecurring adjustments to certain commercial and residential real estate properties classified as other real estate owned are measured at the lower of carrying amount or fair value, less costs to sell. Fair values are generally based on third party appraisals of the property, resulting in a Level 3 classification. In cases where the carrying amount exceeds the fair value, less costs to sell, an impairment loss is recognized.

**Mortgage servicing rights:** Mortgage servicing rights do not trade in an active market with readily observable market data. As a result, the Company estimates the fair value of mortgage servicing rights by using a discounted cash flow model to calculate the present value of estimated future net servicing income. The assumptions used in the discounted cash flow model are those that we believe market participants would use in estimating future net servicing income, including estimates of loan prepayment rates, servicing costs, ancillary income, impound account balances, and discount rates. Significant assumptions in the valuation of mortgage servicing rights include changes in interest rates, estimated loan repayment rates, and the timing of cash flows, among other factors. Mortgage servicing rights are classified as Level 3 measurements due to the use of significant unobservable inputs, as well as significant management judgment and estimation.

**Assets Measured at Fair Value**

The following table presents for each of the fair-value hierarchy levels the Company's assets that are measured at fair value on a recurring and non-recurring basis as of December 31, 2011 (in thousands).

| | Level 1 Inputs | Level 2 Inputs | Level 3 Inputs | Total Fair Value |
|---|---|---|---|---|
| **Measured on a recurring basis:** | | | | |
| Securities available for sale: | | | | |
| U.S. Government agencies and government sponsored enterprises | $ — | $ 97,712 | $ — | $ 97,712 |
| State and political subdivisions | — | 124,424 | — | 124,424 |
| Mortgage-backed securities | — | 403,685 | — | 403,685 |
| Asset-backed securities: | | | | |
| Trust preferred securities | — | — | 1,636 | 1,636 |
| Other | — | 61 | — | 61 |
| | $ — | $ 625,882 | $ 1,636 | $ 627,518 |
| **Measured on a nonrecurring basis:** | | | | |
| Loans: | | | | |
| Loans held for sale | $ — | $ 2,410 | $ — | $ 2,410 |
| Collateral dependent impaired loans | — | — | 2,160 | 2,160 |
| Other assets: | | | | |
| Mortgage servicing rights | — | — | 1,973 | 1,973 |
| Other real estate owned | — | — | 475 | 475 |
| | $ — | $ 2,410 | $ 4,608 | $ 7,018 |

**(17.) FAIR VALUE MEASUREMENTS (Continued)**

The following table presents for each of the fair-value hierarchy levels the Company's assets that are measured at fair value on a recurring and non-recurring basis as of December 31, 2010 (in thousands).

| | Level 1 Inputs | Level 2 Inputs | Level 3 Inputs | Total Fair Value |
|---|---|---|---|---|
| **Measured on a recurring basis:** | | | | |
| Securities available for sale: | | | | |
| U.S. Government agencies and government sponsored enterprises | $ — | $ 140,784 | $ — | $ 140,784 |
| State and political subdivisions | — | 105,666 | — | 105,666 |
| Mortgage-backed securities | — | 419,281 | — | 419,281 |
| Asset-backed securities: | | | | |
| Trust preferred securities | — | — | 572 | 572 |
| Other | — | 65 | — | 65 |
| | $ — | $ 665,796 | $ 572 | $ 666,368 |
| **Measured on a nonrecurring basis:** | | | | |
| Loans: | | | | |
| Loans held for sale | $ — | $ 3,138 | $ — | $ 3,138 |
| Collateral dependent impaired loans | — | — | 2,457 | 2,457 |
| Other assets: | | | | |
| Mortgage servicing rights | — | — | 1,467 | 1,467 |
| Other real estate owned | — | — | 741 | 741 |
| | $ — | $ 3,138 | $ 4,665 | $ 7,803 |

There were no liabilities measured at fair value on a recurring or nonrecurring basis during the years ended December 31, 2011 and 2010.

**Changes in Level 3 Fair Value Measurements**

The reconciliation for all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the years ended December 31 is as follows (in thousands):

| | 2011 | 2010 |
|---|---|---|
| Securities available for sale (Level 3), beginning of year | $ 572 | $ 1,015 |
| Transfers into Level 3 | — | — |
| Sales | (2,478) | — |
| Principal paydowns and other | (53) | 263 |
| Total gains (losses) realized/unrealized: | | |
| Included in earnings | 2,263 | (526) |
| Included in other comprehensive income | 1,332 | (180) |
| Securities available for sale (Level 3), end of year | $ 1,636 | $ 572 |

**(17.) FAIR VALUE MEASUREMENTS (Continued)**

**Fair Value of Financial Instruments**

The Fair Value of Financial Instruments Subsection of the ASC requires disclosure of the fair value of financial assets and financial liabilities, including those financial assets and financial liabilities that are not measured and reported at fair value on a recurring basis or non-recurring basis.

The following discussion describes the valuation methodologies used for assets and liabilities measured or disclosed at fair value. The techniques utilized in estimating the fair values of financial instruments are reliant on the assumptions used, including discount rates and estimates of the amount and timing of future cash flows. Care should be exercised in deriving conclusions about our business, its value or financial position based on the fair value information of financial instruments presented below.

Fair value estimates are made at a specific point in time, based on available market information and judgments about the financial instrument, including estimates of timing, amount of expected future cash flows and the credit standing of the issuer. Such estimates do not consider the tax impact of the realization of unrealized gains or losses. In some cases, the fair value estimates cannot be substantiated by comparison to independent markets. In addition, the disclosed fair value may not be realized in the immediate settlement of the financial instrument.

The estimated fair value approximates carrying value for cash and cash equivalents, FHLB and FRB stock, company owned life insurance, accrued interest receivable, short-term borrowings and accrued interest payable. Fair value estimates for other financial instruments are discussed below.

***Loans held for sale.*** The fair value is based on estimates, quoted market prices and investor commitments.

***Loans.*** For variable rate loans that re-price frequently, fair value approximates carrying amount. The fair value for fixed rate loans is estimated through discounted cash flow analysis using interest rates currently being offered on loans with similar terms and credit quality. For criticized and classified loans, fair value is estimated by discounting expected cash flows at a rate commensurate with the risk associated with the estimated cash flows, or estimates of fair value discounts based on observable market information.

***Deposits.*** The fair values for demand accounts, money market and savings deposits are equal to their carrying amounts. The fair values of certificates of deposit are estimated using a discounted cash flow approach that applies prevailing market interest rates for similar maturity instruments.

***Long-term borrowings (excluding junior subordinated debentures).*** The fair value for long-term borrowings is estimated using a discounted cash flow approach that applies prevailing market interest rates for similar maturity instruments.

***Junior subordinated debentures.*** The fair value for the junior subordinated debentures is estimated using a discounted cash flow approach that applies prevailing market interest rates for similar maturity instruments.

The fair value of a financial instrument is the current amount that would be exchanged between willing parties, other than in a forced liquidation. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Company's various financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument. The accounting guidelines exclude certain financial instruments and all non-financial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented at December 31, 2011 and December 31, 2010 may not necessarily represent the underlying fair value of the Company.

**(17.) FAIR VALUE MEASUREMENTS (Continued)**

The carrying values and fair values of financial instruments as of December 31 are as follows (in thousands):

| | December 31, 2011 | | December 31, 2010 | |
|---|---|---|---|---|
| | Carrying Amount | Estimated Fair Value | Carrying Amount | Estimated Fair Value |
| **Financial assets:** | | | | |
| Cash and cash equivalents | $ 57,583 | $ 57,583 | $ 39,058 | $ 39,058 |
| Securities available for sale | 627,518 | 627,518 | 666,368 | 666,368 |
| Securities held to maturity | 23,297 | 23,964 | 28,162 | 28,849 |
| Loans held for sale | 2,410 | 2,442 | 3,138 | 3,138 |
| Loans | 1,461,516 | 1,493,159 | 1,325,524 | 1,388,787 |
| Accrued interest receivable | 7,655 | 7,655 | 7,613 | 7,613 |
| FHLB and FRB stock | 10,674 | 10,674 | 6,353 | 6,353 |
| **Financial liabilities:** | | | | |
| Demand, savings and money market deposits | 1,230,923 | 1,230,923 | 1,143,136 | 1,143,136 |
| Certificate of deposit | 700,676 | 702,720 | 739,754 | 740,440 |
| Short-term borrowings | 150,698 | 150,698 | 77,110 | 77,110 |
| Long-term borrowings (excluding junior subordinated debentures) | — | — | 10,065 | 10,244 |
| Junior subordinated debentures | — | — | 16,702 | 10,564 |
| Accrued interest payable | 5,207 | 5,207 | 7,620 | 7,620 |

**(18.) PARENT COMPANY FINANCIAL INFORMATION**

Condensed financial statements pertaining only to the Parent are presented below (in thousands).

**Condensed Statements of Condition**

| | December 31, | |
|---|---|---|
| | 2011 | 2010 |
| Assets: | | |
| Cash and due from subsidiary | $ 11,621 | $ 23,894 |
| Investment in and receivables due from subsidiary | 223,577 | 202,754 |
| Other assets | 4,337 | 4,623 |
| Total assets | $ 239,535 | $ 231,271 |
| Liabilities and shareholders' equity: | | |
| Junior subordinated debentures | $ — | $ 16,702 |
| Other liabilities | 2,341 | 2,425 |
| Shareholders' equity | 237,194 | 212,144 |
| Total liabilities and shareholders' equity | $ 239,535 | $ 231,271 |

**(18.) PARENT COMPANY FINANCIAL INFORMATION (Continued)**

**Condensed Statements of Income**

| | Years ended December 31, | | |
|---|---|---|---|
| | 2011 | 2010 | 2009 |
| Dividends from subsidiary and associated companies | $ 9,233 | $ 23,151 | $ 5,051 |
| Management and service fees from subsidiary | 1,161 | 1,163 | 603 |
| Other income (loss) | 78 | (134) | 182 |
| Total income | 10,472 | 24,180 | 5,836 |
| Operating expenses | 3,787 | 4,005 | 4,436 |
| Loss on extinguishment of debt | 1,083 | — | — |
| Total expenses | 4,870 | 4,005 | 4,436 |
| Income before income tax benefit and equity in undistributed earnings(excess distributions) of subsidiary | 5,602 | 20,175 | 1,400 |
| Income tax benefit | 1,539 | 1,323 | 1,286 |
| Income before equity in undistributed earnings (excess distributions) of subsidiary | 7,141 | 21,498 | 2,686 |
| Equity in undistributed earnings (excess distributions) of subsidiary | 15,658 | (211) | 11,755 |
| Net income | $ 22,799 | $ 21,287 | $ 14,441 |

**Condensed Statements of Cash Flows**

| | Years ended December 31, | | |
|---|---|---|---|
| | 2011 | 2010 | 2009 |
| Cash flows from operating activities: | | | |
| Net income | $ 22,799 | $ 21,287 | $ 14,441 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Equity in (undistributed earnings) excess distributions of subsidiary | (15,658) | 211 | (11,755) |
| Depreciation and amortization | 116 | 193 | 318 |
| Share-based compensation | 1,105 | 1,031 | 854 |
| Decrease in other assets | 771 | 980 | 797 |
| (Decrease) increase in other liabilities | (534) | 8 | (230) |
| Net cash provided by operating activities | 8,599 | 23,710 | 4,425 |
| Cash flows from investing activities: | | | |
| Purchase of investment assets, net of disposals | — | — | (1,323) |
| Capital investment in subsidiary | — | — | (15,000) |
| Net cash used in investing activities | — | — | (16,323) |
| Cash flows from financing activities: | | | |
| Redemption of junior subordinated debentures | (16,702) | — | — |
| Proceeds from issuance of preferred and common shares, net of issuance costs | 43,127 | — | (68) |
| Purchase of preferred and common shares | (37,764) | (69) | — |
| Proceeds from issuance of common stock warrant | (2,080) | — | — |
| Proceeds from stock options exercised | 91 | 216 | 15 |
| Dividends paid | (7,564) | (7,690) | (7,485) |
| Other | 20 | — | — |
| Net cash used in financing activities | (20,872) | (7,543) | (7,538) |
| Net (decrease) increase in cash and cash equivalents | (12,273) | 16,167 | (19,436) |
| Cash and cash equivalents as of beginning of year | 23,894 | 7,727 | 27,163 |
| Cash and cash equivalents as of end of the year | $ 11,621 | $ 23,894 | $ 7,727 |

**(19.) SUBSEQUENT EVENT (Unaudited)**

On January 19, 2012, Five Star Bank entered into an agreement to acquire four retail banking branches currently owned by HSBC Bank USA, N.A. and four retail banking branches currently owned by First Niagara Bank, N.A. The deposits associated with these branches total approximately $376 million, while loans total approximately $94 million. The transactions are subject to customary closing conditions, including regulatory approvals, and are expected to close by the end of the third quarter of 2012.

## ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

## IT EM 9A. CONTROLS AND PROCEDURES

### Effectiveness of Controls and Procedures

As of the end of the period covered by this report, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer (Principal Executive Officer) and Chief Financial Officer (Principal Accounting Officer), of the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Rule 13a-15(b), as adopted by the Securities and Exchange Commission ("SEC") under the Securities Exchange Act of 1934 ("Exchange Act"). Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective as of the end of the period covered by this Annual Report on Form 10-K.

Disclosure controls and procedures are the controls and other procedures that are designed to ensure that information required to be disclosed in the reports that the Company files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed in the reports that the Company files or submits under the Exchange Act is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined effective can provide only reasonable assurance with respect to financial statement preparation and presentation.

### Management Report on Internal Control over Financial Reporting and Attestation Report of Independent Registered Public Accounting Firm

Management of Financial Institutions, Inc. (the Company) is responsible for establishing and maintaining adequate internal control over financial reporting. Management assessed the Company's internal control over financial reporting based on criteria established in the Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on this assessment, management has concluded that, as of December 31, 2011, the Company maintained effective internal control over financial reporting. Management's Report on Internal Control over Financial Reporting is included under Item 8 "Financial Statements and Supplementary Data" in Part II of this Form 10-K.

KPMG LLP, an independent registered public accounting firm, has audited the consolidated financial statements included in this Annual Report on Form 10-K, and has issued an attestation report on the effectiveness of the Company's internal control over financial reporting. The Report of Independent Registered Public Accounting Firm that attests the effectiveness of internal control over financial reporting is included under Item 8 "Financial Statements and Supplementary Data" in Part II of this Form 10-K.

### Changes in Internal Control over Financial Reporting

There were no changes in the Company's internal control over financial reporting that occurred during the quarter ended December 31, 2011 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## I TEM 9B. OTHER INFORMATION

Not applicable.

## P ART III

### IT EM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

In response to this Item, the information set forth in the Company's Proxy Statement for its 2012 Annual Meeting of Shareholders (the "2012 Proxy Statement") to be filed within 120 days following the end of the Company's fiscal year, under the headings "Election of Directors," "Business Experience and Qualification of Directors," and "Section 16(a) Beneficial Ownership Reporting Compliance" is incorporated herein by reference.

The information under the heading "Executive Officers of the Registrant" in Part I, Item 1 of this Form 10-K is also incorporated herein by reference.

Information concerning the Company's Audit Committee and the Audit Committee's financial expert is set forth under the caption "Corporate Governance Information" in the 2012 Proxy Statement and is incorporated herein by reference.

The Company has adopted a Code of Business Conduct and Ethics that applies to its principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions. The Code of Business Conduct and Ethics is posted on the Company's internet website at www.fiiwarsaw.com under the Corporate Overview/Governance Documents tabs if the Investor Relations drop down menu. In addition, the Company will provide a copy of the Code of Business Conduct and Ethics to anyone, without charge, upon request addressed to Director of Human Resources at Financial Institutions, Inc., 220 Liberty Street, Warsaw, NY 14569. The Company intends to disclose any amendment to, or waiver from, a provision of its Code of Business Conduct and Ethics that applies to the Company's principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions, and that relates to any element of the Code of Business Conduct and Ethics, by posting such information on the Company's website.

### I TEM 11. EXECUTIVE COMPENSATION

In response to this Item, the information set forth in the 2012 Proxy Statement under the heading "Elements of Executive Compensation" is incorporated herein by reference.

### I TEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

In response to this Item, the information set forth in the 2012 Proxy Statement under the heading "Beneficial Ownership of Common Stock" is incorporated herein by reference. The information under the heading "Equity Compensation Plan Information" in Part II, Item 5 of this Form 10-K is also incorporated herein by reference.

### ITE M 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

In response to this Item, the information set forth in the 2012 Proxy Statement under the headings "Certain Relationships and Related Party Transactions" and "Corporate Governance Information" is incorporated herein by reference.

### I TEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

In response to this Item, the information set forth in the 2012 Proxy Statement under the headings "Audit Committee Report" and "Independent Registered Public Accounting Firm" is incorporated herein by reference.

## PA RT IV

## I TEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

### (a ) FINANCIAL STATEMENTS

Reference is made to the Index to Consolidated Financial Statements of Financial Institutions, Inc. and Subsidiaries under Item 8 “Financial Statements and Supplementary Data” in Part II of this Form 10-K.

### (b ) EXHIBITS

The following is a list of all exhibits filed or incorporated by reference as part of this Report.

| Exhibit Number | Description | Location |
|---|---|---|
| 3.1 | Amended and Restated Certificate of Incorporation of the Company | Incorporated by reference to Exhibits 3.1, 3.2 and 3.3 of the Form 10-K for the year ended December 31, 2008, dated March 12, 2009 |
| 3.2 | Amended and Restated Bylaws of the Company | Incorporated by reference to Exhibit 3.4 of the Form 10-K for the year ended December 31, 2008, dated March 12, 2009 |
| 4.1 | Warrant to Purchase Common Stock, dated December 23, 2008 issued by the Registrant to the United States Department of the Treasury | Incorporated by reference to Exhibit 4.2 of the Form 8-K, dated December 24, 2008 |
| 10.1 | 1999 Management Stock Incentive Plan | Incorporated by reference to Exhibit 10.1 of the S-1 Registration Statement |
| 10.2 | Amendment Number One to the FII 1999 Management Stock Incentive Plan | Incorporated by reference to Exhibit 10.1of the Form 8-K, dated July 28, 2006 |
| 10.3 | Form of Non-Qualified Stock Option Agreement Pursuant to the FII 1999 Management Stock Incentive Plan | Incorporated by reference to Exhibit 10.2 of the Form 8-K, dated July 28, 2006 |
| 10.4 | Form of Restricted Stock Award Agreement Pursuant to the FII 1999 Management Stock Incentive Plan | Incorporated by reference to Exhibit 10.3 of the Form 8-K, dated July 28, 2006 |
| 10.5 | Form of Restricted Stock Award Agreement Pursuant to the FII 1999 Management Stock Incentive Plan | Incorporated by reference to Exhibit 10.1 of the Form 8-K, dated January 23, 2008 |
| 10.6 | 1999 Directors Stock Incentive Plan | Incorporated by reference to Exhibit 10.2 of the S-1 Registration Statement |
| 10.7 | Amendment to the 1999 Director Stock Incentive Plan | Incorporated by reference to Exhibit 10.7 of the Form 10-K for the year ended December 31, 2008, dated March 12, 2009 |
| 10.8 | 2009 Management Stock Incentive Plan | Incorporated by reference to Exhibit 10.8 of the Form 10-Q for the quarterly period ended June 30, 2009, dated August 5, 2009 |
| 10.9 | 2009 Directors’ Stock Incentive Plan | Incorporated by reference to Exhibit 10.9 of the Form 10-Q for the quarterly period ended June 30, 2009, dated August 5, 2009 |
| 10.10 | Form of Restricted Stock Award Agreement Pursuant to the FII 2009 Management Stock Incentive Plan (Special, one-time Award) | Incorporated by reference to Exhibit 10.1 of the Form 8-K, dated January 19, 2010 |
| 10.11 | Form of Restricted Stock Award Agreement Pursuant to the FII 2009 Management Stock Incentive Plan (LTIP Award) | Incorporated by reference to Exhibit 10.2 of the Form 8-K, dated March 1, 2010 |
| 10.12 | Form of “Service Based” Restricted Stock Award Agreement Pursuant to the FII 2009 Management Stock Incentive Plan | Filed Herewith |

| Exhibit Number | Description | Location |
|---|---|---|
| 10.13 | Form of 2012 Performance Program Master Agreement | Filed Herewith |
| 10.14 | Form of 2012 Performance Program Award Certificate | Filed Herewith |
| 10.15 | Amended Stock Ownership Requirements, dated December 14, 2005 | Incorporated by reference to Exhibit 10.19 of the Form 10-K for the year ended December 31, 2005, dated March 15, 2006 |
| 10.16 | Executive Agreement with Peter G. Humphrey | Incorporated by reference to Exhibit 10.1 of the Form 8-K, dated June 30, 2005 |
| 10.17 | Executive Agreement with Martin K. Birmingham | Incorporated by reference to Exhibit 10.4 of the Form 8-K, dated June 30, 2005 |
| 10.18 | Executive Agreement with John J. Witkowski | Incorporated by reference to Exhibit 10.7 of the Form 8-K, dated September 14, 2005 |
| 10.19 | Executive Agreement with George D. Hagi | Incorporated by reference to Exhibit 10.7 of the Form 8-K, dated February 2, 2006 |
| 10.20 | Voluntary Retirement Agreement with Ronald A. Miller | Incorporated by reference to Exhibit 10.2 of the Form 8-K, dated September 26, 2008 |
| 10.21 | Amendment to Voluntary Retirement Agreement with Ronald A. Miller | Incorporated by reference to Exhibit 10.1 of the Form 8-K, dated March 3, 2010 |
| 10.22 | Letter Agreement, dated December 23, 2008, including the Securities Purchase Agreement-Standard Terms attached thereto, by and between the Company and the United States Department of the Treasury | Incorporated by reference to Exhibit 10.1 of the Form 8-K, dated December 24, 2008 |
| 10.23 | Underwriting Agreement dated March 9, 2011 between Financial Institutions, Inc. and Keefe, Bruyette & Woods, Inc., as representative of the underwriters | Incorporated by reference to Exhibit 1.1 of the Form 8-K, dated March 9, 2011 |
| 10.24 | Assignment, Purchase and Assumption Agreement dated January 19, 2012 between First Niagara Bank, National Association and Five Star Bank | Filed Herewith |
| 10.25 | Purchase and Assumption Agreement dated January 19, 2012 between First Niagara Bank, National Association and Five Star Bank | Filed Herewith |
| 11.1 | Statement of Computation of Per Share Earnings | Incorporated by reference to Note 15 of the Registrant's audited consolidated financial statements under Item 8 filed herewith. |
| 21 | Subsidiaries of Financial Institutions, Inc. | Filed Herewith |
| 23 | Consent of Independent Registered Public Accounting Firm | Filed Herewith |
| 31.1 | Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 - Principal Executive Officer | Filed Herewith |
| 31.2 | Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 - Principal Financial Officer | Filed Herewith |
| 32 | Certification pursuant to18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 | Filed Herewith |
| 99.1 | Certification of Chief Executive Officer pursuant to Section 111 (b)(4) of the Emergency Economic Stabilization Act | Filed Herewith |
| 99.2 | Certification of Chief Financial Officer pursuant to Section 111(b) (4) of the Emergency Economic Stabilization Act | Filed Herewith |

| Exhibit Number | Description | Location |
|---|---|---|
| *101.INS | XBRL Instance Document | |
| *101.SCH | XBRL Taxonomy Extension Schema Document | |
| *101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document | |
| *101.LAB | XBRL Taxonomy Extension Label Linkbase Document | |
| *101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document | |
| *101.DEF | XBRL Taxonomy Extension Definition Linkbase Document | |

* Pursuant to Rule 406T of Regulation S-T, the information in this exhibit shall not be deemed to be "filed" for purposes of Section 18 of the Securities Exchange Act of 1934, or otherwise subject to the liability of that section, and shall not be incorporated by reference into any registration statement, prospectus or other document filed under the Securities Act of 1933, or the Securities Exchange Act of 1934, except as shall be expressly set forth by specific reference in such filings.

## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**FINANCIAL INSTITUTIONS, INC.**

March 9, 2012

By: ***/s/ Peter G. Humphrey***
Peter G. Humphrey
President & Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

| Signatures | Title | Date |
|---|---|---|
| ***/s/ Peter G. Humphrey***<br>Peter G. Humphrey | Director, President and Chief Executive Officer<br>(Principal Executive Officer) | March 9, 2012 |
| ***/s/ Karl F. Krebs***<br>Karl F. Krebs | Executive Vice President and Chief Financial Officer<br>(Principal Financial and Accounting Officer) | March 9, 2012 |
| ***/s/ Karl V. Anderson, Jr.***<br>Karl V. Anderson, Jr. | Director | March 9, 2012 |
| ***/s/ John E. Benjamin***<br>John E. Benjamin | Director, Chairman | March 9, 2012 |
| ***/s/ Barton P. Dambra***<br>Barton P. Dambra | Director | March 9, 2012 |
| ***/s/ Samuel M. Gullo***<br>Samuel M. Gullo | Director | March 9, 2012 |
| ***/s/ Susan R. Holliday***<br>Susan R. Holliday | Director | March 9, 2012 |
| ***/s/ Erland E. Kailbourne***<br>Erland E. Kailbourne | Director | March 9, 2012 |
| ***/s/ Robert N. Latella***<br>Robert N. Latella | Director | March 9, 2012 |
| ***/s/ James L. Robinson***<br>James L. Robinson | Director | March 9, 2012 |
| ***/s/ James H. Wyckoff***<br>James H. Wyckoff | Director | March 9, 2012 |

**Exhibit 10.12**

**RESTRICTED STOCK AWARD AGREEMENT**

**Pursuant to the**

**FINANCIAL INSTITUTIONS, INC.**

**2009 MANAGEMENT STOCK INCENTIVE PLAN**

| | |
|---|---|
| **Name of Participant:** | [ ] |
| **Date of Grant:** | [ ] |
| **Number of Shares:** | [ ] |
| **Value of each Share on Date of Grant:** | [ ] |
| **Vesting Schedule:** | The Vested Percentage of the Number of Shares set forth above shall be determined as of the following Vesting Date(s): |

| Vesting Date | Vested Percentage |
|---|---|
| Second anniversary of the Grant Date | 100 |

This RESTRICTED STOCK AGREEMENT (this "Agreement"), dated as of [ ], is made between Financial Institutions, Inc. (the "Company") and the above-named individual (the "Participant") to record the grant to the Participant by the Company's Management Development and Compensation Committee (the "Committee") of an award of restricted stock (the "Award") on the Date of Grant set forth above pursuant to Section 7 of the Financial Institutions, Inc. 2009 Management Stock Incentive Plan (the "Plan").

The Company and the Participant hereby agree as follows:

**Section 1. Grant of Shares** . The Committee hereby grants to the Participant, as of the Date of Grant, subject to and in accordance with the terms and conditions of the Plan and this Agreement, the Number of Shares set forth above of the Company's Common Stock, par value $.01 per share (the "Common Stock"). The grant of shares of Common Stock to the Participant, evidenced by this Agreement, is an award of restricted stock (as defined in the Plan) and such shares of restricted stock are referred to herein as the "Shares."

**Section 2. Vesting of Shares.** Subject to Section 3 below, provided that the Participant provides substantial services and remains in continuous employment with the Company or a Subsidiary through the Vesting Date(s) set forth above, ownership of the Shares shall vest pursuant to the Vesting Schedule set forth above. For purposes of this Agreement, "Subsidiary" means any subsidiary within the meaning of Rule 405 of the Securities Act of 1933, as amended.

**Section 3. Effects of Certain Events.**

(a) Change in Control . If prior to the latest of the Vesting Dates set forth above, there is a change in control (as such term is defined in the Plan) of the Company, then all Shares not yet vested shall become immediately vested.

(b) Death or Disability . If prior to the latest of the Vesting Dates set forth above, Participant's employment with the Company or one of its Subsidiaries terminates by reason of death, or Disability, then all Shares not yet vested shall become immediately vested.

For purposes of this Agreement, "Disability" means (i) in the case of a Participant whose employment with the Company or a Subsidiary is subject to the terms of an employment or consulting agreement that includes a definition of "Disability," the meaning set forth in such employment or consulting agreement during the period that such employment or consulting agreement remains in effect; and (ii) in all other cases, the meaning as set forth under the Company's long-term disability plan applicable to the Participant as may be amended from time to time, and in the event the Company does not maintain any such plan with respect to a Participant, a physical or mental condition resulting from bodily injury, disease or mental disorder which renders the Participant incapable of continuing his or her usual and customary employment with the Company or a Subsidiary, as the case may be, for a period of not less than 120 days or such other period as may be required by applicable law.

**Section 4. Forfeiture.** Shares that do not become vested in accordance with the vesting criteria set forth in Section 2 of this Agreement shall be forfeited to the Company.

**Section 5. Dividends.** No dividends shall accrue or be paid to the Participant with respect to any Shares subject to the Award that have not become vested Shares or that are subject to any restrictions or conditions on the record date for dividends, unless the Committee provides otherwise.

**Section 6. Rights as Shareholder.** Except for the transfer and other restrictions set forth elsewhere in this Agreement (including the limitations on dividends set forth in Section 5 above) and in the Plan, the Participant, as record holder of the Shares, shall possess all the rights of a holder of the Company's Common Stock (including voting and dividend rights); provided, however, that prior to becoming vested and transferable the certificates representing such Shares shall be held by the Company for the benefit of the Participant. As the Shares become vested Shares, the Company shall, as applicable, either remove the notations on any Shares issued in book entry form which have vested or deliver to the Participant a certificate or certificates evidencing the number of vested Shares. As noted above, the Participant shall not receive any dividends on unvested Shares, and such dividends shall be permanently forfeited.

**Section 7. Legend.** Each share certificate representing the Shares shall bear a legend indicating that such Shares are "Restricted Stock" and are subject to the provisions of this Agreement and the Plan.

**Section 8. No Transferability.** The Shares may not be sold, transferred, pledged, assigned, encumbered, or otherwise alienated or hypothecated until they become fully vested and transferable in accordance with Section 2 of this Agreement and then only to the extent permitted under this Agreement and the Plan and by applicable securities laws. Prior to full vesting and transferability, all rights with respect to the Shares granted to a Participant under the Plan shall be available, during such Participant's lifetime, only to such Participant.

**Section 9. Stock Power** . Concurrently with the execution of this Agreement, the Participant shall deliver to the Company a stock power, endorsed in blank, relating to the Shares. Such stock power shall be in the form attached hereto as Exhibit A. The stock power with respect to any certificate representing Shares that do not vest shall be completed in the name of the Company by an officer of the Company, and the Shares shall be returned to either authorized but unissued shares or treasury shares, depending on their original source.

**Section 10. Withholding Taxes** . The Company shall be entitled to require payment of any amounts required by federal, state or local tax law to be withheld with respect to the transfer or vesting of the Shares, or any other taxable event related thereto. The Company may permit the Participant to make such payment in one or more of the forms specified below:

(a) by cash or check made payable to the Company;

(b) by the deduction of such amount from other compensation payable to the Participant, including without limitation, salary, bonus and other compensation;

(c) by withholding vested shares of Common Stock which have a then current fair market value not greater than the amount necessary to satisfy the Company's withholding obligation based on the minimum statutory withholding rates for federal, state and local income tax and payroll tax purposes; or

(d) in any combination of the foregoing.

In the event the Participant fails to provide timely payment of all sums required by the Company pursuant to this Section, the Company shall have the right and option, but not obligation, to treat such failure as an election by the Participant to provide all or any portion of such required payment by means of tendering Shares in accordance with Section 10(c).

**Section 11. Adjustment of Shares** . As provided by the Plan, in the event of any change in the Common Stock of the Company by reason of any stock dividend, stock split, recapitalization, reorganization, merger, consolidation, split-up, combination, or exchange of Shares, or of any similar change affecting the Common Stock, the Shares shall be adjusted automatically consistent with such change to prevent substantial dilution or enlargement of the rights granted to, or available for, the Participant hereunder.

**Section 12. No Employment Rights** . Neither the Plan nor this Award shall confer upon the Participant any right with respect to continuance of employment by the Company or any Subsidiary nor shall they interfere in any way with the right of the Company or any Subsidiary to terminate the Participant's employment at any time, with or without cause.

**Section 13. Coordination with Plan** . The Participant hereby acknowledges receipt of a copy of the Plan and agrees to be bound by all of the terms and provisions thereof including any that may conflict with those contained in this Agreement. Capitalized terms used in this Agreement shall have the meaning given to such terms under the Plan.

**Section 14. Notices.** All notices to the Company shall be in writing and sent to the Company's Director of Human Resources at the Company's offices. Notices to the Participant shall be addressed to the Participant at the Participant's address as it appears on the Company's records.

**Section 15. Amendment.** The Company may alter, amend or terminate this Agreement only with the Participant's consent, except as otherwise expressly provided by the Plan or this Agreement.

**Section 16. Governing Law.** This Agreement shall be governed by the laws of the State of New York, without reference to principles of conflict of laws, and construed accordingly.

**Section 17. Compensation Recovery Policy.** Notwithstanding any other provision of this Agreement to the contrary, any Shares granted and/or issued hereunder, and/or any amount received with respect to any sale of any such Shares, shall be subject to potential cancellation, recoupment, rescission, payback or other action in accordance with the terms of the Company's compensation recovery policy, if any, or any similar policy that the Company may adopt from time to time (the "Policy"). The Participant agrees and consents to the Company's application, implementation and enforcement of (i) the Policy that may apply to the Participant and (ii) any provision of applicable law relating to cancellation, rescission, payback or recoupment of compensation, and expressly agrees that the Company may take such actions as are necessary to effectuate the Policy or applicable law without further consent or action being required by the Participant. To the extent that the terms of this Agreement and the Policy or any similar policy conflict, then the terms of such policy shall prevail.

**Section 18. Section 280G of the Code.** In the event that the accelerated vesting of the Shares, together with all other payments and the value of any benefit received or to be received by the Participant, would result in all or a portion of such payment being subject to the excise tax under Section 4999 of the Code (the "Excise Tax"), then the Participant's payment shall be either (a) the full payment or (b) such lesser amount that would result in no portion of the payment being subject to the Excise Tax, whichever of the foregoing amounts, taking into account the applicable federal, state, and local employment taxes, income taxes and the Excise Tax, results in the receipt by the Participant, on an after-tax basis, of the greatest amount of the payment notwithstanding that all or some portion of the payment may be taxable under Section 4999 of the Code. Any such reduction shall be made by the Company in compliance with all applicable legal authority, including Section 409A. All determinations required to be made under this Section shall be made by the nationally recognized accounting firm which is the Company's outside auditor immediately prior to the event triggering the payments that are subject to the Excise Tax, which firm must be reasonably acceptable to the Participant (the "Accounting Firm"). The Company shall cause the Accounting Firm to provide detailed supporting calculations of its determinations to the Company and the Participant. Notice must be given to the Accounting Firm within 15 business days after an event entitling the Participant to a payment under Section 3(a) of this Agreement. All fees and expenses of the Accounting Firm shall be borne solely by the Company.

IN WITNESS WHEREOF, the Committee and the Participant have caused this Agreement to be executed on the date set forth opposite their respective signatures, it being further understood that the Date of Grant may differ from the date of signature.

Dated: _____

**FOR THE COMPANY:**

By: _____

Name: _____

Title: _____

Dated: _____

**PARTICIPANT:**

By: _____

Name: _____

**EXHIBIT A**

**STOCK POWER**

FOR VALUE RECEIVED, the undersigned does hereby sell, assign and transfer to Financial Institutions, Inc. (the "Company"), [ ] shares of the Company's common stock represented by **Certificate No. [ ]** . The undersigned authorizes the Secretary of the Company to transfer the stock on the books of the Company in the event of the forfeiture of any shares issued under the Restricted Stock Award Agreement dated as of [ ] between the Company and the undersigned.

**Dated:** _____

_____

[Participant's Name]

**Exhibit 10.13**

**FINANCIAL INSTITUTIONS, INC.**
**2009 MANAGEMENT STOCK INCENTIVE PLAN**

**2012 PERFORMANCE PROGRAM**
**MASTER AGREEMENT**

This 2012 Performance Program Master Agreement (this "Master Agreement") relating to a grant (the "Award") of restricted stock of Financial Institutions, Inc. (the "Company"), dated as of the Award Date set forth in the Award Certificate, is made by and between the Company and each Participant pursuant to the Financial Institutions, Inc. 2009 Management Stock Incentive Plan (the "Plan"). The Award Certificate is included with and made part of this Master Agreement. In this Master Agreement and each Award Certificate, unless the context otherwise requires, words and expressions shall have the meanings given to them in the Plan, except as herein defined.

**Section 1. Definitions** . For purposes of the Award and this Master Agreement, the following terms shall have the following meanings:

(a) "Award Certificate" means the separate certificate given to each Participant specifying the Award Date, Number of Shares, Performance Period, and Performance Range for such Participant's Award.

(b) "Board" means the Board of Directors of Financial Institutions, Inc.

(c) "Code" means the Internal Revenue Code of 1986, as amended.

(d) "Committee" means the Management Development and Compensation Committee of the Board. Any reference herein to the Committee shall be deemed to include any person to whom any duty of the Committee has been delegated pursuant to Section 6(a) of this Master Agreement.

(e) "Common Stock" means the shares of common stock of the Company, par value $0.01 per share.

(f) "Disability" means (i) in the case of a Participant whose employment with the Company or a Subsidiary is subject to the terms of an employment or consulting agreement that includes a definition of "Disability," the meaning set forth in such employment or consulting agreement during the period that such employment or consulting agreement remains in effect; and (ii) in all other cases, the meaning as set forth under the Company's long-term disability plan applicable to the Participant as may be amended from time to time, and in the event the Company does not maintain any such plan with respect to a Participant, a physical or mental condition resulting from bodily injury, disease or mental disorder which renders the Participant incapable of continuing his or her usual and customary employment with the Company or a Subsidiary, as the case may be, for a period of not less than 120 days or such other period as may be required by applicable law.

(g) "Earned Shares" means Shares that have become earned based on the attainment of the Performance Requirements.

(h) “Individual Performance Requirement” means the individual performance requirement, as set forth in Section 4 of Schedule A to this Master Agreement.

(i) “Participant” means the Company’s Chief Executive Officer, Executive Vice Presidents or Senior Vice Presidents, to whom an Award has been granted under the Plan.

(j) “Performance Goals” means the threshold, target and maximum performance goals for each Performance Requirement, as set forth in Section 5 of Schedule A to this Master Agreement.

(k) “Performance Period” means the one-year period specified in the Award Certificate.

(l) “Performance Range” means, with regard to any Participant, the threshold, target and maximum percentage of Shares that may become Earned Shares based on attainment of the Performance Requirements, each as set forth in a Participant’s Award Certificate.

(m) “Performance Requirements” means the performance requirements, as set forth in Section 3(a) of this Master Agreement.

(n) “Qualified Performance-Based Award” means an Award that is intended to meet the requirements for “qualified performance-based compensation” under Section 162(m) of the Code.

(o) “Service Requirements” means the requirement of continued employment and substantial services with the Company, as set forth in Section 3(b) of this Master Agreement.

(p) “Subsidiary” means any subsidiary of the Company within the meaning of Rule 405 of the Securities Act of 1933, as amended.

(q) “Vested Shares” means Earned Shares that have become vested, nonforfeitable and transferable based on satisfaction of the Service Requirements.

(r) “Weighting Percentage” means the weighting given to a Performance Requirement as set forth in Section 5 of Schedule A to this Master Agreement.

**Section 2. Grant of Restricted Stock.** Subject to the provisions of this Master Agreement and the provisions of the Plan and the Award Certificate, the Committee grants to the Participant named in the Award Certificate, as of the Award Date, an Award of the Number of Shares of the Company’s Common Stock set forth in the Award Certificate. The grant of shares of Common Stock to the Participant is an award of restricted stock (as defined in the Plan), and such shares of restricted stock are referred to herein as the “Shares.”

**Section 3. Vesting of the Shares.** There are two vesting requirements that must be satisfied before a Participant becomes vested in the Shares: (i) the Performance Requirements set forth in Section 3(a) below; and (ii) the Service Requirements set forth in Section 3(b) below. Both the Performance Requirements and the Service Requirements must be satisfied before a Share will become a Vested Share.

(a) Performance Requirements and Earned Shares . Subject to Section 4 of this Master Agreement, the Number of Shares, if any, that shall become Earned Shares is determined in accordance with the methodology set forth in Schedule A.

(b) Service Requirements and Vested Shares . Subject to Section 4 of this Master Agreement, the number of Earned Shares that shall become Vested Shares is based on the Participant providing substantial services and remaining in the continuous employment of the Company or a Subsidiary through a specified date, or through specified dates (each, a "Service Date," and collectively, the "Service Dates"). The Percentage of Earned Shares that shall become Vested Shares and the Service Dates applicable to such Vested Shares are set forth in the Service Requirements section of the Participant's Award Certificate.

(c) Forfeiture . Shares that do not become Vested Shares in accordance with the Performance Requirements and the Service Requirements shall be forfeited to the Company.

**Section 4. Effects of Certain Events.**

(a) General . Subject to Sections 4(b) through 4(d) of this Master Agreement, in the event that a Participant's employment with the Company is terminated before the Shares become Vested Shares under the Service Requirements, all unvested Shares subject to the Award are automatically forfeited.

(b) Death or Disability . In the event of a Participant's death or termination of employment due to Disability before the Shares become Vested Shares under the Service Requirements, such Participant shall immediately vest in all of the Shares that have become Earned Shares under the Performance Requirements but have not yet become Vested Shares under the Service Requirements. Any Shares that have not yet become Earned Shares shall be forfeited.

(c) Change in Control . In the event of a change in control of the Company (as defined in the Plan), all of a Participant's Shares shall immediately become Vested Shares, unless directed otherwise by a resolution of the Committee adopted prior to and specifically relating to the occurrence of such change in control.

**Section 5. Dividends** . No dividends shall accrue or be paid to the Participant with respect to any Shares subject to the Award that have not become Vested Shares or that are subject to any restrictions or conditions on the record date for dividends, unless the Committee provides otherwise.

**Section 6. Miscellaneous**

(a) Administration . The Award shall be administered by the Committee. The Committee shall have authority to interpret the Award, the Award Certificate and this Master Agreement, to prescribe rules and regulations relating to the Award, the Award Certificate and this Master Agreement, to take any other actions it deems necessary or advisable for the administration of the Award, the Award Certificate and this Master Agreement and shall retain all general authority granted to it under Section 2 of the Plan. In accordance with applicable law, the Committee may delegate any of the responsibilities under this Master Agreement to the Chief Executive Officer of the Company or the Finance or Human Resources departments of the Company, or may receive recommendations from such individuals and departments regarding such responsibilities.

(b) Amendment . The Committee may, at any time, amend, modify or terminate this Master Agreement. Termination of this Master Agreement after the end of the Performance Period but before Shares become Earned or Vested Shares will not reduce Participants' rights to receive Vested Shares for the Performance Period. Termination or amendment of this Master Agreement during the Performance Period may be retroactive to the beginning of the Performance Period, at the discretion of the Committee. If a change in control occurs, no amendment or termination may adversely affect existing Awards without the consent of the Participant.

(c) Adjustments . As provided by the Plan, in the event of any change in the Common Stock of the Company by reason of any stock dividend, stock split, recapitalization, reorganization, merger, consolidation, split-up, combination, or exchange of Shares, or of any similar change affecting the Common Stock, the Shares shall be adjusted automatically consistent with such change to prevent substantial dilution or enlargement of the rights granted to, or available for, the Participant hereunder. Furthermore, the Committee shall adjust the Performance Requirements to the extent (if any) it determines that the adjustment is necessary or advisable to preserve the intended incentives and benefits to reflect any material change in corporate capitalization, any material corporate transaction (such as a reorganization, combination, separation, merger, acquisition, or any combination of the foregoing), or any complete or partial liquidation of the Company, or any other similar special circumstances, including the issuance of a significant number of shares of Common Stock. Any such adjustment to a Qualified Performance-Based Award shall be made in a manner that complies with Section 162(m) of the Code.

(d) No Transferability . The Shares may not be sold, transferred, pledged, assigned, encumbered, or otherwise alienated or hypothecated until they become fully vested and transferable in accordance with Section 3 of this Master Agreement and then only to the extent permitted under this Master Agreement, the Award Certificate, the Plan and by applicable securities laws. Prior to full vesting and transferability, all rights with respect to the Shares granted to a Participant under the Plan shall be available, during such Participant's lifetime, only to such Participant.

(e) No Right to Continued Employment . The terms and conditions of the Award, the Award Certificate, this Master Agreement and the Plan shall not be deemed to constitute a contract of employment between the Company and a Participant. Such employment is hereby acknowledged to be an "at will" employment relationship that can be terminated at any time for any reason, or no reason, with or without cause, and with or without notice, except as otherwise provided in a written employment agreement. Nothing in the Award, the Award Certificate, this Master Agreement or the Plan shall be deemed to give a Participant the right to be retained in the service of the Company as an employee or to interfere with the right of the Company to discipline or discharge a Participant at any time.

(f) Rights as a Shareholder . Except for the transfer and other restrictions set forth elsewhere in this Master Agreement (including the limitations on dividends set forth in Section 5 of this Master Agreement), the Award Certificate and the Plan, the Participant, as record holder of the Shares, shall possess all the rights of a holder of the Company's Common Stock (including voting); provided, however, that prior to becoming vested and transferable the certificates representing such Shares shall be held by the Company for the benefit of the Participant. As the Shares become Vested Shares, the Company shall, as applicable, either remove the notations on any Shares issued in book entry form which have vested or deliver to the Participant a certificate or certificates evidencing the number of Vested Shares (or, in either case, such lesser number of Shares as may result after giving effect to Section 6(g) of this Master Agreement).

(g) Withholding Taxes . The Company shall be entitled to require payment of any amounts required by federal, state or local tax law to be withheld with respect to the transfer or vesting of the Shares, or any other taxable event related thereto. The Company may permit the Participant to make such payment in one or more of the forms specified below:

(i) by cash or check made payable to the Company;

(ii) by the deduction of such amount from other compensation payable to the Participant, including without limitation, salary, bonus and other compensation;

(iii) by tendering shares of Common Stock already owned by the Participant or Vested Shares which have a then current fair market value not greater than the amount necessary to satisfy the Company's withholding obligation based on the minimum statutory withholding rates for federal, state and local income tax and payroll tax purposes; or

(iv) in any combination of the foregoing.

In the event the Participant fails to provide timely payment of all sums required by the Company pursuant to this Section, the Company shall have the right and option, but not obligation, to treat such failure as an election by the Participant to provide all or any portion of such required payment by means of tendering Vested Shares in accordance with Section 6(g)(iii) of this Master Agreement.

(h) Legend . Each share certificate representing the Shares shall bear a legend indicating that such Shares are "Restricted Stock" and are subject to the provisions of this Master Agreement and the Plan.

(i) Stock Power . Concurrently with the grant of the Award, the Participant shall deliver to the Company a stock power, endorsed in blank, relating to the Shares. Such stock power shall be in the form attached to the Award Certificate as Exhibit A. The stock power with respect to any certificate representing Shares that do not vest shall be completed in the name of the Company by an officer of the Company, and the Shares shall be returned to either authorized but unissued shares or treasury shares, depending on their original source.

(j) Coordination with Plan and the Award Certificate . The Participant hereby acknowledges receipt of a copy of the Plan and the Award Certificate and agrees to be bound by all of the terms and provisions thereof including any that may conflict with those contained in this Master Agreement.

(k) Notices . All notices to the Company shall be in writing and sent to the Company's Director of Human Resources at the Company's offices. Notices to the Participant shall be addressed to the Participant at the Participant's home or work address, including via interoffice mail, as it appears on the Company's records. Any such notices may be made in electronic format or through means of online or other electronic transmission.

(l) Compensation Recovery Policy . Notwithstanding any other provision of this Master Agreement to the contrary, any Shares granted and/or issued hereunder, and/or any amount received with respect to any sale of any such Shares, shall be subject to potential cancellation, recoupment, rescission, payback or other action in accordance with the terms of the Company's compensation recovery policy, if any, or any similar policy that the Company may adopt from time to time (the "Policy"). The Participant agrees and consents to the Company's application, implementation and enforcement of (i) the Policy that may apply to the Participant and (ii) any provision of applicable law relating to cancellation, rescission, payback or recoupment of compensation, and expressly agrees that the Company may take such actions as are necessary to effectuate the Policy or applicable law without further consent or action being required by the Participant. To the extent that the terms of this Master Agreement and the Policy or any similar policy conflict, then the terms of such policy shall prevail.

(m) Section 280G of the Code . In the event that the accelerated vesting of the Shares, together with all other payments and the value of any benefit received or to be received by the Participant, would result in all or a portion of such payment being subject to the excise tax under Section 4999 of the Code (the "Excise Tax"), then the Participant's payment shall be either (a) the full payment or (b) such lesser amount that would result in no portion of the payment being subject to the Excise Tax, whichever of the foregoing amounts, taking into account the applicable federal, state, and local employment taxes, income taxes and the Excise Tax, results in the receipt by the Participant, on an after-tax basis, of the greatest amount of the payment notwithstanding that all or some portion of the payment may be taxable under Section 4999 of the Code. Any such reduction shall be made by the Company in compliance with all applicable legal authority, including Section 409A. All determinations required to be made under this Section shall be made by the nationally recognized accounting firm which is the Company's outside auditor immediately prior to the event triggering the payments that are subject to the Excise Tax, which firm must be reasonably acceptable to the Participant (the "Accounting Firm"). The Company shall cause the Accounting Firm to provide detailed supporting calculations of its determinations to the Company and the Participant. Notice must be given to the Accounting Firm within 15 business days after an event entitling the Participant to a payment under Section 4(c) of this Master Agreement. All fees and expenses of the Accounting Firm shall be borne solely by the Company.

(n) Governing Law . This Master Agreement, to the extent not otherwise governed by the Code or the laws of the United States, shall be governed by the laws of the State of New York, without reference to principles of conflict of laws, and construed accordingly.

* * * * *

**FINANCIAL INSTITUTIONS, INC.**
**2009 MANAGEMENT STOCK INCENTIVE PLAN**
**2012 PERFORMANCE PROGRAM MASTER AGREEMENT**

**SCHEDULE A**

**Section 1. Definitions** . For purposes of the Award and this Master Agreement, the following terms shall have the following meanings:

(a) "Earnings Per Share" means diluted earnings per share, as such amount as is reported on the Company's audited financial statements.

(b) "Efficiency Ratio" means the ratio of expense to revenue as reported in the Company's annual report to shareholders on Form 10-K.

(c) "Gateway Requirement" means Five Star Bank's Composite "CAMELS" rating in place on December 31, 2012.

(d) "Net Charge-off Ratio" means the ratio of the Company's net charge-offs to average loans outstanding as reported in the Company's annual report to shareholders on Form 10-K.

**Section 2. Earned Shares** . Subject to the Committee's authority to adjust the number of Earned Shares as described in Section 9 of this Schedule A, the Earned Shares at the end of the Performance Period is determined based on the achievement of:

(a) the Gateway Requirement;

(b) the Individual Performance Requirement;

(c) the Performance Requirements, consisting of: (i) Earnings Per Share; (ii) Net Charge-off Ratio; (iii) Efficiency Ratio; and

(d) for Qualified Performance-Based Awards, the Threshold Performance Requirement set forth in Section 8 of this Schedule A.

**Section 3. Gateway Requirement** . If the Gateway Requirement is not a composite rating of "2" or better, all Shares issued under this Master Agreement shall be forfeited and shall not become Earned Shares.

**Section 4. Individual Performance Requirement** . If the Participant does not receive a minimum performance rating of "satisfactory" for the Performance Period, as determined by the Company in its sole discretion, all Shares issued under this Master Agreement shall be forfeited and shall not become Earned Shares.

**Section 5. Performance Requirements** . The Performance Requirements and the applicable Performance Goals at threshold, target and maximum for each Performance Requirement, as well as the Weighting Percentage for each Performance Requirement are as follows:

| | Performance Goals | | | |
|---|---|---|---|---|
| **Performance Requirement** | **Threshold** | **Target** | **Maximum** | **Weighting Percentage** |
| Earnings Per Share | $ [ ] | $ [ ] | $ [ ] | [ ]% |
| Net Charge-off Ratio | [ ]% | [ ]% | [ ]% | [ ]% |
| Efficiency Ratio | [ ]% | [ ]% | [ ]% | [ ]% |

**Section 6. Performance Results.**

(a) For each Performance Requirement, the Number of Shares that vest and become Earned Shares based on the achievement of that Performance Requirement's Performance Goals at threshold, target and maximum is equal to the product of (i) the Number of Shares subject to the Award; (ii) the Performance Range set forth in the Participant's Award Certificate at threshold, target or maximum, respectively; and (iii) the Performance Requirement's Weighting Percentage, rounded down to a whole number.

(b) In the event that the Company's actual performance for the Performance Period does not meet the threshold for a Performance Requirement, no Shares shall be Earned Shares for such Performance Requirement.

(c) If the Company's actual performance for the Performance Period is between threshold and target for the Performance Requirement, the number of Earned Shares for that Performance Requirement is equal to the product of: (i) the Number of Shares subject to the Award; (ii) the actual performance achievement, determined using straight line interpolation between the threshold and the target from the Participant's Performance Range set forth in the Participant's Award Certificate; and (iii) the Performance Requirement's Weighting Percentage, rounded down to a whole number.

(d) If the Company's actual performance for the Performance Period is between target and maximum for the Performance Requirement, the number of Earned Shares for that Performance Requirement is equal to the product of: (i) the Number of Shares subject to the Award; (ii) the actual performance achievement, determined using straight line interpolation between the target and maximum from the Participant's Performance Range set forth in the Participant's Award Certificate; and (iii) the Performance Requirement's Weighting Percentage, rounded down to a whole number.

(e) If the Company's actual performance for the Performance Period is at or above maximum for a Performance Requirement, the number of Earned Shares is equal to the product of: (i) the Number of Shares subject to the Award; (ii) the Performance Range set forth in the Participant's Award Certificate at maximum; and (iii) the Performance Requirement's Weighting Percentage, rounded down to a whole number.

(f) The total number of Number of Shares that become Earned Shares shall be the sum of the number of Earned Shares for each Performance Requirement.

**Section 7. Actual Performance** . The Committee reviews and approves the actual Earnings Per Share, Net Charge-off Ratio and Efficiency Ratio for the Performance Period.

**Section 8. Qualified Performance-Based Awards.**

(a) Establishment . Only Qualified Performance-Based Awards shall be subject to the additional Threshold Performance Requirement. In the case of a Qualified Performance-Based Award, the Threshold Performance Requirement shall be established within 90 days after commencement of the Performance Period in a manner that complies with Section 162(m) of the Code. The Threshold Performance Requirement is met if the Company achieves positive [return on equity] for the Performance Period.

(b) Performance Results and Maximum Shares . In the case of a Qualified Performance-Based Award, if the Threshold Performance Requirement is achieved, the number of Earned Shares shall be: (i) the Number of Shares subject to the Award (which, for the avoidance of doubt, is the maximum number of Shares subject to the Award); or (ii) any lesser amount determined by the Committee based on the level of actual performance with respect to the Performance Requirements. It is anticipated that the Committee will exercise discretion such that the number of Earned Shares would represent the amount that would be payable pursuant to the applicable Performance Requirements, rather than the maximum number of Shares subject to the Award, unless the actual attainment of the Performance Requirements also results in the maximum number of Earned Shares. For the avoidance of doubt, with respect to Qualified Performance-Based Awards, the number of Vested Shares shall not exceed the maximum number of Shares determined under Section 8(b)(i) of this Schedule A.

(c) Measurement and Certification . In the case of a Qualified Performance-Based Award, the Committee will measure and certify: (i) the achievement of the Threshold Performance Requirement and the number of Shares that have become Earned Shares based on the Threshold Performance Requirement; and (ii) the achievement of the Service Requirements and the number of Shares that have become Earned Shares based on the Service Requirements, in each case, in a manner that complies with Section 162(m) of the Code, including the requirement that the performance goal be objectively measured and certified in writing.

(d) Intent and Administration . It is intended that Qualified Performance-Based Awards meet the requirements "qualified performance-based compensation" and shall be fully deductible by the Company without regard to the limitations of Section 162(m) of the Code. Qualified Performance-Based Awards shall be administered consistent with such intention. The maximum annual share limit of Section 4 of the Plan shall apply with respect to Qualified Performance-Based Awards. As of the Award Date, Section 4 of the Plan provides that the maximum number of shares of Common Stock that may be granted under the Plan to any one Participant in any one calendar year is 300,000.

**Section 9. Final Number of Earned Shares** . Subject to the limitations on Qualified Performance-Based Awards imposed by Section 8(b) of this Schedule A, the number of Earned Shares may be adjusted upward or downward by the Committee, in its sole and absolute discretion, to a whole number, not to exceed the Number of Shares set forth in that Participant's Award Certificate.

**EXAMPLE** ( *for illustration purposes only* )

Suppose a Participant received an Award and his or her Award Certificate provided for a Number of Shares of 1,000 and a Performance Range as follows:

| Threshold | Target | Maximum |
|---|---|---|
| 40% | 80% | 100% |

The Performance Requirements, Weighting Percentages and Performance Goals were as set forth above in this Schedule A. Suppose the performance results for the Performance Period are as follows:

| Performance Requirement | Performance Result | Level Achieved |
|---|---|---|
| Earnings Per Share | $ 1.44 | Target |
| Net Charge-off Ratio | 58.0% | Maximum |
| Efficiency Ratio | 0.70% | Threshold |

The Earned Shares for each Performance Requirement would be determined as follows:

- The number of Earned Shares for the Earnings Per Shares Performance Requirement would be 480 Shares (1,000 Shares x 80% (Target) x 60% (Weighting Percentage)).
- The number of Earned Shares for the Net Charge-off Ratio Performance Requirement would be 200 Shares (1,000 Shares x 100% (Maximum) x 20% (Weighting Percentage)).
- The number of Earned Shares for the Efficiency Ratio Performance Requirement would be 80 Shares (1,000 Shares x 40% (Threshold) x 20% (Weighting Percentage)).
- The total number of Earned Shares for the Award would be 760 Shares (480 Earned Shares for the Earnings Per Shares Performance Requirement plus 200 Earned Shares for the Net Charge-off Ratio Performance Requirement plus 80 Earned Shares for the Efficiency Ratio Performance Requirement).

**Exhibit 10.14**

**FINANCIAL INSTITUTIONS, INC.**
**2009 MANAGEMENT STOCK INCENTIVE PLAN**

**2012 PERFORMANCE PROGRAM**
**AWARD CERTIFICATE**

Financial Institutions, Inc., a New York financial holding company (the "Company"), hereby grants to the Participant as of the Award Date set forth below, a restricted stock award to receive the Number of Shares (the "Shares") as set forth below (the "Award"). Each Share subject to the Award consists of a share of restricted stock issued under the 2009 Management Stock Incentive Plan (the "Plan"), which shall vest upon attainment of the Performance Requirements and the Service Requirements set forth in the 2012 Performance Program Master Agreement (the "Master Agreement").

Award Date: [ ]

Participant: [ ]

Number of Shares: [ ]

Performance Period: January 1, 2012 through December 31, 2012

| Performance Range: | Threshold | Target | Maximum |
|---|---|---|---|
| | [40]% | [80]% | [100]% |

| Service Requirements: | Percentage of Earned Shares | Service Date |
|---|---|---|
| | [50]% | [Second anniversary of the Award Date] |
| | Remaining [50]% | [Third anniversary of the Award Date] |

The Award is subject to the terms and conditions set forth in this Award Certificate, the Plan and the Master Agreement. All terms and provisions of the Plan and the Master Agreement, as the same may be amended from time to time, are incorporated and made part of this Award Certificate. If any provision of this Award Certificate is in conflict with the terms of the Plan or the Master Agreement, then the terms of the Plan or the Master Agreement, as applicable, shall govern. All capitalized terms used in this Award Certificate and not defined herein shall have the meanings assigned to them in the Plan or the Master Agreement. The Participant hereby expressly acknowledges receipt of a copy of the Plan and the Master Agreement.

*(signature page immediately follows)*

IN WITNESS WHEREOF, the parties have executed this Award Certificate as of the Award Date.

FINANCIAL INSTITUTIONS, INC.

By: _____
Name:
Title:

The Participant hereby accepts and agrees to be bound by all of the terms and conditions of this Award Certificate, the Master Agreement and the Plan.

_____
PARTICIPANT

**SCHEDULE A**

**STOCK POWER**

FOR VALUE RECEIVED, the undersigned does hereby sell, assign and transfer to Financial Institutions, Inc. (the "Company"), [ ] shares of the Company's common stock represented by Certificate No. [ ]. The undersigned authorizes the Secretary of the Company to transfer the stock on the books of the Company in the event that either: (a) any shares are forfeited under the terms of the Company's 2012 Performance Program Master Agreement (the "Master Agreement"); or (b) any shares are transferred to the Company in satisfaction of the withholding obligations of the undersigned as provided in the Plan and the Master Agreement.

Dated:

_____

PARTICIPANT

**Exhibit 10.24**

# ASSIGNMENT, PURCHASE AND ASSUMPTION AGREEMENT

by and between

**FIRST NIAGARA BANK, NATIONAL ASSOCIATION**

and

**FIVE STAR BANK**

**JANUARY 19, 2012**

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This ASSIGNMENT, PURCHASE AND ASSUMPTION AGREEMENT, dated as of January 19, 2012, is between First Niagara Bank, National Association, a national banking association with its principal office in Buffalo, New York (" Assignor "), and Five Star Bank, a New York State chartered bank with its principal office in Warsaw, New York (" Purchaser ").

RECITALS

WHEREAS, Assignor entered into the Purchase and Assumption Agreement dated as of July 30, 2011 (the " Primary Purchase Agreement ") by and among HSBC Bank USA, National Association, a national banking association (" HSBC "), HSBC Securities (USA) Inc., a Delaware corporation (" HSI "), and HSBC Technology & Services (USA) Inc., a Delaware corporation (" HTSI " and collectively with HSBC and HSI, the " HSBC Sellers ") and Assignor;

WHEREAS, pursuant to, and on the terms and conditions set forth in, the Primary Purchase Agreement, (i) Assignor agreed to purchase from the HSBC Sellers, and the HSBC Sellers agreed to sell to Assignor, those assets identified and defined in the Primary Purchase Agreement as the "Purchased Assets" and referred to and defined in this Agreement as the " Primary Purchased Assets " and (ii) the HSBC Sellers agreed to transfer to Assignor, and Assignor agreed to assume, those liabilities and obligations identified and defined in the Primary Purchase Agreement as the "Assumed Liabilities" and referred to and defined in this Agreement as the " Primary Assumed Liabilities ";

WHEREAS, the Primary Purchase Agreement permits Assignor, on the terms and conditions set forth therein, to assign its right to purchase a portion of the Primary Purchased Assets and its obligations to assume the related portion of the Primary Assumed Liabilities to a third party purchaser;

WHEREAS, Assignor desires to assign its right to purchase a portion of the Primary Purchased Assets and its obligations to assume the related portion of the Primary Assumed Liabilities to Purchaser, and Purchaser desires to acquire such portion of the Primary Purchased Assets and to assume the related portion of the Primary Assumed Liabilities, on the terms and conditions set forth herein; and each of the HSBC Sellers has consented to such assignment, subject to the terms of such consent and to the rights of the HSBC Sellers to consent to any future amendment of this Agreement as provided in Section 14.1 hereof;

WHEREAS, Assignor's assignment of rights and obligations to Purchaser under this Agreement and Purchaser's acquisition of such rights and assumption of such obligations (i) are not intended to, and shall not diminish, the rights of Assignor or the HSBC Sellers under the Primary Purchase Agreement or the obligations of Assignor to the HSBC Sellers, or of the HSBC Sellers to Assignor, under the Primary Purchase Agreement and (ii) are not intended to, and shall not vest in, Purchaser any rights, claims for indemnification or other claims against any HSBC Seller and no HSBC Seller shall have any liability of any kind to Purchaser;

WHEREAS, the assets, rights and liabilities subject to assignment, purchase and assumption in this Agreement consist solely of the Assignor's rights under the Primary Agreement with respect to the portion of the Primary Purchased Assets and the related portion of the Primary Assumed Liabilities, provided hereby and, except as otherwise set forth herein, do
not include any other assets, rights or liabilities of Assignor or its Affiliates (whether now existing or hereafter acquired); and

WHEREAS, concurrent with the execution and delivery of this Agreement HSBC Sellers have executed the confirmation letter in substantially the form attached as Exhibit D .

NOW, THEREFORE, in consideration of and subject to each of the covenants, representations, warranties, terms and conditions hereinafter set forth, the receipt and sufficiency of which are hereby acknowledged, the parties, intending to be legally bound, hereby agree as follows:

## ARTICLE I

## DEFINITIONS; CONSTRUCTION

Section 1.1 Definitions . For purposes of this Agreement, the parties covenant and agree to the following definitions and other terms:

" Accrued Interest and Fees " shall mean (i) with respect to the Assumed Deposits, the interest, fees, costs, and other charges (whether billed or unbilled) that have been accrued but not yet paid, credited or charged to the Assumed Deposits; and (ii) with respect to the Purchased Assets, the interest, dividends, fees, costs, and other charges (whether billed or unbilled) that have been accrued but not yet paid, credited or charged to the Purchased Assets, in each case as set forth in the general ledger of the applicable HSBC Seller maintained in the ordinary course of business of the HSBC Sellers in accordance with the internal controls and procedures of the HSBC Sellers, consistently applied.

" Adjustment Payment Date " shall have the meaning specified in Section 3.3(d) .

" Affiliate " shall mean, with respect to any Person, any other Person that directly, or through one or more intermediaries, Controls, is Controlled by or is under common Control with, such Person.

" Affiliated Employees " shall mean the employees of any Affiliate of HSBC, so identified on Schedule 1.1(c)(ii) (as updated pursuant to Section 7.12 ).

" Aggregate Asset Amount " shall have the meaning specified in Section 3.1(b)(2) .

" Agreement " shall mean this Assignment, Purchase and Assumption Agreement, including the Schedules and Exhibits (excluding Exhibit C) hereto, as may be amended and/or restated from time to time.

" Allocation Statement " shall have the meaning specified in Section 3.4(a) .

" Applicable Law " shall mean any federal, state, local, domestic or foreign law, including common law, statute, ordinance, rule, regulation, code, order, judgment, injunction or decree enacted, issued, promulgated, enforced or entered by, or any formal interpretive letter issued by, a Government Entity.

" Appraised Value " shall mean, with respect to any real property, the fair market value (assuming current use) of such real property as determined by the appraisal of an independent third-party appraiser in accordance with the Primary Purchase Agreement. The portion of the appraisal fees allocated to Assignor under the Primary Purchase Agreement with respect to the real property included within the Purchased Assets shall be split fifty percent/fifty percent (50%/50%) between Assignor and Purchaser.

" Assignment and Assumption Agreement " shall have the meaning specified in Section 4.2(a)(5) .

" Assignor " shall have the meaning specified in the Preamble.

" Assignor Indemnified Parties " shall have the meaning specified in Section 13.3(a).

" Assignor Regulatory Approvals " shall have the meaning specified in Section 5.3 .

" Assumed Agreements " shall have the meaning specified in Section 2.1(a)(10) .

" Assumed Contracts " shall have the meaning specified in Section 2.1(a)(10) .

" Assumed Deposits " shall mean deposits (as defined in 12 U.S.C. § 1813(l)) that are held by HSBC or any of its Subsidiaries in connection with the Transferred Business, including demand deposits, savings accounts, money market deposit accounts, mutual fund and reserve fund sweep accounts, negotiable order of withdrawal accounts, certificates of deposit, deposits acquired through the telephone or the internet or other electronic media and, subject to Section 7.11 , IRA, Employee Pension Plan and Keogh accounts, including any debit accounts related thereto, in each case, that are listed on Schedule 1.1(a) (as updated pursuant to Section 7.12 ), excluding: (i) structured deposits; (ii) brokered deposits; (iii) unclaimed deposits subject to unclaimed property statute/escheatment; (iv) deposits constituting money orders, certified and official checks and other items in the process of clearing' and (v) deposits by state, county and municipal government agencies and authorities.

" Assumed Letters of Credit " shall have the meaning specified in Section 2.1(a)(9) .

" Assumed Liabilities " shall have the meaning specified in Section 2.2(a) .

" ATM " shall mean an automated teller machine.

" ATM Real Property Leases " shall have the meaning specified in Section 2.1(a)(5) .

" Banking Centers " shall mean the branches and offices, including any related drive-thru teller facilities, of HSBC and its Subsidiaries listed on Schedule 1.1(b).

" Banking Center Customers " shall mean, individually and collectively, (i) the Persons named as the owners of the deposit accounts relating to the Assumed Deposits, (ii) customers related to the Transferred Business Banking Relationships and the Transferred Wealth Management Relationships, (iii) the primary obligors under the Purchased Loans, and (iv) other

Persons who are customers of the Transferred Business, including, in each case, Banking Center customers who conduct activities or receive Banking Related Services through the internet or other electronic media. " Banking Receivables " shall have the meaning specified in Section 2.1 (a)(14) .

" Banking Related Services " shall mean banking and banking-related services, brokerage, custody, financial planning, insurance, estate planning, tax planning, liquidity or cash management, lending (including commercial real estate lending), issuance of credit cards and similar products, investment advisory, investment banking, asset management and trust and fiduciary services.

" Bill of Sale " shall have the meaning specified in Section 4.2(a)(4) .

" Business Banking " shall mean the business of providing Banking Related Services through the Banking Centers to business organizations, that are not Specified Enterprises.

" Business Day " shall mean any day excluding Saturday, Sunday and any day on which banking institutions located in New York State are authorized or required by Applicable Law or other governmental action to be closed.

" Business Employees " shall mean, as of any particular date: (i) the persons actively employed as of such date by HSBC or any of its Subsidiaries principally in connection with the Transferred Business; and (ii) the persons employed as of such date by HSBC or any of its Subsidiaries principally in connection with the Transferred Business who are absent from work on account of vacation, jury duty, funeral leave, personal day, sickness, short-term disability, workers compensation leave, military leave, leave under the Family Medical Leave Act or other approved leave of absence or for whom an obligation to return to active employment exists under a contractual obligation or law, in each case, that are listed on Schedule 1.1(c)(i) (as updated pursuant to Section 7.12 ).

" Business Material " shall have the meaning specified in Section 8.7(b) .

" Business Premises " shall mean, as applicable, the Purchased Real Property and/or the real property subject to a Real Property Lease.

" Card Rewards Liability " shall mean any Liabilities arising from Enhancements associated with the Credit Card Accounts and Receivables.

" Cash on Hand " shall have the meaning specified in Section 2.1(a)(13) .

" Claim Notice " shall have the meaning specified in Section 13.4(a) .

" Close of Business " shall mean the local time that the Banking Centers close to the public.

" Closing " shall have the meaning specified in Section 4.1 .

" Closing Date " shall have the meaning specified in Section 4.1 .

" Closing Payment " shall have the meaning specified in Section 3.1(b) .

" Closing Statement " shall have the meaning specified in Section 3.2(a) .

" Code " shall mean the Internal Revenue Code of 1986, as amended.

" Comparable Job Offer " shall mean an offer of employment with Purchaser or an Affiliate of Purchaser that sets forth the following terms of employment from the Closing Date through at least December 31, 2012: (i) a position requiring substantially comparable skills and abilities as the employee's position immediately prior to the Closing Date (it being understood that whether a position is managerial or non-managerial shall not in and of itself preclude an offer from being a Comparable Job Offer), (ii) does not involve a significant change in work schedule, (iii) has benefits that are no less favorable, in the aggregate, to those in effect immediately prior to the Closing Date, (iv) has an annual aggregate total compensation (the combination of annual base salary or rate of pay and incentive and commission arrangements) opportunity per performance period that is substantially the same as the aggregate total compensation (the combination of annual base salary or rate of pay and incentive and commission arrangements) opportunity in effect for such employee immediately prior to the Closing, (v) is at a work location not more than thirty-five (35) miles from such employee's work location immediately prior to the Closing Date, and (vi) includes a work status (full or part-time) that is not changed from that in effect immediately prior to the Closing Date.

" Confidentiality Agreement " shall mean the confidentiality agreement, dated as of August 10, 2011 among First Niagara Financial Group Inc., HSBC and Financial Institutions, Inc., the sole shareholder of Purchaser.

" Contract " shall mean any written agreement, contract, arrangement, bond note, commitment, franchise, indemnity, indenture, instrument, lease or license, together with any exhibits, schedules or documents executed or delivered in connection therewith and any modifications, amendments, restatements or other supplements thereto.

" Control " and the correlative terms "Controlling" and "Controlled" shall mean, as used with respect to any Person, possession of the power to direct or cause the direction of the management and policies of such Person, directly or indirectly, whether through the ownership of voting securities, by contract or otherwise.

" Controlled Group Liability " shall mean any and all liabilities (i) under Title IV of ERISA, (ii) under Section 302 of ERISA, (iii) under sections 412, 430 and 4971 of the Code, and (iv) as a result of a failure to comply with the continuation coverage requirements of Section 601 et seq . of ERISA and Section 4980B of the Code.

" Conversion " shall mean the conversion of the processing, reporting, payment and other systems associated with the Transferred Business from the systems of the HSBC Sellers to the systems of Purchaser.

" Conversion Plan " shall have the meaning specified in Section 8.6(c)(1) .

" Conversion Project Manager " shall have the meaning specified in Section 8.6(a) .

" CRA " shall mean the Community Reinvestment Act of 1977, as amended.

" CRA Assets " shall have the meaning specified in Section 2.1(a)(8) .

" Credit Card Accounts and Receivables " shall mean the accounts and Receivables related to the general purpose and small business credit cards issued by HSBC or an Affiliate of HSBC to its customers, including Banking Center Customers.

" Credit Documents " shall mean all documents evidencing or securing a Loan or Assumed Letter of Credit, in the possession of HSBC or its Subsidiaries (regardless of where located, including in file or imaging systems of HSBC or its Subsidiaries), including, without limitation, all original notes, reimbursement agreements, security agreements, deeds of trust, mortgages, loan agreements, and corresponding reports, certifications and disclosures required by Applicable Law, guarantees, sureties and insurance policies (including title insurance policies), applications and credit information, financial information, insurance information, signature cards, all information on obligors and borrowers and guarantors, taxpayer identification number certifications and records relating thereto, and all modifications, waivers and consents relating to any of the foregoing.

" Damages " shall mean all actions, costs, damages, disbursements, obligations, penalties, liabilities, losses, expenses, assessments, judgments, settlements or deficiencies (including any interest, penalties, investigation, legal, accounting and other reasonable out-of-pocket costs and expenses incurred in the investigation, collection, prosecution and defense of any action, suit, proceeding or claim and amounts paid in settlement, but not including indirect, incidental, exemplary, special, consequential or punitive damages that are imposed upon or otherwise incurred by the indemnified party).

" de minimis loss " shall have the meaning specified in Section 13.2(b) .

" Debt Protection Services " shall mean credit insurance, debt protection or similar services offered by or through HSBC or its Affiliates to obligors under the Credit Card Accounts and Receivables.

" Designated Footprint " shall mean all of the State of New York, except for the following counties: Bronx, Kings, Nassau, New York, Putnam, Queens, Richmond, Rockland, Suffolk and Westchester.

" Direct Banking Business " shall mean the business conducted by HSBC or its Affiliates of providing Banking Related Services through the telephone or the internet or other electronic media, including, but not limited to, internet-only checking accounts, savings accounts and certificates of deposit.

" Disclosure Schedule " shall mean, with respect to Purchaser or Assignor, a schedule delivered by it or them to the other upon the execution and delivery of this Agreement setting forth, among other things, items the disclosure of which is required under this Agreement, either in response to an express disclosure requirement contained in a provision of this

Agreement or as an exception to one or more of the representations and warranties or covenants contained in this Agreement; provided that the mere inclusion of an item in a Disclosure Schedule as an exception to a representation will not be considered an admission by the disclosing party that such item (or any non-disclosed item or information of comparable or greater significance) represents a material exception or fact, event or circumstance or that such item has had or is expected to result in a Material Adverse Effect, as the case may be; provided , further , that an item disclosed by either party in such party's Disclosure Schedule shall be deemed to be a disclosure against any other representation, warranty or covenant of such party in this Agreement if such disclosure would reasonably appear on its face to be a disclosure thereunder if repeated thereunder.

" Employee Pension Plan " shall mean any employee pension plan for which HSBC serves as a trustee, including, but not limited to, employee pension benefit plans as defined in Section 3(2) of ERISA, retirement plans qualified under the requirements of Section 401(a) of the Code, nonqualified deferred compensation plans, excess benefit plans and supplemental executive retirement plans.

" Employee Plans " shall have the meaning specified in Section 5.17(b) .

" Enhancements " shall mean all benefits, enhancements, features, offers, point programs, promotional rate programs, balance transfer programs, introductory rate programs, reward programs, rebate programs, fee-based programs (including "Identity Protector" and "Credit Keeper") and other similar services provided to card holders in connection with their respective Credit Card Accounts and Receivables.

" Environment " shall mean any soil, surface waters, wetlands, groundwaters, sediments, surface or subsurface strata, ambient air and any other environmental medium.

" Environmental Conditions " shall have the meaning specified in Section 8.9 .

" Environmental Law " shall mean any law, statute, regulation, rule, ordinance, by-law, order or other binding decision of any Governmental Entity regarding the protection of the Environment, Hazardous Materials, exposure to Hazardous Materials, worker health and safety and/or public health and safety.

" Environmental Objections " shall have the meaning specified in Section 8.9.

" ERISA " shall mean the Employee Retirement Income Security Act of 1974, as amended, and the regulations thereunder.

" ERISA Affiliate " shall mean, with respect to any entity, trade or business, any other entity, trade or business that is a member of a group described in Section 414(b), (c), (m) or (o) of the Code or Section 4001(b)(1) of ERISA that includes the first entity, trade or business, or that is a member of the same "controlled group" as the first entity, trade or business pursuant to Section 4001(a)(14) of ERISA.

" ESA " shall mean a Phase I ESA or a Phase II ESA.

" Excluded Assets " shall have the meaning specified in Section 2.1(b) .

" Excluded Contracts " shall mean any and all Contracts of the HSBC Sellers and their respective Affiliates that are not Assumed Contracts, including, but not limited to, all Contracts that apply primarily to operations of the HSBC Sellers or their respective Affiliates other than the Transferred Business and all data processing Contracts, regardless of scope.

" Excluded Deposits " shall mean any and all deposits of HSBC and its Affiliates that are not Assumed Deposits, including, but not limited to: (i) any proprietary deposits of HSBC of any of its Affiliates booked at the Banking Centers, (ii) any deposits associated with the Retained Businesses (including deposits booked at the Banking Centers) or the Non-Assigned Transferred Business, (iii) deposits acquired through the telephone or the internet or other electronic media from Persons with primary addresses located in the Designated Footprint that are not Banking Center Customers, (iv) any deposits that become Excluded Deposits pursuant to Section 7.11, and (v) any deposits of Retained Employees.

" Excluded Liabilities " shall have the meaning specified in Section 2.2(b) .

" Excluded Taxes " shall mean (A) any Income Taxes of any of the HSBC Sellers or Assignor or any of their respective Subsidiaries (whether or not relating to the Transferred Business), (B) any Income Taxes of any member of an affiliated, consolidated, combined, or unitary group of which any of the HSBC Sellers Assignor or any of their respective Subsidiaries was a member on or prior to the Closing Date, including pursuant to Treasury Regulation Section 1.1502-6 or any analogous or similar state, local or non-U.S. law or regulation, (C) any Income Taxes of any other Person imposed on any of the HSBC Sellers or Assignor any of their respective Subsidiaries as a transferee or successor, by contract or pursuant to any law, rule or regulation, and (D) any Non-Income Taxes relating to the Transferred Business for any Pre-Closing Period, provided that the allocation of the amount of Non-Income Taxes between the Pre-Closing Period and the Post-Closing Period shall be determined (i) with respect to Transfer Taxes in accordance with Article X , (ii) with respect to real and personal property and other Non-Income Taxes imposed on a time basis (other than any Transfer Taxes) by allocating pro rata on a time basis and (iii) with respect to any Non-Income Taxes not imposed on a time basis, on a closing of the books method.

" FDI Act " shall mean the Federal Deposit Insurance Act, as amended.

" FDIC " shall mean the Federal Deposit Insurance Corporation.

" Federal Funds Rate " shall mean, for any day, the rate per annum (rounded upwards, if necessary, to the nearest 1/100th of 1%) equal to the average of the rates on overnight Federal funds transactions with members of the Federal Reserve System arranged by Federal funds brokers on such day, as published by the Federal Reserve Bank of New York on the Business Day next succeeding such day; provided that, if such day is not a Business Day or the Federal Funds Rate is not so published for any day, the Federal Funds Rate for such day shall be such rate on such transactions on the next Business Day as so published on the next succeeding Business Day.

" Final Closing Statement " shall have the meaning specified in Section 3.3(a) .

" Final Schedules " shall have the meaning specified in Section 7.12 .

" FINRA " shall mean the Financial Industry Regulatory Authority.

" GAAP " shall mean generally accepted accounting principles in the United States of America consistently applied.

" Governmental Entity " shall mean any federal, state, local, domestic or foreign agency, court, tribunal, administrative body, arbitration panel, department or other legislative, judicial, governmental, quasi-governmental entity or Self-Regulatory Organization.

" Hazardous Material " shall mean any pollutant, contaminant, hazardous substance, toxic substance, hazardous material or hazardous waste as defined under any Environmental Law, including any petroleum product, asbestos-containing material, polychlorinated biphenyl or radon, and any other substances that by their nature or use are subject to regulation under Environmental Laws.

" HSBC " shall have the meaning specified in the Preamble.

" HSBC Entity Names " shall mean the names "HSBC," "HSBC Premier," the hexagon logo and any Trademark, name or logo related thereto, or employing the word "HSBC," "HSBC Premier," the hexagon logo or any derivation, variation, translation or adaptation thereof, and any Trademark, word, name or logo confusingly similar thereto or embodying any of the foregoing, whether alone or in combination with any other words, names, logos or trademarks, and whether registered or unregistered, including, but not limited to, the items listed on Schedule 2.1(b)(6) .

" HSBC Seller Name License " shall have the meaning specified in Section 8.7(b).

" HSBC Sellers " shall have the meaning specified in the Preamble.

" HSBC's Savings Plan " shall have the meaning specified in Section 9.1(e).

" HSI " shall have the meaning specified in the Preamble.

" HSR Act " shall mean the Hart-Scott-Rodino Antitrust Improvements Act of 1976.

" HTSI " shall have the meaning specified in the Preamble.

" Income Tax " shall mean any federal, state, local, or non-U.S. income Tax.

" Indemnified Parties " shall have the meaning specified in Section 13.3(a) .

" Indemnifying Party " shall have the meaning specified in Section 13.4(a) .

" Information " shall have the meaning specified in Section 7.5 .

" Intellectual Property " shall mean (i) all intellectual property, industrial property, proprietary and similar rights in any jurisdiction owned or held for use under license, whether or not subject to statutory registration or protection, and whether now known or hereafter recognized in any jurisdiction, including such rights in and to: (A) Trademarks; (B) inventions and discoveries (whether or not reduced to practice), all improvements thereto, all patents (including utility and design patents, industrial designs and utility models), registrations, invention disclosures and applications therefor, including divisions, revisions, supplementary protection certificates, continuations, continuations-in-part and renewal applications, and including renewals, extensions, reissues and re-examinations thereof; (C) published and unpublished works of authorship (including databases and other compilations of information, computer and electronic data processing programs, software, both source code and object code, flow charts, diagrams, descriptive texts and similar items), copyrights therein and thereto, and registrations and applications therefor, and all renewals, extensions, restorations and reversions thereof; (D) trade secrets, confidential business and technical information and any other confidential information (including ideas, research and development, know-how, formulae, drawings, prototypes, models, designs, technology, compositions, manufacturing, production and other processes and techniques, schematics, technical data, engineering, production and other designs, drawings, engineering notebooks, industrial models, software and specifications, business methods, customer lists, representative lists and supplier lists, and any other information meeting the definition of a trade secret under the Uniform Trade Secrets Act or similar laws) and (E) moral rights, design rights, mask works and rights of privacy and publicity; and (ii) in the case of (i)(A) through (i)(E), all benefits, privileges, causes of action and remedies relating to any of the foregoing, whether before or hereafter accrued (including the rights to sue for all past, present or future infringements or other violations of any rights in the assigned and to settle and retain proceeds from any such actions).

" IRA " shall mean an account created by a trust for the benefit of an individual or his or her beneficiary and that complies with the provisions of Section 408 or 408A of the Code.

" Keogh " shall mean an account created by a trust for the benefit of employees (some or all of whom are owner-employees) and that complies with the provisions of Section 401 of the Code.

" Knowledge " shall mean (i) with respect to Purchaser, the actual knowledge, without independent investigation, of the officers of Purchaser listed on Schedule 1.1(e) and (ii) with respect to Assignor, the actual knowledge, without independent investigation, of the officers of Assignor listed on Schedule 1.1(f) . For purposes of this definition, an officer shall be deemed to have actual knowledge of facts that would be reasonably expected to come to the attention of such officer in the course of the management reporting practices of Purchaser or Assignor, as applicable, and, with respect to Assignor, an officer shall be deemed to have actual knowledge of facts set forth in the written representations and warranties, and in any officer's certificates or written verifications made by the HSBC Sellers in or pursuant to the Primary Purchase Agreement.

" Landlord Consent " shall mean the consent (or waiver) of a landlord under a Real Property Lease or ATM Real Property Lease, as applicable, as shall be required pursuant to the terms of such Real Property Lease or ATM Real Property Lease, as applicable, to assign or sublease the subject Business Premises or ATM, as applicable, to Purchaser or its designated Subsidiary.

" Letter of Credit " shall mean any letter of credit, including any standby letter of credit, issued by HSBC in connection with the Transferred Business.

" Liabilities " shall mean any and all debts, liabilities, commitments and obligations of any kind, whether fixed, contingent or absolute, matured or unmatured, liquidated or unliquidated, accrued or not accrued, asserted or not asserted, known or unknown, determined, determinable or otherwise, whenever or however arising (including whether arising out of any contract or tort based on negligence or strict liability) and whether or not the same would be required by GAAP to be reflected in financial statements or disclosed in the notes thereto.

" License Agreement " shall mean the license agreement between the relevant HSBC Seller or Affiliate of HSBC and Purchaser, substantially in the form attached as Exhibit B hereto, with such changes as the parties may agree.

" Lien " shall mean any mortgage, deed of trust, easement, declaration, restriction, pledge, hypothecation, assignment, deposit arrangement, option, equity interest, encumbrance, lien (statutory or other), preference, participation interest, priority or other security agreement or preferential arrangement of any kind or nature whatsoever relating to that property, including any conditional sale or other title retention agreement, any financing lease having substantially the same economic effect as any of the foregoing and the filing of any financing statement under the UCC or comparable law of any jurisdiction to evidence any of the foregoing; provided , however , that no Lien shall be deemed to be created by this Agreement or the Primary Purchase Agreement.

" Loans " shall mean all loans or other extensions of credit, including, but not limited to, loans which have been partially charged off, interests in loan participations and assignments, customer liabilities on bankers acceptances as well as legally binding commitments and obligations to extend credit (including any unfunded or partially funded revolving loans, lines of credit, overdraft lines of credit and courtesy extensions or similar arrangements, and including short-term municipal investments (such as bond anticipation notes and revenue anticipation notes)), excluding (i) any loans made by HSBC or its Subsidiaries to HSBC or any of its Affiliates, (ii) Student Loans and (iii) Credit Card Accounts and Receivables.

" Losses " shall have the meaning specified in Section 13.2(a) .

" Material Adverse Effect " shall mean any circumstance or change in or effect on the Purchased Assets or the Assumed Liabilities that, individually or in the aggregate, with all other circumstances, changes or effects is materially adverse to, or would reasonably be expected to have a materially adverse effect on (a) the business, assets, properties, operations, results of operations or financial condition of the Purchased Assets or Transferred Business, taken as a whole ( provided , however , that with respect to this clause (a) "Material Adverse Effect" shall not include effects to the extent resulting from (i) changes after the date of this Agreement in general economic, legal, regulatory or political conditions (including the outbreak or escalation of hostilities or acts of terrorism to the extent not directly impacting Purchased Assets or facilities

or systems of the Transferred Business); (ii) changes after the date of this Agreement in general financial and capital market conditions, including changes generally in prevailing interest rates; (iii) changes after the date of this Agreement in general industry conditions affecting financial institutions, including banks and broker-dealers; (iv) changes after the date of this Agreement in law, International Financial Reporting Standards, GAAP or regulatory accounting principles, or authoritative interpretations thereof; (v) any action or omission required to be taken or omitted to be taken pursuant to the express terms of this Agreement; and (vi) the public announcement of this Agreement, including the impact thereof on customers, suppliers and employees and others having business relationships with the Banking Centers and, in the case of clauses (i) through (iv), only to the extent that such items do not have a disproportionate adverse effect on the Purchased Assets, the Assumed Liabilities or the Transferred Business, taken as a whole); or (b) the ability of Assignor to perform its obligations under this Agreement or the other Transaction Documents, or timely consummate the transactions contemplated hereby and thereby.

" Middle-Market and Large Corporate Banking Business " shall mean the business of providing Banking Related Services to Specified Enterprises, including existing and future Relationships with Specified Enterprises.

" Net Book Value " shall mean the book value net of any associated allowance, reserve or other contra-asset account, as reflected in the applicable HSBC Seller's books and records, determined in accordance with GAAP consistently applied; provided , however , that no Federal, state, local, or foreign income tax assets or tax liabilities shall be reflected.

" Non-Assigned Transferred Business " shall mean the entirety of the Transferred Business (as the term "Transferred Business" is defined in the Primary Purchase Agreement, and not as such term is defined in this Agreement) excluding the portion thereof that consists solely of the Transferred Business (as the term "Transferred Business" is defined in this Agreement).

" Non-Income Taxes " shall mean Taxes other than Income Taxes.

" Nonperforming Loan " shall mean, as of the Close of Business on the Closing Date, any Loan with respect to which (i) any principal or interest on such Loan or receivable shall be due and unpaid by the obligor thereunder for sixty (60) days or more prior to the Closing Date (other than loans guaranteed by the Veterans' Administration or the Federal Housing Administration), (ii) an obligor has filed or has had filed against such obligor proceedings in bankruptcy, trusteeship or receivership, (iii) the loans or receivables have been completely charged off, (iv) the balance is no longer owed by the obligor whether or not as a result of a settlement agreement between the obligor and HSBC or any of its Subsidiaries or (v) in the case of a mortgage loan, the loan has been repurchased by HSBC or any of its Subsidiaries.

" Notice Period " shall have the meaning specified in Section 13.4(a) .

" Outside Date " shall mean July 30, 2012, provided that if on the Outside Date all conditions to closing contained in Article XI that are capable of being completed prior to the Closing Date, other than completion of the activities necessary to effect the Conversion, have been satisfied or waived, Assignor may, in its sole discretion, upon written notice to Purchaser, automatically extend the Outside Date to August 31, 2012. If Assignor elects to extend the Outside Date, all references in this Agreement to the "Outside Date" will be to the Outside Date as extended.

" Permitted Liens " shall mean (i) Liens for Taxes, assessments or governmental charges or levies not yet due and payable or which although delinquent can be paid without penalty or are being contested in good faith by appropriate proceedings and for which adequate provision has been made on HSBC's books and records; (ii) Liens resulting from a filing by a lessor as a precautionary filing for a lease; (iii) Liens imposed by law, such as carriers', warehousemen's and mechanics' Liens and other similar liens arising in the ordinary course which secure payment of obligations not more than thirty (30) days past due or which are being contested in good faith by appropriate proceedings and for which adequate provision has been made on HSBC's books and records; (iv) purchase money security interests for the purchase or leasing of office equipment, computers, vehicles and other items of tangible personal property so long as the existence of such lease or other financing arrangement has been disclosed to the party to whom the applicable representation is made by express reference in the Disclosure Schedule and for which adequate provision has been made on HSBC's books and records; (v) in the case of real property, zoning, building, subdivision, environmental regulations, entitlement or other land use regulations; (vi) in the case of real property, easements, quasi-easements, encumbrances, licenses, covenants, rights-of-way, rights of re-entry or other restrictions, including any other agreements, conditions or restrictions or Liens, that would be shown by a current title report or any conditions that would be shown by a current survey or physical inspection; and (vii) any other Liens affecting the Purchased Assets which do not impede the ownership, operation or value of such Purchased Assets, taken as a whole, in any material respect.

" Person " shall mean an individual, a corporation, a partnership, an association, a limited liability company, a Government Entity, a trust or other entity or organization.

" Personal Property Leases " shall have the meaning specified in Section 2.1(a)(4) .

" Phase I ESA " shall mean a Phase I environmental site assessment conducted in accordance with the ASTM E1527 protocol.

" Phase II ESA " shall mean a Phase II environmental site assessment consisting of soil and/or groundwater sampling, conducted in accordance with the work plan approved by the HSBC Sellers pursuant to Section 7.1(a) .

" Post-Closing Period " shall mean any taxable period (or portion thereof) beginning after a Closing Date.

" Pre-Closing Period " shall mean any taxable period (or portion thereof) ending on (and including) a Closing Date or ending prior to a Closing Date.

" Prepaid Expenses " shall have the meaning specified in Section 2.1(a)(15) .

" Previously Disclosed " means, as of any given date, that the existence of a fact or condition was disclosed by one party to the other party through a Disclosure Schedule.

" Primary Closing Date " shall have the meaning specified in the Primary Purchase Agreement.

" Primary Purchased Assets " shall have the meaning specified in the Preamble.

" Primary Assumed Liabilities " shall have the meaning specified in the Preamble.

" Private Banking Business " shall mean the business of providing private banking and personal trust and investment services (including, but not limited to, brokerage, custody, insurance, investment banking, financial planning, estate planning, tax planning, liquidity management, lending, investment advisory, asset management and trust and fiduciary services) and Banking Related Services to Persons (including their Related Persons) with at least four million dollars ($4,000,000) in total investible assets or classified, as of the date hereof, as "Private Bank" customers pursuant to HSBC's internal customer classifications.

" Purchased Assets " shall have the meaning specified in Section 2.1(a) .

" Purchased ATMs " shall have the meaning specified in Section 2.1(a)(5) .

" Purchased Loans " shall have the meaning specified in Section 2.1(a)(6) .

" Purchased Overdrafts " shall mean overdrafts (whether specifically extended or courtesy) of the book balance of any accounts listed on Schedule 1.1(h) (as updated pursuant to Section 7.12 ).

" Purchased Personal Property " shall have the meaning specified in Section 2.1(a)(3) .

" Purchased Real Property " shall have the meaning specified in Section 2.1(a)(1) .

" Purchaser " shall have the meaning specified in the Preamble.

" Purchaser Indemnified Parties " shall have the meaning specified in Section 13.2(a) .

" Purchaser Objection " shall have the meaning specified in Section 3.3(c) .

" Purchaser Premium " shall have the meaning specified in Section 3.1(d).

" Purchaser Regulatory Approvals " shall have the meaning specified in Section 6.3 .

" Qualifying Remediation Cost " shall have the meaning specified in Section 8.9 .

" Real Property Leases " shall have the meaning specified in Section 2.1(a)(2) .

" Receivables " shall mean any amount posted as owing by an obligor under any credit card account, including any amounts owing for the payment of goods and services (including Debt Protection Services and Enhancements), cash advances, cash advance fees, access check fees, annual card membership fees, Accrued Interest and Fees and any other fee, expense or charge of every nature, kind and description whatsoever, less any amount owed by HSBC or any of its Affiliates to the obligor as a credit balance, but only to the extent that such amounts owed by the obligor are owned by HSBC or its Affiliates.

" Regulatory Approvals " shall mean, collectively, Assignor Regulatory Approvals and the Purchaser Regulatory Approvals.

" Related Person " shall mean, with respect to a Person, any other Person that is (i) an Affiliate of such Person, (ii) established for the benefit of such Person, or (iii) a member of such Person's immediate family.

" Relationships " shall mean any existing and future banking or other financial relationships with an identified Person or group of Persons and their Related Persons, including, but not limited to, any deposit, lending, investment, investment banking, asset management or financial advisory relationships and any accounts related thereto.

" Release " shall mean any release, migration, seepage, discharge, or disposal into the Environment, including, without limitation, as any of the foregoing may be defined in or pursuant to any Environmental Laws.

" Remediation Plan " shall have the meaning specified in Section 8.9 .

" Required Government Approvals " shall have the meaning specified in Section 11.1(b) .

" Retained Businesses " shall mean the following businesses (wherever conducted by HSBC and its Affiliates, including within the Designated Footprint) and the current and future Relationships associated therewith: (i) the Middle-Market and Large Corporate Banking Business, (ii) the Private Banking Business, (iii) the Student Loan Business, and (iv) the Direct Banking Business. "Retained Businesses" shall also include the business of providing other financial services (including Banking Related Services) to customers of such Retained Businesses and their Related Persons.

" Retained Employees " shall mean those employees of the HSBC Sellers or any of their Affiliates that will not or do not become Transferred Business Employees (as defined herein) on the Closing Date.

" Safe Deposit Agreements " shall have the meaning specified in Section 2.1(a)(7) .

" SBA " shall mean the United States Small Business Administration.

" SBA Loan " shall mean a Purchased Loan that is secured by an SBA guaranty whether in whole or in part; provided that no SBA Loan shall be considered a Purchased Loan unless and until such time as any required third-party (including the SBA) consents related to the transfer of such SBA Loan have been obtained.

" Self-Regulatory Organization " shall mean FINRA, the National Futures Association, the Chicago Board of Trade, the New York Stock Exchange, any national securities exchange (as defined in the Securities Exchange Act of 1934, as amended), any other securities exchange, futures exchange, contract market, any other exchange or corporation or similar self-regulatory body or organization.

" Settlement Procedures Agreement " shall mean the agreement attached to this Agreement as Exhibit E.

" Signage " shall mean any proprietary display, including a display bearing an HSBC Entity Name, used by any HSBC Seller or its Affiliates at the Banking Centers to identify the applicable HSBC Seller's or its Affiliates' place(s) of business or to advertise any HSBC Seller's or its Affiliates' products, services or brand.

" Sign-On Payment " shall have the meaning specified in Section 9.1(l) .

" Specified Enterprise " shall mean (x) a business organization that (i) had annual revenues greater than thirty million dollars ($30,000,000) in any of its last five (5) fiscal years and any Affiliate of such a business organization; (ii) is a business organization or an Affiliate of a business organization whose head office is located outside of the United States; (iii) had annual revenues greater than fifteen million dollars ($15,000,000), at least thirty percent (30%) of which in any of the last five (5) fiscal years was attributable to activities outside of the United States or sales to Persons located outside of the United States; (iv) has a Relationship with any non-U.S. Affiliate of the HSBC Sellers; or (v) is classified, as of the date hereof, as a "Middle Market Enterprise" or a "Global Banking and Markets" customer pursuant to HSBC's internal customer classifications; or (y) a Person listed on Schedule 1.1(k) .

" Student Loan Business " shall mean the business of HSBC and its Affiliates of making Student Loans to any Person, regardless of location.

" Student Loans " shall mean loans under the Federal Family Education Loan Program authorized by Part B, Title IV of the Higher Education Act of 1965, as amended or under the Department of Education's Direct Loan Program (including the published rules, regulations and interpretations of the Department of Education thereunder or thereof) or any other similar federal, state or private loans, including, but not limited to, private or alternative loans (such as undergraduate loans, graduate loans, health professional loans and continuing education loans).

" Sublease Agreement " shall have the meaning specified in Section 8.2(b) .

" Subsidiary " of a Person shall mean any other Person, of which such Person, directly or indirectly, owns securities or other ownership interest having (i) a majority of the economic interests of such entity or (ii) the ordinary voting power to elect a majority of the board of directors or such Person performing similar functions.

" Tax " shall mean any tax of any kind, including any federal, state, local and foreign income, profits, license, severance, occupation, windfall profits, capital gains, capital stock, transfer, registration, social security (or similar), production, franchise, gross receipts, payroll, sales, employment, use, property, excise, value added, estimated, stamp, alternative or add-on minimum, environmental, withholding and any other tax or like assessment, together with all interest, penalties and additions imposed with respect to such amounts and including any obligation to indemnify or otherwise assume or succeed to the tax liability of any other Person.

" Tax Return " shall mean any return, declaration, report, claim for refund or information return or statement filed or required to be filed with any Taxing Authority relating to Taxes, including any schedule or attachment thereto, and including any amendment thereof.

" Taxing Authority " shall mean any Governmental Entity having or purporting to exercise jurisdiction with respect to any Tax.

" Third-Party Claim " shall have the meaning specified in Section 13.4(a) .

" Trademarks " shall mean trademarks, service marks, certification marks, collective marks, Internet domain names, e-mail addresses, logos, product names and slogans, symbols, trade dress, assumed names, fictitious names, trade names, d/b/a's, brand names, business names, corporate names and any and every other form of trade identity and other indicia of origin, whether registered or unregistered, all applications and registrations for the foregoing, including all renewals of same, and all goodwill associated therewith and symbolized thereby.

" Transfer Taxes " shall mean all U.S. federal, state and local and all foreign or other excise, sales, use, value added, transfer (including real property transfer or gains), stamp, documentary, filing, recordation and other similar taxes and fees that may be imposed or assessed in connection with the transfer of the Transferred Business as contemplated under the Primary Purchase Agreement or this Agreement, together with any interest, additions or penalties with respect thereto and any interest in respect of such additions or penalties.

" Transferred Business " shall mean the following businesses, in each case as conducted as of July 30, 2011 by the HSBC Sellers or any of their respective Subsidiaries through the Banking Centers: (i) the consumer banking business serving the retail market (including deposit taking, lending, securities brokerage, insurance brokerage and other consumer banking business conducted in the Banking Centers), including the business relating to the Assumed Deposits and Purchased Loans; (ii) Business Banking; (iii) the Wealth Management Business; and (iv) the other business and operations conducted in or through the Banking Centers; provided , however , that the term "Transferred Business" shall not include (i) any businesses or operations primarily related to the Retained Businesses or (ii) any businesses or operations related to (x) any of the branches and offices, including related drive-thru teller facilities, of the HSBC Sellers and their Subsidiaries or of Assignor and its Subsidiaries, other than the Banking Centers, or (y) any of the Primary Purchased Assets or Primary Assumed Liabilities, other than the Purchased Assets and Assumed Liabilities. For the avoidance of doubt, the reference above in this definition of Transferred Business to "July 30, 2011" shall not be construed as limiting the assets and liabilities that are included in the Transferred Business to those that actually existed at July 30, 2011.

" Transferred Business Banking Relationships " shall mean the Business Banking Relationships held by HSBC and its Subsidiaries that are listed on Schedule 1.1(l) (as updated pursuant to Section 7.12 ).

" Transferred Business Employees " shall mean the Business Employees and the Affiliated Employees who accept Purchaser's offer of employment.

" Transferred Wealth Management Relationships " shall mean the Relationships listed on Schedule 1.1(m) , as well as all assets under management associated with each of such Relationships.

" Transition Coordinators " shall have the meaning specified in Section 7.8 .

" Transition Services Agreement " shall mean the Transition Services Agreement between the HSBC Sellers, Assignor and Purchaser, substantially in the form attached as Exhibit A , with such changes as the parties thereto may agree.

" Transitional Period " shall have the meaning specified in Section 8.7(b) .

" UCC " shall mean the Uniform Commercial Code, as in effect in New York State or any other applicable state.

" Update Date " shall have the meaning specific in Section 7.12.

" WARN Act " shall mean the federal Worker Adjustment and Retraining Notification Act, as amended, or any similar state, local, or foreign laws with respect to any event affecting Business Employees or Affiliated Employees **.**

" Wealth Management Business " shall mean the business of providing financial planning, insurance, investment advisory and similar services through financial advisors or licensed bankers located in the Banking Centers (regardless of where the customer is located), other than to Retained Employees.

" Wealth Management Employees " shall have the meaning specified in Section 5.17(a) and identified on Schedule 1.1(c)(ii) .

Section 1.1 Interpretation . (a) Unless the context otherwise requires:

(1) references herein to specific Articles, Sections, Subsections, Exhibits or Schedules shall refer, respectively, to Articles, Sections, Subsections, Exhibits or Schedules of this Agreement;

(2) references to any agreement or other document are to such agreement or document as amended, modified, supplemented or replaced from time to time;

(3) references to any statute or regulation refer to such statute or regulation as amended, modified, supplemented or replaced from time to time (and, in the case of statutes, include any rules and regulations promulgated under the statute) and references to any Section of any statute or regulation include any successor to such section;

(4) references to any Government Entity include any successor to such Government Entity;

(5) the words “hereof,” “herein,” and “hereunder” and words of similar import, when used in this Agreement, shall refer to this Agreement as a whole and not to any particular provision of this Agreement;

(6) the terms defined in the singular have a comparable meaning when used in the plural, and vice versa;

(7) the terms “Dollars” and “$” mean U.S. Dollars;

(8) wherever the word “include,” “includes,” or “including” is used in this Agreement, it shall be deemed to be followed by the words “without limitation”; and

(9) references herein to any gender include the other gender.

(b) The table of contents and headings contained in this Agreement are for reference purposes only and do not limit or otherwise affect any of the provisions of this Agreement.

(c) The parties to this Agreement have participated jointly in the negotiation and drafting of this Agreement. In the event of an ambiguity or a question of intent or interpretation, this Agreement shall be construed as if drafted jointly by the parties, and no presumption or burden of proof shall arise favoring or disfavoring any party by virtue of the authorship of any provision of this Agreement.

## ARTICLE II

## ASSIGNMENT AS TO PURCHASE AND SALE OF PURCHASED ASSETS AND ASSUMPTION OF ASSUMED LIABILITIES

Section 2.1 Purchase and Sale of Transferred Business . (a) *Purchased Assets.* At the Closing, and subject to the terms and conditions set forth herein, and consistent with Sections 2.5, 8.9 and 14.2 of the Primary Purchase Agreement, Assignor will direct the applicable HSBC Sellers to sell, assign, transfer, convey and deliver, or cause one or more of its Subsidiaries to sell, assign, transfer, convey and deliver, free and clear of Liens (other than Permitted Liens) to Purchaser, and Purchaser will purchase, acquire and accept from each applicable HSBC Seller or its applicable Subsidiaries, a portion of the Primary Purchased Assets, consisting solely of all right, title, interest and obligations of each applicable HSBC Seller or its applicable Subsidiaries in, to, and under the following assets, properties, rights, Contracts and claims of each applicable HSBC Seller or its applicable Subsidiaries, wherever located, whether tangible or intangible, real, personal or mixed (the “ Purchased Assets ”):

(1) the real property listed on Schedule 2.1(a)(1) and related improvements and fixtures, together with all assignable real property rights, benefits and appurtenances pertaining thereto (the “ Purchased Real Property ”);

(2) subject to the receipt of any required third-party consents, the real property leases, subleases, licenses or other Contracts listed on Schedule 2.1(a)(2) (the " Real Property Leases "");

(3) the furniture, equipment, materials and supplies owned by the HSBC Sellers and their respective Subsidiaries as of the Closing Date and located at the Business Premises, but excluding all proprietary systems or proprietary materials located in the Business Premises (collectively, the " Purchased Personal Property ");

(4) subject to the receipt of any required third-party consents, the leases, subleases, licenses or other contracts associated with the furniture, equipment, materials and supplies leased by the HSBC Sellers and their respective Subsidiaries as of the Closing Date and located at the Business Premises, (collectively, the " Personal Property Leases ");

(5)(i) the ATM units and the real property on which such ATMs are located that are owned by HSBC or any of its Subsidiaries in connection with the Transferred Business, a list of which, as of the date hereof, is set forth on Schedule 2.1(a)(5)(i) (the " Purchased ATMs "), and (ii) subject to the receipt of any required third-party consents, all of HSBC's or HSBC's Subsidiaries' rights with respect to the leases, subleases, licenses or other contracts pursuant to which HSBC or any of its Subsidiaries leases real property on which ATMs are located, in connection with the Transferred Business, a list of which leases, as of the date hereof, is set forth on Schedule 2.1(a)(5)(ii) (the " ATM Real Property Leases ");

(6) the Loans (including any servicing and other rights relating thereto of HSBC or any of its Subsidiaries) made or purchased by HSBC or any of its Subsidiaries in connection with the Transferred Business that are listed on Schedule 2.1(a)(6) , together with all Contracts evidencing or executed and delivered in connection with such Loans and including all obligations to make additional extensions of credit thereunder and all related collateral, excluding Nonperforming Loans (collectively, the " Purchased Loans "). The parties agree that no Nonperforming Loans shall be included in the Purchased Loans;

(7) all safe deposit Contracts and leases for safe deposit boxes located at the Banking Centers (the " Safe Deposit Agreements ");

(8) the CRA-eligible loans, other than any Nonperforming Loans, listed on Schedule 2.1(a)(8) (the " CRA Assets ");

(9) subject to the receipt of any required third-party consents the Letters of Credit issued by HSBC or any of its Subsidiaries that are listed on, Schedule 2.1(a)(9) together with all reimbursement agreements and related documents (including, but not limited to, any collateral documents) with respect to the Assumed Letters of Credit and all collateral in the possession of or otherwise granted to HSBC or any Affiliate of HSBC in connection therewith (collectively, the " Assumed Letters of Credit ").

(10) subject to the receipt of any required third-party consents, the rights of the HSBC Sellers or their respective Subsidiaries with respect to the operating Contracts under which goods or services are provided exclusively in connection with the Transferred Business as conducted at the Banking Centers, (the " Assumed Contracts ," and together with the Real Property Leases, ATM Real Property Leases, Assumed Letters of Credit and Personal Property Leases, the " Assumed Agreements "");

(11) all books, records and other data relating primarily to the Transferred Business, including all files (including suspicious activity reports to the extent permitted by Applicable Law), customer and supplier lists, mailing lists, accounting records, documentation or records primarily relating to the Transferred Business or the administration of the Assumed Agreements and the Assumed Deposits, real property files with respect to Purchased Real Property and Real Property Leases (including lease documentation, maintenance records, plans and permits, to the extent in the possession of the HSBC Sellers or any of their respective Subsidiaries), catalogs, printed materials and all technical and other data relating to the Transferred Business other than (i) corporate minute books and, except for Forms W-8 and W-9 and similar tax forms provided to the HSBC Sellers or any of their respective Subsidiaries by customers of the Transferred Business, income tax records of the HSBC Sellers or any of their respective Subsidiaries, (ii) personnel files and records and (iii) books and records to the extent relating to accounts that have terminated prior to Closing; provided , however , that the HSBC Sellers and their respective Subsidiaries shall have the right to retain copies of all such books, records and other data that are part of the Purchased Assets to the extent reasonably necessary for, and solely for use in connection with, tax, regulatory, litigation or other legitimate, non-competitive purposes;

(12) any and all rights of the HSBC Sellers and their respective Subsidiaries that are by their terms transferrable and that have arisen, or that arise, under or pursuant to warranties, representations, indemnifications, reimbursement agreements, letters of credit, insurance policies to the extent held for the benefit of the HSBC Sellers and their respective Subsidiaries in connection with the Transferred Business or guaranties in favor of the HSBC Sellers and their respective Subsidiaries or made for the benefit of the HSBC Sellers and their respective Subsidiaries by their respective customers, predecessors in interest, suppliers, vendors, or Affiliates of any of the foregoing, to the extent relating to the Purchased Assets or the Assumed Liabilities, in either case with respect to the period following the Closing;

(13) all U.S. cash on hand at the Banking Centers at the Close of Business on the Closing Date, including vault cash, petty cash, tellers' cash, prepaid postage, bank orders, checks, certified checks and cash equivalents (exclusive of the contents of any safe deposit boxes) located at the Banking Centers, as determined by a cash count to be mutually conducted jointly by HSBC, Assignor and Purchaser but excluding any cash contained in ATMs not physically located at the Banking Centers and cash contained in security vehicles or otherwise maintained in vaults by vendors on behalf of HSBC or HSBC's Subsidiaries, whether or not associated with the Transferred Business (the " Cash on Hand ");

(14) accrued income receivable and accounts receivable of the HSBC Sellers and their respective Subsidiaries to the extent arising from the Transferred Business and existing as of the Closing Date (the " Banking Receivables "), as set forth on the general ledger of the applicable HSBC Seller maintained in the ordinary course of business of the HSBC Sellers in accordance with the internal controls and procedures of the HSBC Sellers, consistently applied;

(15) all prepaid charges and fees of the HSBC Sellers and their respective Subsidiaries to the extent arising in the Transferred Business and existing as of the Closing Date (the " Prepaid Expenses "), as set forth on the general ledger of the applicable HSBC Seller maintained in the ordinary course of business of the HSBC Sellers in accordance with the internal controls and procedures of the HSBC Sellers, consistently applied;

(16) the Purchased Overdrafts;

(17) subject to the receipt of any required third-party consents, any income, commissions, compensation or allowances receivable or payable after the Closing Date in respect of annuities (including additional premium payments thereto after the Closing Date) and interests in mutual funds sold by the HSBC Sellers or any of their respective Subsidiaries in the conduct or operation of the Transferred Business on or prior to the Close of Business on the Closing Date;

(18) the benefits, rights, rights of action and claims (express or implied) related to the Purchased Assets and Assumed Liabilities acquired and assumed by Purchaser pursuant to the terms of this Agreement; and

(19) subject to the receipt of any required third-party consents, the Transferred Wealth Management Relationships and the Transferred Business Banking Relationships.

(b) *Excluded Assets* . Notwithstanding anything to the contrary contained in Section 2.1(a) , Purchaser will not purchase, assume or otherwise acquire any assets of the HSBC Sellers or any of their respective Affiliates that are not expressly included in the Purchased Assets (collectively, the " Excluded Assets "), including, by way of example only, the following assets, properties, rights, Contracts and claims, wherever located, whether tangible or intangible, real, personal or mixed:

(1) all assets, properties, rights, Contracts and claims, including Loans and extensions of credit in process, wherever located, whether tangible or intangible, real, personal or mixed, primarily related to the Retained Businesses;

(2) other than the Real Property Leases and ATM Real Property Leases, all leases, subleases, licenses or other Contracts pursuant to which the HSBC Sellers or any of their respective Affiliates leases, subleases or licenses real property;

(3) all Nonperforming Loans and Loans to Retained Employees;

(4) the Excluded Contracts;

(5) all assets related to employee benefit arrangements of any HSBC Seller or Assignor or any of their respective Affiliates, including the Employee Plans;

(6) all Intellectual Property of the HSBC Sellers and their respective Affiliates, including all right, title and interest in and to all proprietary or licensed software, systems or programs or computer software agreements of the HSBC Sellers and their respective Affiliates, including any rights (ownership, licensed or otherwise) to any of the HSBC Entity Names and any other Trademarks of the HSBC Sellers or their respective Affiliates, including those identified on Schedule 2.1(b)(6) ;

(7) all books, records and other data that cannot, without unreasonable effort or expense, be separated from books and records maintained by the HSBC Sellers or their respective Affiliates in connection with the Retained Businesses or to the extent that such books, records and other data relate to Excluded Assets, Excluded Liabilities or Business Employees or Affiliated Employees who do not become Transferred Business Employees, and all personnel files and records; provided that, to the extent permitted under, and in accordance with, Section 7.1(b) , Assignor shall use commercially reasonable efforts to cause the HSBC Sellers to provide Purchaser with access to any such books, records and other data for which the above-referenced separation would cause the HSBC Sellers to incur unreasonable effort or expense;

(8) all licenses, charters, and legal entities of the HSBC Sellers or their respective Affiliates; and

(9) all Credit Card Accounts and Receivables.

(c) Purchaser understands, acknowledges and agrees that the assignment by Assignor pursuant to this Agreement relates solely to, and Purchaser, pursuant to this Agreement, is purchasing only, the Purchased Assets (and assuming only the Assumed Liabilities) specified in this Agreement and, except as may be expressly provided for in this Agreement, Purchaser has no interest in any other Relationship which the HSBC Sellers, Assignor or any of their respective Affiliates has or may have with any Banking Center Customer (subject to Section 7.9 ) or any other customer of any HSBC Seller, Assignor or any of their respective Affiliates. Purchaser further understands, acknowledges and agrees that each HSBC Seller and its Affiliates are retaining any and all rights and claims which any of them may have, including, but not limited to, indemnification or reimbursement rights, with respect to the Purchased Assets and the Assumed Liabilities, to the extent that such rights or claims relate to the conduct of the Transferred Business prior to the Closing Date, unless such rights or claims relate to liabilities, duties, responsibilities and obligations of any HSBC Seller, Assignor or any of their Affiliates arising or accruing on or prior to the Closing Date which are included in the Assumed Liabilities.

Section 2.2 Assumption of Liabilities . (a) *Assumed Liabilities.* From and after the Closing, and subject to the terms and conditions set forth herein, and consistent with Sections 2.5, 8.9 and 14.2 of the Primary Purchase Agreement, Purchaser will assume, and will pay, perform and discharge as they become due, all of the following liabilities and obligations of the HSBC Sellers and Assignor solely to the extent such liabilities and obligations are required to be satisfied, paid or performed after the Closing Date (collectively, the " Assumed Liabilities "):

(1) the Assumed Deposits;

(2) the Assumed Agreements, except for any liability or obligation under such Assumed Agreements (i) to be performed prior to the Closing Date or (ii) arising from a breach of, or default under, any such Assumed Agreements by the HSBC Sellers or their respective Affiliates;

(3) all liabilities and obligations accruing after the Closing Date that relate to or arise from the employment of the Transferred Business Employees by Purchaser after the Closing Date, including all compensation, benefits, severance, workers' compensation and welfare benefit claims and employment-related liabilities incurred after the Closing Date;

(4) any Accrued Interest and Fees on the Assumed Deposits, where such Accrued Interest and Fees is not otherwise deducted in determining the Net Book Value of any Purchased Asset; and

(5) any Liability, duty or obligation of any nature whatsoever, whether accrued, absolute, primary or secondary, contingent or otherwise, direct or indirect, asserted or unasserted, known or unknown that arises based on the conduct of the Transferred Business after the Closing Date relating to the Transferred Business, the Purchased Assets or the Assumed Liabilities, of whatever kind or nature, primary or secondary, direct or indirect.

Purchaser's obligations under this Section 2.2(a) shall not be subject to offset or reduction by reason of any actual or alleged breach of any representation, warranty or covenant contained in this Agreement or the Primary Purchase Agreement or any document delivered in connection herewith or any right or alleged right to indemnification hereunder or thereunder. All periodic fees or charges shall be shared on a proportionate basis as of the Closing Date in accordance with Section 3.3(b) .

(b) *Excluded Liabilities* . Notwithstanding anything to the contrary set forth in Section 2.2(a), other than the Assumed Liabilities, neither Purchaser nor any of its Subsidiaries will assume or be bound by any Liability, duty or obligation of any of the HSBC Sellers or Assignor or any of their respective Affiliates (collectively, the " Excluded Liabilities "), including, by way of example only, the following Liabilities of the HSBC Sellers and their respective Affiliates (and, if applicable, Assignor):

(1) any Liability, duty or obligation of any of the HSBC Sellers or their respective Affiliates of any nature whatsoever, whether accrued, absolute, primary or secondary, contingent or otherwise, direct or indirect, asserted or unasserted, known or unknown, that is primarily related to the Retained Business or the Non-Assigned Transferred Business;

(2) any Liability, duty or obligation of any of the HSBC Sellers, Assignor or their respective Affiliates of any nature whatsoever, whether accrued, absolute, contingent or otherwise, asserted or unasserted, known or unknown, to the extent relating to or arising from or in connection with any Excluded Asset;

(3) the Excluded Deposits;

(4) any compensation or benefit Liabilities to Business Employees or Affiliated Employees with respect to services provided to HSBC or its Affiliates prior to the Closing Date (including, without limitation, all liabilities for accrued but unused paid time off) and any Liabilities under the Employee Plans, whether or not such claims are submitted for payment or reimbursement on or before the Closing Date, except to the extent otherwise provided under Section 9.1 ;

(5) any Controlled Group Liability arising under any Employee Plan or any employee benefit plan sponsored, maintained or contributed to or by any current or former ERISA Affiliate of the HSBC Sellers or any of their respective Subsidiaries;

(6) any liability for Excluded Taxes (whether or not relating to the Transferred Business); and

(7) the Card Rewards Liability.

Notwithstanding anything in Section 13.9 to the contrary, in no event shall Article XIII limit the retention by, as applicable, the HSBC Sellers or Assignor of Excluded Liabilities as between Purchaser and Assignor and/or the HSBC Sellers; provided that , in accordance with Section 13.11 , nothing herein shall provide Purchaser with any right or claim against the HSBC Sellers, including for indemnification.

Section 2.3 Sale and Transfer of Servicing . Purchased Loans shall be sold by the HSBC Sellers on a servicing-released basis (and without limitation, any related escrow deposits shall be transferred to Purchaser). As of the Closing Date, all rights, obligations, liabilities and responsibilities with respect to the servicing of the Purchased Loans after the Closing Date will be assumed by Purchaser.

Section 2.4 Effect of Assignment of Rights and Obligations . Assignor and Purchaser acknowledge and agree (i) that Purchaser shall not have any rights, claims for indemnification or other claims against any HSBC Seller, (ii) that no HSBC Seller shall have any liability of any kind to Purchaser as a result of the transactions provided for in this Agreement except and unless and then only to the extent an HSBC Seller expressly agrees in writing and (iii) that neither HSBC nor any of its Affiliates is a party to this Agreement.

## ARTICLE III

## CLOSING PAYMENT AND ADJUSTMENTS

Section 3.1 Closing Payment . (a) On the Closing Date, and pursuant to the Assignment from Assignor, Purchaser shall acquire the Purchased Assets and shall assume the Assumed Liabilities.

(b) Pursuant to Section 3.2(b) , on the Closing Date, Assignor shall pay to Purchaser (or, in the event that the payment calculated pursuant hereto is a negative number, Purchaser shall pay to Assignor the absolute value of such figure) by electronic wire transfer in an amount in U.S. dollars (the " Closing Payment ") equal to:

(1) an amount equal to the aggregate Net Book Value, as set forth on the Closing Statement (as defined in Section 3.2(a) ), of the sum of (i) the Assumed Deposits, plus Accrued Interest and Fees thereon and (ii) the other Assumed Liabilities, MINUS

(2) an amount (the " Aggregate Asset Amount ") equal to the sum of the following, as set forth on the Closing Statement (as defined in Section 3.2(a) ):

(i) the aggregate face amount of Cash on Hand as of the Close of Business on the Closing Date; PLUS

(ii) the aggregate Appraised Value of the Purchased Real Property; PLUS

(iii) the sum of (x) the unpaid principal balance of the Purchased Loans and the Purchased Overdrafts, as of the Close of Business on the Closing Date, in each case plus Accrued Interest and Fees thereon, and (y) the aggregate Net Book Values, as of the Close of Business on the Closing Date, of each of the following: the Purchased Personal Property; the Purchased ATMs; the Assumed Letters of Credit; and the Prepaid Expenses.

(c) The parties agree that the commercial intention of the calculation of the Closing Payment as set out in this Section 3.1 is that the Transferred Business sold pursuant to this Agreement has sufficient assets (cash or otherwise) to cover its liabilities.

(d) On the Closing Date, Purchaser shall pay to Assignor, by electronic wire transfer an amount (the " Purchaser Premium ") in U.S. dollars equal to four percent (4.0%) of the average daily balance (including Accrued Interest and Fees) of the Assumed Deposits for the calendar month immediately preceding the month in which the Closing occurs and this amount shall be subject to adjustment (and adjusted) as indicated in Section 3.2 .

Section 3.2 Closing Statement and Closing Payment . (a) *Closing Statement* . Assignor shall prepare a statement substantially in the form of Exhibit 3.2 (the " Closing Statement ") showing the Aggregate Asset Amount and the calculation thereof, reflecting the Purchased Assets and Assumed Liabilities, which shall be prepared based on the draft Closing Statement as of the Update Date, provided to Assignor by the HSBC Sellers.

(b) *Closing Payment; Purchaser Premium.* At the Closing, Assignor shall pay to Purchaser (or, if applicable, Purchaser shall pay to Assignor) the Closing Payment, calculated pursuant to Section 3.1(b) , as reflected on the Closing Statement. The amount paid at the Closing shall be subject to subsequent adjustment based on the Final Closing Statement, prepared pursuant to Section 3.3 . In addition, at the Closing, Purchaser shall pay to Assignor the Purchaser Premium calculated pursuant to Section 3.1(d) based on the Closing Statement. The amount so paid by Assignor including on account of the Purchaser Premium shall be subject to adjustment based on the Final Closing Statement with the Purchaser Premium computed based on the month-to-date average daily balance (including Accrued Interest and Fees) of the Assumed Deposits for the calendar month in which the Closing occurs up to and including the Closing Date.

Section 3.3 Final Closing Statement, Allocation of Fees and Expenses, and Post-Closing Adjustment . (a) *Final Closing Statement.* Not later than five (5) Business Days after Assignor has received the Final Closing Statement (as defined in the Primary Purchase Agreement and with respect to the Banking Centers), Assignor shall deliver to Purchaser a statement, as of the Close of Business on the Closing Date, and prepared in accordance with GAAP applied consistently with the practices used in the preparation of the Closing Statement except as and to the extent that this Agreement provides for different valuation methodologies for particular categories of Purchased Assets and Assumed Liabilities, showing the Aggregate Asset Amount and the calculation thereof, reflecting the Purchased Assets and Assumed Liabilities, as of the Close of Business on the Closing Date (as reflected on the Final Schedules), and reflecting such other adjustments as are appropriate in accordance with Section 3.3(b) (the " Final Closing Statement "). Assignor shall afford Purchaser and its accountants and attorneys the opportunity to review all work papers and documentation used by Assignor in preparing the Final Closing Statement.

(b) *Allocation of Fees and Expenses.* Except as otherwise provided herein, to effect the intention of the parties that the economics of the Transferred Business (except to the extent of the Banking Receivables and the Prepaid Expenses purchased by Purchaser pursuant to Section 2.1(a)(14) and Section 2.1(a)(15) , respectively) shall be for the account of the applicable HSBC Seller up to the Close of Business on the Closing Date and thereafter shall be for the account of Purchaser (as assignee of a portion of Assignor's rights under the Primary Purchase Agreement) all fees and expenses with respect to the Transferred Business that relate to both the period before and the period after the Closing Date, shall reflect a proration between Purchaser (as assignee of a portion of Assignor's rights under the Primary Purchase Agreement), on the one hand, and the applicable HSBC Seller, on the other hand, based on the full amount of the latest available bills or statements on the basis of a three hundred sixty-five (365)-day calendar year (except to the extent accrued on a three hundred sixty (360)-day calendar year, in which case proration shall be based on a three hundred sixty (360)-day calendar year) as of the Close of Business on the Closing Date. In furtherance of the foregoing, all operating expenses related to the Transferred Business, as the case may be, including, but not limited to, rent, utility, maintenance, and service expenses attributable to operations of the Transferred Business until the Close of Business on the Closing Date shall be paid by and shall be the obligation of the

applicable HSBC Seller in accordance with the Primary Purchase Agreement. All of such expenses attributable to operations of the Transferred Business after the Close of Business on the Closing Date shall be paid by and be the obligation of Purchaser. All real and personal property, use and other Taxes imposed on a time basis with respect to the Transferred Business shall reflect a proration between Purchaser (as assignee of a portion of Assignor's rights under the Primary Purchase Agreement), on the one hand, and the applicable HSBC Seller, on the other hand, in the same manner based on the full amount of the Tax for the relevant period, unless such amount is not reasonably ascertainable, in which case the full amount of the Tax for the prior period shall be used. Any rental income from subtenants or other third-party occupants of real property shall also reflect a proration between Purchaser (as assignee of a portion of Assignor's rights under the Primary Purchase Agreement), on the one hand, and the applicable HSBC Seller, on the other hand, as of the Close of Business on the Closing Date. To the extent that any Tax, fees or expenses described in this Section 3.3(b) are not discovered or the actual amount thereof is not known prior to the final determination of the Final Closing Statement, the parties shall cooperate with one another so that the applicable HSBC Seller and Purchaser each pays its appropriate share of any such fee or expense, depending upon whether such fee or expense relates to the period before or after the Close of Business on the Closing Date. The parties intend that the pro rations provided for in this Section 3.1(b) shall be calculated in the same manner as provided for in Section 3.3(b) of the Primary Purchase Agreement, and Purchaser shall pay to Assignor (or to the applicable HSBC Seller if so directed by Assignor) any pro rations payable by Purchaser hereunder and Assignor shall pay (or shall use commercially reasonable efforts to cause HSBC to pay directly to Purchaser) any pro rations owing to Purchaser.

(c) Except as otherwise expressly provided herein, the determination of the Final Closing Statement shall be final and binding on the parties hereto, unless, within thirty (30) days after receipt by Purchaser of the Final Closing Statement, Purchaser shall notify Assignor and HSBC in writing of its disagreement with any amount included therein or omitted therefrom (a " Purchaser Objection "), in which case, if the parties are unable to resolve the disputed items within ten (10) Business Days of the receipt by Assignor and HSBC of notice of such disagreement, such items shall be determined by a nationally recognized independent accounting firm selected by mutual agreement between Assignor, HSBC and Purchaser; provided , however , that in the event the fees of such firm as estimated by such firm would exceed fifty percent (50%) of the net amount in dispute, the parties agree that such firm will not be engaged by either party and that such net amount in dispute will be equally apportioned between Assignor and Purchaser. Such accounting firm shall be instructed to resolve the disputed items within ten (10) Business Days of engagement, to the extent reasonably practicable. The determination of such accounting firm shall be final and binding on the parties hereto. The fees of any such accounting firm shall be divided equally between Assignor and Purchaser.

(d) Not later than the Close of Business on the second (2 nd ) Business Day following the final determination of the Final Closing Statement, pursuant to Section 3.3(c) (the " Adjustment Payment Date "), Assignor and Purchaser shall effect the transfer of any funds as may be necessary to reflect changes in the Purchased Assets and Assumed Liabilities (including without limitation, changes in the month-to-date average daily balance (including Accrued Interest and Fees) of the Assumed Deposits) between the Closing Statement and the Final Closing Statement and resulting changes in the Closing Payment and/or Purchaser Premium, together with interest thereon computed from the Closing Date up to, but not including, the

Adjustment Payment Date, at the Federal Funds Rate; provided , however , that if a Purchaser Objection is timely made, within two (2) Business Days of the date of such Purchaser Objection, Assignor and Purchaser shall effect the transfer of any funds as may be necessary to reflect the undisputed portion of the changes in the Purchased Assets and Assumed Liabilities between the Closing Statement and the Final Closing Statement and resulting adjustments to the Closing Payment and/or Purchaser Premium, together with interest thereon computed from the Closing Date up to, but not including, the date of such payment at the Federal Funds Rate.

Section 3.4 Allocation of Consideration . (a) Promptly upon Assignor's receipt from HSBC of the draft allocation statement prepared by HSBC pursuant to Section 3.4 of the Primary Purchase Agreement, Assignor shall deliver to Purchaser a draft allocation statement setting forth the proposed calculation of the aggregate amount of consideration paid by Purchaser in respect of the Transferred Business, together with such adjustments as are appropriate to take into consideration the difference, if any, between the amount of the Purchaser Premium under this Agreement and the amount of the Premium and the Liquidity Payment (each as defined in the Primary Purchase Agreement) allocable to the Transferred Business under the Primary Purchase Agreement (the " Allocation Statement ") and the proposed allocation in the form required in Section 1060 of the Code of such aggregate amount among the Purchased Assets. If within twenty (20) days after Purchaser's receipt of the draft Allocation Statement, Purchaser shall not have objected in writing to such draft statement, then such draft statement shall become the Allocation Statement. In the event that Purchaser objects in writing within such twenty (20) day period, Assignor and Purchaser shall negotiate in good faith, including with HSBC, to resolve the dispute; provided , however , that Purchaser acknowledges that the methodology used to prepare the Allocation Statement in connection with the Primary Closing (as defined in the Primary Purchase Agreement) shall govern the preparation of the Allocation Statement under this Agreement.

(b) The parties hereto agree to report the allocation of the total consideration among the Purchased Assets in a manner consistent with the Allocation Statement, and agree to act consistently in the preparation and filing of all Tax Returns (including filing Form 8594 with their respective federal income Tax Returns for the taxable year that includes the Closing Date and any other forms or statements required by the Code, Treasury regulations, the Internal Revenue Service or any applicable state or local Taxing Authority) and in the course of any Tax audit, Tax review or Tax litigation relating thereto; provided that neither Assignor nor any of its Affiliates nor Purchaser or any of its Affiliates will be obligated to litigate any challenge to such allocation of the aggregate consideration by a Taxing Authority.

## ARTICLE IV

## THE CLOSING

Section 4.1 Closing Time and Place . The consummation of the transfer of the Transferred Business, including the Purchased Assets and the Assumed Liabilities, and the payment of the Closing Payment, in each case as contemplated by this Agreement, shall take place at a closing (the " Closing "), to be held at 10:00 a.m., New York time, at the offices of Assignor in Buffalo, New York, on the date that Purchaser and Assignor agree in writing, in consultation with, and subject to the prior approval of the HSBC Sellers (the " Closing Date ").

The Closing shall be deemed effective as of 11:59 p.m., New York time, on the Closing Date. If the Closing Date occurs on a day other than a Business Day, any wire transfers that otherwise would have been made on the Closing Date shall be evidenced on the Closing Date through arrangements mutually agreed by the parties, and such wire transfers shall occur on the first Business Day following the Closing Date.

Section 4.2 Closing Documents . (a) *Deliveries of Assignor* . At the Closing, Assignor shall deliver or cause the applicable HSBC Sellers to deliver the following documents to Purchaser, all of which shall be in a form reasonably satisfactory to Purchaser:

(1) the updated Schedules contemplated by Section 7.12 ;

(2) the officers' certificates contemplated by Section 11.3(c)

(3) a bargain and sale deed without a covenant against grantor's acts (or its substantive equivalent) for the Purchased Real Property;

(4) a bill of sale, in substantially the form attached hereto as Exhibit 4.2(a)(4) (the " Bill of Sale "), executed by the HSBC Sellers transferring to Purchaser free and clear of Liens (other than Permitted Liens) all of the right, title and interest of the HSBC Sellers and their respective Subsidiaries in and to the Purchased Assets;

(5) a duly executed Assignment and Assumption Agreement, in substantially the form attached hereto as Exhibit 4.2(a)(5) (the " Assignment and Assumption Agreement "), assigning the right, title and interest of the HSBC Sellers and their respective Subsidiaries in and to the Purchased Assets, free and clear of Liens (other than Permitted Liens) and providing for the assumption of the Assumed Liabilities by Purchaser;

(6) an affidavit pursuant to Section 1445 of the Code certifying to the non-foreign status of Assignor and each HSBC Seller and each of their respective Subsidiaries, as applicable, conveying real property located in the United States hereunder;

(7) the Purchased Loans, duly and properly endorsed to Purchaser by HSBC, together with all notes, guarantees, agreements and other evidence thereof and all collateral and security interests securing the Purchased Loans in the possession of HSBC or its Subsidiaries and all necessary assignments (if applicable, in recordable form), endorsements and other instruments of conveyance as may be necessary under the circumstances; provided that all such assignments, endorsements and other instruments of conveyance shall be without recourse as to collection to HSBC;

(8) subject to the relevant provisions of Exhibit A, possession of, or access to, all Credit Documents in whatever form or medium (including imaged documents), all collateral in the custody or possession of HSBC or its Subsidiaries, and all funds held in escrow, in each case, relating to the Purchased Loans or the Assumed Letters of Credit;

(9) all other documents and instruments reasonably necessary to (i) transfer the Purchased Assets to Purchaser, (ii) reflect the assumption of the Assumed Liabilities by Purchaser or (iii) effectuate the other transactions to be taken by the HSBC Sellers contemplated by this Agreement; and

(10) a certificate, dated the Closing Date and validly executed on behalf of Assignor by an appropriate officer certifying that the conditions specified in Section 11.4(a) of the Primary Purchase Agreement have been satisfied.

(b) *Deliveries of Purchaser*. At the Closing, Purchaser shall deliver the following documents to the HSBC Seller and to Assignor, all of which shall be in form reasonably satisfactory to Assignor:

(1) the officer's certificate contemplated by Section 11.2(c) ;

(2) a duly executed Assignment and Assumption Agreement;

(3) an executed Bill of Sale; and

(4) all other documents and instruments reasonably necessary to (i) receive the Purchased Assets from the HSBC Sellers or any of their respective Subsidiaries, (ii) assume the Assumed Liabilities from the HSBC Sellers or any of their respective Subsidiaries or (iii) effectuate the other transactions to be taken by Purchaser contemplated by this Agreement.

Section 4.3 Delivery of Purchased Assets . Assignor shall or shall cause the HSBC Sellers to deliver to Purchaser at the Close of Business on the Closing Date (or at such other date if mutually agreed to by Purchaser and Assignor) all of the fixed assets and other tangible personal property to the extent not located on or at the Business Premises (including real property files, Cash on Hand, and keys to safe deposit boxes) constituting Purchased Assets hereunder being purchased at such Closing.

## ARTICLE V

## REPRESENTATIONS AND WARRANTIES OF ASSIGNOR

Except as Previously Disclosed, Assignor represents and warrants to Purchaser, as of the date hereof (or as of such other date as may be expressly provided in any representation or warranty), as follows:

Section 5.1 Organization . Assignor is a national bank duly organized, validly existing and in good standing under the laws of the United States.

Section 5.2 Authority; Capacity . Assignor has the power and authority to enter into and perform this Agreement and any other documents executed pursuant hereto. This Agreement and any other documents or instruments executed pursuant hereto and the execution, delivery and performance hereof and thereof have been duly authorized and approved by all

necessary corporate action on the part of Assignor, and this Agreement and the instruments and documents executed pursuant hereto constitute, or when executed will constitute, the valid and binding obligations of Assignor, enforceable against Assignor in accordance with their terms, except as enforcement may be limited by receivership, conservatorship and supervisory powers of bank regulatory agencies generally as well as by bankruptcy, insolvency, reorganization, moratorium or other laws of general applicability relating to or affecting creditors' rights, or the limiting effect of rules of law governing specific performance, equitable relief and other equitable remedies or the waiver of rights or remedies.

Section 5.3 Consents and Approvals . None of Assignor or any of its Subsidiaries, nor to the Knowledge of Assignor, the HSBC Sellers or any of their respective Subsidiaries, is required to obtain any order, permit, consent, approval or authorization of, or required to make any declaration or filing with, any Governmental Entity or third party in connection with the execution and delivery of this Agreement and the transactions contemplated hereby, except (i) compliance with the applicable requirements of the HSR Act and the approvals or non-objections of the Governmental Entity listed on Schedule 5.3 (the " Assignor Regulatory Approvals ") and (ii) other consents or approvals, the failure of which to obtain would not reasonably be expected to, individually or in the aggregate, have a Material Adverse Effect.

Section 5.4 No Breaches; Defaults . Assuming the receipt of all regulatory approvals referenced in Section 5.3 , the execution and delivery of this Agreement and any instruments or other documents executed pursuant hereto by Assignor do not and the consummation of the transactions contemplated by this Agreement, will not constitute: (i) a breach or violation of or default under any law, rule, regulation, judgment, order, governmental permit or license of Assignor or to which Assignor is subject, which breach, violation or default would prevent or materially delay Assignor from being able to perform its obligations under this Agreement in all material respects, or (ii) a breach or violation of or a default under the articles of association (or certificate of incorporation, as applicable) or bylaws of Assignor.

Section 5.5 Compliance with Law . Except as disclosed on Schedule 5.5 , Assignor and its Subsidiaries have conducted and are conducting their business in all material respects in compliance with all Applicable Law, including, without limitation, all regulations, orders, and opinions of the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation, and, except as would not, individually or in the aggregate, result in a material adverse effect, neither Assignor nor any of its Subsidiaries is subject to any order or ruling directed to it by, or memorandum of understanding with, any Governmental Entity. Except as disclosed on Schedule 5.5 , to the Knowledge of Assignor, each HSBC Seller and its Subsidiaries: (i) is in compliance in all material respects with Applicable Law applicable to the Purchased Assets, Assumed Liabilities and Transferred Business; (ii) has conducted and is conducting the Transferred Business (including, without limitation, all matters relating to the Business Employees, Affiliated Employees and the Business Premises) in compliance in all material respects with Applicable Law; and (iii) has properly administered in all material respects all accounts within the Transferred Business for which any of them acts as a fiduciary, including accounts for which any of them serves as a trustee, agent, custodian, personal representative, guardian, conservator or investment advisor, in accordance with the terms of the agreements governing such accounts and Applicable Law, provided that the environmental matters addressed by Section 5.19 shall be

governed exclusively by Section 5.19 and not this Section 5.5 and compliance with law matters specifically addressed elsewhere in this Article V shall be governed by such specific representations and not this Section 5.5 . Assignor has received no notice of and has no Knowledge of any planned or threatened objection by any community group to the transactions contemplated hereby.

Section 5.6 Litigation and Related Matters . There are no actions, suits, or proceedings, whether civil, criminal or administrative, pending or, to the Knowledge of Assignor, threatened against or affecting Assignor which would materially impede, delay or prevent Assignor or any of its Subsidiaries from entering into this Agreement or performing its terms. Except as disclosed on Schedule 5.6 , to the Knowledge of Assignor, as of the date of this Agreement there are no actions, suits, or proceedings, whether civil, criminal or administrative, pending or, threatened related to the Transferred Business, Purchased Assets or Assumed Liabilities, against or affecting any HSBC Seller which would (i) reasonably be expected to, individually or in the aggregate, have a Material Adverse Effect or (ii) prevent or materially delay Assignor from being able to perform the material obligations of Assignor under this Agreement.

Section 5.7 No Brokers or Finders . Except for Goldman, Sachs & Co. and Sandler O'Neill & Partners, L.P., whose fees will be paid by Assignor, there is no investment banker, broker, finder or other intermediary that has been retained by or is authorized to act on behalf of Assignor or any of its Affiliates who might be entitled to any fee or commission from Assignor or its Affiliates in connection with the transactions contemplated hereby.

Section 5.8 Operations . Since March 31, 2011, and except as otherwise expressly contemplated by this Agreement, and to the Knowledge of Assignor, the HSBC Sellers and their respective Subsidiaries have in all material respects conducted the Transferred Business only in, and have not engaged in any material transaction with respect to the Transferred Business other than in, the ordinary course of business consistent with past practice. Since March 31, 2011, there has not been any event, occurrence or circumstance that has had or that would reasonably be expected to have, individually or in the aggregate, a Material Adverse Effect.

Section 5.9 Real Property Leases . (a) Assignor has provided Purchaser with true and correct copies of all Real Property Leases and a list of all of the tenants or other occupants of the Business Premises subject to a Real Property Lease as of the date set forth on such list.

(b) Each Real Property Lease is in full force and effect in all material respects, and, to the Knowledge of Assignor, neither any HSBC Seller nor the landlord is in default under any of its respective obligations thereunder.

(c) Except as would not, individually or in the aggregate, reasonably be expected to have a Material Adverse Effect, to the Knowledge of Assignor, none of the HSBC Sellers or any of their respective Subsidiaries has received any written notice of a nonrenewal of any Real Property Lease or a condemnation proceeding relating to any real property that is subject to a Real Property Lease that would materially affect a property or its intended use.

Section 5.10 Purchased Real Property . (a) On the Closing Date, Assignor shall cause the applicable HSBC Seller or its applicable Subsidiaries to convey good and marketable title to the Purchased Real Property free and clear of all Liens, except for Permitted Liens.

(b) Except as disclosed on Schedule 5.10 , to the Knowledge of Assignor, none of the HSBC Sellers or any of their respective Subsidiaries has received any written notice of a condemnation proceeding relating to the Purchased Real Property.

Section 5.11 Assumed Deposits . The HSBC Sellers have the right to transfer or assign each of the Assumed Deposits to Purchaser. The Assumed Deposits have been solicited, originated and administered in accordance with the terms of the respective governing documents and all Applicable Law and regulations, in each case, in all material respects. The Assumed Deposits are insured by the FDIC to the fullest extent permitted in accordance with the FDI Act and the HSBC Sellers and their Subsidiaries have paid all assessments due thereunder. Each of the agreements relating to the Assumed Deposits is valid, binding, and enforceable upon its respective parties in accordance with its terms except as enforceability may be limited by bankruptcy, insolvency, reorganization, moratorium, or other similar laws affecting creditors' rights, and by the exercise of judicial discretion in accordance with general principles applicable to equitable and similar remedies.

Section 5.12 Purchased Loans (a) Each Purchased Loan (i) is evidenced by notes, agreements, or other evidences of indebtedness that are true, genuine and what they purport to be, materially complete and correct sets of originals of which (or, to the extent an original is not necessary for the enforcement thereof, true, correct and complete copies thereof) are included in the Credit Documents which will be delivered, or made available, to Purchaser pursuant to Section 2.1(a) ; (ii) constitutes a legal, valid and binding obligation of the respective borrower(s) or obligor(s), enforceable, to the Knowledge of Assignor, by the holder thereof in accordance with its terms subject, as to enforcement, to applicable bankruptcy, insolvency, reorganization, liquidation and other similar laws and equitable principles relating to or affecting the enforcement of creditors' rights generally, (iii) is free from all material claims, defenses, rights of rescission, any discount, allowance, set-off, counterclaim, presently pending bankruptcy or other defenses by the borrower, and (iv) complies in all material respects with Applicable Law, including all applicable lending laws and regulations.

(b) Each Purchased Loan (i) was originated by an HSBC Seller or a Subsidiary of an HSBC Seller (or, in the case of a Purchased Loan that was purchased by any HSBC Seller or a Subsidiary of an HSBC Seller, by the Person making such Purchased Loan): (x) in the ordinary course of business at the time such Purchased Loan was made; and (y) in accordance with Applicable Law, in all material respects; and (ii) to the extent it is identified as secured in Schedule 2.1(a)(6) , is secured by a valid, perfected and enforceable Lien on the secured property described in the applicable security agreement.

(c) Each Purchased Loan has been originated, created, maintained, serviced and administered in all material respects in accordance with (i) Applicable Law; (ii) the applicable HSBC Seller's or its applicable Subsidiaries' written loan servicing and operating procedures as in effect from time to time; and (iii) the respective Credit Documents governing each Purchased Loan.

(d) Immediately following the sale of each Purchased Loan, Purchaser will own such Purchased Loan free and clear of any encumbrance, equity, participation interest, Lien, pledge, charge, claim or security interest.

(e) To the Knowledge of Assignor, neither the borrower nor any guarantor of any of the Purchased Loans is in bankruptcy and, there are no facts, circumstances or conditions with respect to any such Purchased Loans, the collateral therefor or the borrower's credit standing, that could reasonably be expected to cause any such Purchased Loans to become delinquent or adversely affect the collectability, the value or the marketability of such Purchased Loans.

(f) To the Knowledge of Assignor, none of the rights or remedies under the Credit Documents relating to the Purchased Loans has been amended, modified, waived, subordinated or otherwise altered by any HSBC Seller or any Subsidiary of an HSBC Seller, except as evidenced by a written instrument which is a part of the file with respect to the Purchased Loan and appropriately recorded as necessary to establish all rights of mortgagee into assignee.

(g) The HSBC Sellers may transfer or assign the Purchased Loans to Purchaser without the approval or consent of any obligor thereunder and without creating any breach of any agreement pursuant to which another party has purchased a participating interest in the Purchased Loan.

(h) Subject to obtaining any required consent from any third party, including the SBA, with respect to each SBA Loan that is subject to a guaranty, such guaranty is in full force and effect and is freely transferrable as an incident to the sale of each SBA Loan.

(i) None of the Purchased Loans are serviced by third parties, and there are no obligations, agreements or understandings that could result in any Purchased Loan becoming subject to any such third party servicing.

(j) Except as set forth in this Section 5.12 , Assignor does not make any representation or warranty to Purchaser relating to the Purchased Loans.

Section 5.13 Intentionally Omitted

Section 5.14 Assumed Contracts . To the Knowledge of Assignor, each party to any Assumed Contract to which an HSBC Seller or any of its Subsidiaries is a party has performed in all material respects its obligations thereunder to the extent that such obligations to perform have accrued, no party is in default under such Assumed Contracts and none of such Assumed Contracts was entered into outside the ordinary course of business of any applicable HSBC Seller or its Subsidiaries. Each such Assumed Contract constitutes the legal, valid and binding obligation of the applicable HSBC Seller or its Subsidiaries, and, to the Knowledge of Assignor, the respective third party, and is enforceable in accordance with its terms subject as to enforcement, to applicable bankruptcy, insolvency, reorganization, liquidation and other similar laws and equitable principles relating to or affecting the enforcement of creditors' rights generally.

Section 5.15 Regulatory Matters . There are no pending, or to the Knowledge of Assignor, threatened disputes or controversies between Assignor or any HSBC Seller and any federal, state or local governmental authority that (i) would reasonably be expected to prevent or materially delay Assignor from being able to perform its obligations under this Agreement or (ii) would reasonably be expected to impair the validity or consummation of this Agreement or the transactions contemplated hereby. Neither Assignor nor, to the Knowledge of Assignor, any HSBC Seller has received any notice from any Governmental Entity indicating that such Governmental Entity would oppose or not promptly grant or issue its consent or approval, if requested, with respect to the transactions contemplated hereby and has no reason to believe that, if requested, any Governmental Entity required to approve the transactions contemplated hereby would oppose or not promptly grant or issue its consent or approval.

Section 5.16 Necessary Permits . Except as set forth on Schedule 5.16 , the HSBC Sellers and their respective Subsidiaries have all material permits, licenses, orders, ratings and approvals of all Governmental Entities necessary for them to operate the Transferred Business substantially as presently operated (the " Necessary Permits "), and (i) all of the Necessary Permits are in full force and effect in all material respects, and (ii) to the Knowledge of Assignor, no suspension or cancellation of any Necessary Permit has been threatened.

Section 5.17 Business Employees, Affiliated Employees and Benefits . (a) Schedule 1.1(c)(i) and Schedule 1.1(c)(ii) list, as of December 22, 2011, all Business Employees (excluding Retained Employees) who are identified as employed in the Transferred Business by the internal records of the HSBC Sellers, and the Affiliated Employees, respectively, as well as the position, corporate and functional title, status as exempt or non-exempt, identification number, hire date, status as full or part-time, status as active or on leave, if on leave, the date leave commenced, geographic location and remuneration (including base salary, base wage, commission schedule and prior year's incentive award, in each case, as applicable) of each such Business Employee or Affiliated Employee. Schedule 1.1(c)(ii) will separately identify the Affiliated Employees who are employed by HSI in connection with the Wealth Management Business (the " Wealth Management Employees "). Within five (5) Business Days prior to the Closing Date, and at such other dates as reasonably requested by the Purchaser, but no more frequently than once every thirty (30) days, Assignor shall update Schedule 1.1(c)(i) and Schedule 1.1(c)(ii ) in electronic format, to reflect any newly hired Business Employees, any additional hired or identified Affiliated Employees, those Business Employees or Affiliated Employees whose employment has terminated, and any other change in the other information on Schedule 1.1(c)(i) or Schedule 1.1(c)(ii) , respectively; provided , however , that no updated information shall be provided with respect to those Business Employees or Affiliated Employees previously listed on Schedule 1.1(c)(i) or Schedule 1.1(c)(ii) , respectively, who have rejected a Comparable Job Offer or who have not received a Comparable Job Offer from Purchaser as of such date.

(b) Schedule 5.17(b) lists all of the material employee benefit and compensation plans, programs, agreements and arrangements, including all pension, retirement, retiree medical, profit-sharing, thrift, savings, deferred compensation, compensation, incentive, equity-based, change in control, severance, welfare, fringe benefit, perquisite and similar plans sponsored, maintained or contributed to by the HSBC Sellers or any of their respective ERISA Affiliates and in which any Business Employee or Affiliated Employee is eligible to participate,

excluding any nonqualified deferred compensation plan under which benefits, other than interest credits, are no longer being earned or accrued or to which contributions are no longer being made (the " Employee Plans "). Assignor has made available to Purchaser copies of the most recent summary plan descriptions and annual enrollment guides with respect to the Employee Plans.

Section 5.18 Labor Contracts and Relations . Except as set forth on Schedule 5.18 , with respect to Business Employees or Affiliated Employees, none of the HSBC Sellers or any of their respective Subsidiaries is a party to any collective bargaining agreement, contract, or other agreement or understanding with a labor union or labor organization, and none of the HSBC Sellers or any of their respective Subsidiaries is the subject of a proceeding asserting it has committed an unfair labor practice or seeking to compel it to bargain with any labor organization as to wages and conditions of employment, nor, to the Knowledge of Assignor, is any such proceeding threatened, nor is there any strike or other labor dispute by the Business Employees or Affiliated Employees pending or threatened, nor does Assignor or any HSBC Seller have Knowledge of any activity involving any Business Employees or Affiliated Employees seeking to certify a collective bargaining unit or engaging in union organizational activity.

Section 5.19 Environmental Matters . Except as set forth on Schedule 5.19 :

(a) To the Knowledge of Assignor, each HSBC Seller and its respective Subsidiaries is currently in compliance in all material respects with all Environmental Laws applicable to any Business Premises, and with respect to any operations or activities conducted by any HSBC Seller or any of its Subsidiaries on such Business Premises. Neither Assignor nor any of the HSBC Sellers or their respective Subsidiaries has received any written notice that there has been any failure to comply with Environmental Laws applicable to the Purchased Real Property, and with respect to any operations or activities conducted by any HSBC Seller or any of its Subsidiaries on such premises except any such notice with respect to a failure to comply which has been fully resolved.

(b) To the Knowledge of Assignor, the HSBC Sellers and their respective Subsidiaries have all material environmental permits and approvals required under Environmental Laws for all facilities and improvements and any operations activities presently conducted by the HSBC Sellers and their respective Subsidiaries on the Purchased Real Property, and, to the Knowledge of Assignor, each HSBC Seller and its Subsidiaries is currently in compliance with all such permits and approvals.

(c) There is no suit, claim, demand, action, consent order, or proceeding pending or, to the Knowledge of Assignor, threatened in which Assignor or any HSBC Seller or any of their respective Subsidiaries or, with respect to threatened proceedings, could reasonably be expected to be named as a defendant, responsible party or potentially responsible party (i) for alleged noncompliance, with any Environmental Laws or (ii) relating to the Release into or presence in the Environment of any Hazardous Materials, in either case at or on any Purchased Real Property.

(d) To the Knowledge of Assignor, there have been no Releases into the Environment of any Hazardous Materials in, on, from, under or affecting any Business Premises which would reasonably be expected to have a material adverse impact on such Business Premises.

(e) Assignor has provided to Purchaser copies of all documentation in its possession or under its control pertaining to environmental conditions at the Business Premises.

Section 5.20 Books and Records . With respect to each Assumed Agreement and all accounts related thereto, to the Knowledge of Assignor, the accounting, financial and other books and records kept by the HSBC Sellers and their Subsidiaries are in all material respects complete and accurate and have been maintained in the ordinary course of business and in compliance with in all material respects with Applicable Law. The books and records included within the Purchased Assets include all customary branch, customer and customer-related information reasonably necessary to service the Assumed Deposits and Purchased Loans on an ongoing basis, and to otherwise operate the Transferred Business being acquired under this Agreement in substantially the manner currently operated by the HSBC Sellers.

Section 5.21 Safe Deposit Boxes . Each HSBC Seller and its Subsidiaries is in compliance, in all material respects, with the terms and conditions of the Safe Deposit Agreements.

Section 5.22 Insurance Coverage . The business and operations of the Transferred Business are insured against such risks and in such amounts and with such coverage deemed appropriate by management of the HSBC Sellers and not in a manner materially inconsistent with industry practice for a global financial institution. Since January 1, 2010, all premiums payable under all insurance policies and fidelity bonds that currently cover the assets, business, operations and employees of the Transferred Business have been timely paid in all material respects, and the HSBC Sellers and their respective Subsidiaries have otherwise complied in all material respects with the terms and conditions of all such policies and bonds. Since January 1, 2010, there is no material claim by the HSBC Sellers or any of their respective Subsidiaries related to the Transferred Business pending under any such policies or bonds as to which coverage has been denied by the underwriters of such policies or bonds applicable to the Transferred Business. To the Knowledge of Assignor, no insurer has threatened a termination of coverage under any such policies or bonds, except notices required to be given by Applicable Law prior to the expiration of any policy or bond advising that coverage will terminate by its terms if such policy or bond is not renewed.

Section 5.23 Taxes . (a) All Tax Returns required to have been filed with respect to the Transferred Business (such Tax Returns, the " Tax Returns ") have been filed with the appropriate Taxing Authority; each such Tax Return is true, complete and correct in all material respects. All Taxes shown to be due on such Tax Returns, and all Taxes due and attributable to the Transferred Business, have been timely paid, withheld and timely paid to the appropriate Taxing Authority, or reflected in an appropriate tax reserve in accordance with GAAP on the financial statements of the applicable HSBC Sellers, other than those Taxes the failure of which to be paid would not result in a Lien on the Purchased Assets or become a liability of Purchaser.

(b) No notice of deficiency or assessment of Taxes has been received from any Taxing Authority with respect to the Transferred Business. There is no material dispute or claim concerning any Tax relating to the Transferred Business either (A) claimed or raised by any Taxing Authority in writing or (B) of which Assignor has Knowledge. There are no Liens on any of the Purchased Assets that arose in connection with any failure (or alleged failure) to pay any Tax (whether or not such Tax relates to the Transferred Business).

Section 5.24 Investment Products; Personnel . Each Business Employee or Affiliated Employee who is required by Applicable Law to be licensed to sell non-deposit investment products, including insurance and securities, is validly licensed and in good standing with each applicable regulator, including FINRA and the state insurance regulators.

Section 5.25 Transferred Wealth Management Relationships . (a) (1) *Customer Relationships* Each Transferred Wealth Management Relationship has been in all material respects originated and serviced (i) to the Knowledge of Assignor, in conformity with applicable policies of HSI, (ii) in accordance with the terms of any applicable instrument or agreement governing the relationship with such customer, (iii) in accordance with any instructions received from such customers and (iv) in compliance with Applicable Law. To the Knowledge of Assignor, each instrument or agreement governing a Transferred Wealth Management Relationship has been duly and validly executed and delivered by HSI and the other contracting parties, and each such instrument or agreement constitutes a valid, binding and enforceable obligation of the parties thereto, subject as to enforcement, to applicable bankruptcy, insolvency, reorganization, liquidation and other similar laws and equitable principles relating to or affecting the enforcement of creditors' rights generally.

(2) To the Knowledge of Assignor, as of the date hereof, HSI has not received any written notice from any customer related to the Transferred Wealth Management Relationships that it intends to bring a claim against HSI or any of its Affiliates in connection with the Transferred Wealth Management Relationships.

(b) *Conduct of the Wealth Management Business* : To the Knowledge of Assignor, HSI currently has in place an effective system of policies and procedures and a supervisory system reasonably designed to achieve and maintain material compliance with all applicable federal and state securities laws (and the rules of any applicable Self-Regulatory Organization). To the Knowledge of Assignor, the Affiliated Employees associated with the Transferred Wealth Management Relationships, in their capacities as employees, have complied in all material respects with Applicable Laws.

(c) *Financial Advisors* : Schedule 5.25(c) lists each Affiliated Employee who, as of the date hereof, is a financial advisor associated with the Transferred Wealth Management Relationships, the assets under management attributable to each such financial advisor and the Banking Center(s) in which each such financial advisor is located. As of the date hereof, to the Knowledge of Assignor, HSI has not received any notice that any financial advisor listed in Schedule 5.25(c) has terminated or intends to terminate his or her employment.

Section 5.26 The Primary Purchase Agreement . Exhibit C is a true, correct and complete copy of the Primary Purchase Agreement and all of the Exhibits and Schedules thereto. As of the date of this Agreement, Assignor has no Knowledge of any breach of any representation or warranty made by an HSBC Seller in the Primary Purchase Agreement or of any breach of any covenant or agreement of an HSBC Seller in the Primary Purchase Agreement.

Section 5.27 Limitations on and Disclaimer of Representations and Warranties . Except for its representations and warranties expressly set forth in this Agreement, Assignor makes no representations or warranties, express or implied, as to the Transferred Business, the Banking Centers, the Purchased Assets or the Assumed Liabilities. Purchaser acknowledges that notwithstanding the representations or warranties in this Agreement or in the Primary Purchase Agreement, neither HSBC nor any of its Affiliates makes any representations or warranties whatsoever to Purchaser, either express or implied.

Section 5.28 Financing . On the Closing Date, Assignor or the HSBC Sellers, as applicable, will have sufficient cash, available lines of credit or other sources of immediately available funds to enable it to make the Closing Payment and to promptly pay any other amounts to be paid by it under this Agreement on the Closing Date.

## ARTICLE VI

## REPRESENTATIONS AND WARRANTIES OF PURCHASER

Except as Previously Disclosed, Purchaser hereby represents and warrants to Assignor, as of the date hereof (or as of such other date as may be expressly provided in any representation or warranty), as follows:

Section 6.1 Organization . Purchaser is a bank duly organized, validly existing and in good standing under the laws of the State of New York. Purchaser has all the requisite corporate power and corporate authority, as well as all requisite licenses, franchises, permits, qualifications and similar permissions and authorities, to own the Purchased Assets, assume the Assumed Liabilities and to carry on the Transferred Business and is duly qualified to do business in and is in good standing as a foreign corporation or other entity in each jurisdiction where the ownership of the Purchased Assets and the conduct of the Transferred Business requires such qualification, except where the failure to be so qualified or be in good standing would not, individually or in the aggregate, have a material adverse effect on Purchaser.

Section 6.2 Authority; Capacity . Purchaser has the power and authority to enter into and perform this Agreement and any instruments or other documents executed pursuant hereto. This Agreement and any instruments or other documents executed pursuant hereto, and the execution, delivery and performance hereof and thereof have been duly authorized and approved by all necessary corporate action on the part of Purchaser, and this Agreement and the instruments and documents executed pursuant hereto constitutes, or when executed will constitute, the valid and binding obligations of Purchaser, enforceable against Purchaser in accordance with its terms, except as enforcement may be limited by receivership, conservatorship and supervisory powers of bank regulatory agencies generally as well as bankruptcy, insolvency, reorganization, moratorium or other laws of general applicability relating to or affecting creditors' rights, or the limiting effect of rules of law governing specific performance, equitable relief and other equitable remedies or the waiver of rights or remedies.

Section 6.3 Consents and Approvals . (a) Neither Purchaser nor any of its Affiliates is required to obtain any order, permit, consent, approval or authorization of, nor required to make any material declaration or filing with, any Governmental Entity or third-party in connection with the execution and delivery of this Agreement or the consummation of the transactions contemplated hereby, except compliance with the applicable requirements of the HSR Act and the approvals or non-objections of the Governmental Entities set forth on Schedule 6.3(a) (such approvals, the " Purchaser Regulatory Approvals ").

(b) There are no pending, or to the Knowledge of Purchaser, threatened disputes or controversies between Purchaser or any of its Affiliates and any Governmental Entity, including, without limitation, with respect to capital requirements, that (i) would reasonably be expected to prevent or delay Purchaser from being able to perform its obligations under this Agreement or (ii) would reasonably be expected to impair the validity or consummation of this Agreement or the transactions contemplated hereby. Purchaser has not received any indication from any Governmental Entity that such Governmental Entity would oppose or refuse to grant or issue its consent or approval, if required, with respect to the transactions contemplated hereby and has no reason to believe that, if requested, any Governmental Entity required to approve the transactions contemplated hereby would oppose or not promptly grant or issue its consent or approval.

(c) As of the date hereof, both currently and after giving effect to the transactions contemplated hereby (on a pro forma basis): (i) Purchaser is and will be at least "well-capitalized", as defined in the FDI Act; and (ii) Purchaser meets all capital requirements, standards and ratios required by each state or federal bank regulator with jurisdiction over Purchaser, including, without limitation, any such higher requirement, standard or ratio as applied to Purchaser by state or federal bank regulator, and no such regulator has indicated that it will condition any of the Purchaser Regulatory Approvals upon an increase in Purchaser's capital or compliance with any capital requirement, standard or ratio.

(d) The deposits of Purchaser and its Subsidiaries are insured by the FDIC to the fullest extent permitted by law, and all premiums and assessments required to be paid in connection therewith have been paid when due by Purchaser.

(e) Purchaser was rated at least satisfactory following its most recent CRA examination by the regulatory agency responsible for its supervision and has no reason to believe that it will not maintain at least a satisfactory rating following its next CRA examination. Purchaser has received no notice of and has no Knowledge of any planned or threatened objection by any community group to the transactions contemplated hereby.

Section 6.4 No Breaches; Defaults . Assuming the receipt of all regulatory approvals referenced in Section 6.3(a) , the execution and delivery of this Agreement and any instruments or other documents executed pursuant hereto by Purchaser do not and the consummation of the transactions contemplated by this Agreement, will not constitute: (i) a breach or violation of or default under any law, rule, regulation, judgment, order, governmental

permit or license of Purchaser or to which it is subject, which breach, violation or default would prevent or materially delay Purchaser from being able to perform its obligations under this Agreement in all material respects, or (ii) a breach or violation of or a default under the articles of association (or certificate of incorporation, as applicable) or bylaws of Purchaser.

Section 6.5 Litigation and Related Matters . There are no actions, suits, or proceedings, whether civil, criminal or administrative, pending or, to the Knowledge of Purchaser threatened against or affecting Purchaser which could materially impede, delay or prevent Purchaser or any of its Subsidiaries from entering into this Agreement or performing its terms.

Section 6.6 Compliance with Laws and Regulations . Except as set forth in Schedule 6.6, Purchaser and its Subsidiaries have conducted and are conducting their business in all material respects in compliance with all Applicable Law, including, without limitation, all regulations, orders, and opinions of [the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation and the New York Department of Financial Services], and, except as would not, individually or in the aggregate, result in a material adverse effect, none of Purchaser or its Subsidiaries is subject to any order or ruling directed to it by, or memorandum of understanding with, any Governmental Entity. Purchaser has received no notice of and has no Knowledge of any planned or threatened objection by any community group to the transactions contemplated hereby.

Section 6.7 No Brokers or Finders . Except for Keefe, Bruyette & Woods, Inc., whose fees will be paid by Purchaser, there is no investment banker, broker, finder or other intermediary that has been retained by or is authorized to act on behalf of Purchaser or any of its Affiliates who might be entitled to any fee or commission from Purchaser or any of its Affiliates in connection with the transactions contemplated hereby.

Section 6.8 Financing . On the Closing Date, Purchaser will have sufficient cash, available lines of credit or other sources of immediately available funds to enable it to make the Closing Payment and to promptly pay any other amounts to be paid by it under this Agreement on the Closing Date.

Section 6.9 Eligibility . As of the date hereof, Purchaser satisfies, and as of the Closing Date will satisfy, all clearing standards and requirements under Applicable Law to (1) acquire the Transferred Wealth Management Relationships and (2) employ the financial advisors associated with the Transferred Wealth Management Relationships.

## ARTICLE VII

## GENERAL COVENANTS

Section 7.1 Access to Properties and Records Relating to the Transferred Business . (a) To the extent permitted by Applicable Law, from the date hereof until the earlier of the Closing Date and the termination of this Agreement, Assignor will use commercially reasonable efforts to provide to Purchaser and to its officers, accountants, counsel, and other representatives reasonable access during the normal business hours of the HSBC Sellers to the

properties, books, contracts and records of the HSBC Sellers and their respective Subsidiaries relating primarily to the Transferred Business for purposes related to the consummation of the transactions contemplated by this Agreement, including for the purposes of conducting (x) a Phase I ESA and, if necessary to develop a Remediation Plan, a Phase II ESA, at the Purchased Real Property and (y) a Phase I ESA at all Business Premises subject to a Real Property Lease, subject to consent of the landlord under the applicable Real Property Lease; provided , however , that (x) such access shall be at reasonable times and upon reasonable prior notice and shall not disrupt the personnel and operations of the HSBC Sellers and their respective Subsidiaries; and (y) prior to conducting any proposed Phase II ESA, any work plans associated with such Phase II ESA shall be submitted to, and approved by, the HSBC Sellers (such approval not to be unreasonably withheld) and provided further that Purchaser's access to Tax Returns filed by or otherwise relating to the HSBC Sellers or any of their respective Subsidiaries; shall be governed by Article X . All requests for access to such offices, properties, books, and records shall be made to Assignor and Assignor will in turn either provide such access to Purchaser (if Assignor has copies of the applicable items) or make such requests to such representatives of the HSBC Sellers as the HSBC Sellers shall designate, who shall be responsible for coordinating such requests and all permitted access. Purchaser and Assignor shall promptly provide the HSBC Sellers with a copy of any report or other record relating to any ESA conducted at the Purchased Real Property or Business Premises subject to a Real Property Lease and with a copy of any Remediation Plan. Prior to conducting any Phase II ESA, Purchaser and Assignor shall provide the HSBC Sellers with a copy of the insurance certificate for any consultant that will conduct, in whole or in part, a Phase II ESA, which insurance certificate shall name the HSBC Sellers as additional insureds. Purchaser and Assignor shall indemnify the HSBC Sellers for any Losses arising from or relating to any ESA, to the extent such Losses are not recovered by the HSBC Sellers under such consultant's insurance policy.

(b) Following the Closing, to the extent permitted by Applicable Law, Purchaser will grant Assignor and any HSBC Seller and their respective representatives reasonable access during Purchaser's normal business hours to all books, records and other data related to the Transferred Business and to the Transferred Business Employees (including making such persons reasonably available to Assignor or any Affiliate or to an HSBC Seller or any Affiliate for depositions, witness preparation, trial preparation and fact-gathering, but excluding any proceedings, or threatened proceedings, between Assignor or an HSBC Seller, or an Affiliate of either of them, and Purchaser or an Affiliate of Purchaser) at reasonable times and upon reasonable prior notice and provided such access shall not disrupt the personnel and operations of Purchaser and its Subsidiaries, if such access is reasonably deemed necessary or desirable by Assignor or any HSBC Seller or any of its Subsidiaries in connection with its tax, regulatory, litigation, contractual or other legitimate, non-competitive matters, including for purposes of handling claims related to Section 2.2 for which Transferred Business Employees may have relevant information. Nothing in the foregoing shall prevent Assignor or any HSBC Seller or any of their respective Subsidiaries from seeking to make such persons available via subpoena or other legal or similar process.

(c) If the HSBC Sellers do not deliver books, records and other data pursuant to Section 2.1(b)(7) that are otherwise required to be delivered pursuant to Section 2.1(a)(11) , in accordance with Exhibit A , the Assignor will use commercially reasonable efforts to cause the HSBC Sellers to hold such books, records and other data as custodians for Purchaser and, in their capacity as custodians, to provide to Purchaser access to such books, records and other data in the manner provided in Exhibit A .

(b) Purchaser will review with Assignor and HSBC Purchaser's information security controls of the system or systems used by Purchaser to maintain the security of customer data, including providing reasonable access to Purchaser's owned facilities and data centers and, to the extent permitted under the relevant contract, to third-party facilities and data centers.

Section 7.2 Efforts; Regulatory Filings and Other Actions . (a) Each of the parties hereto agrees to use its reasonable best efforts to take, or cause to be taken, all actions and to do, or cause to be done, all things necessary, proper or advisable to consummate and make effective as promptly as practicable the transactions contemplated hereby and to cooperate with the other parties in connection with the foregoing. Without limiting the generality of the foregoing, each of the parties shall use its reasonable best efforts: (i) to obtain all Regulatory Approvals as promptly as practicable, (ii) to lift or rescind as promptly as practicable any injunction or restraining order or other order adversely affecting the ability of the parties hereto to consummate the transactions contemplated hereby, (iii) to effect all necessary registrations and filings, if any, and (iv) to fulfill all of the conditions to the obligations of the parties to consummate the transactions contemplated by this Agreement set forth in Article XI .

(b) In furtherance, and not in limitation, of the covenants set forth in Section 7.2(a) , each of the parties hereto agrees to use its reasonable best efforts to take, or cause to be taken, all actions and to do, or cause to be done, all things necessary, proper or advisable to obtain the Required Government Approvals as promptly as practicable, and within thirty (30) days after the date hereof, each party will file any application, notice or report required to be filed by such party with any Governmental Entity with respect to any Regulatory Approval or otherwise required in connection with the transactions contemplated hereby and will use its reasonable best efforts to obtain a waiver from any applicable waiting period, and will make any further filings pursuant thereto that may be necessary in connection therewith.

(c) Each party shall, subject to Applicable Law, (i) permit counsel for the other party, as well as counsel to HSBC, to review in advance, and consider in good faith the views of the other party in connection with, any proposed written communication to any Governmental Entity in connection with the transactions contemplated hereby, and (ii) provide counsel for the other party and counsel for HSBC with copies of all filings made by such party, and all material correspondence between such party (and its advisors) with any Governmental Entity and any other information supplied by such party and such party's Affiliates to a Governmental Entity or received from such a Governmental Entity in connection with the transactions contemplated hereby; provided , however , that materials may be redacted (x) to remove references concerning the valuation of the Transferred Business (or any aspect thereof), (y) as necessary to comply with contractual arrangements, and (z) as necessary to address reasonable privilege or confidentiality concerns (including with respect to the Retained Businesses). Each party agrees that it will use reasonable best efforts to keep the other party and HSBC fully informed with respect to all applications and developments related thereto and, where reasonably practicable under the circumstances, give the other party reasonable advance notice of, and whenever appropriate, invite the other party and HSBC (and give due consideration in good faith to any reasonable request of the other party) to participate in, any

meetings or discussions held with any Governmental Entity; provided that such participation is not objected to by such Governmental Entity. The parties further covenant and agree to mutually identify the most expedient method of effecting, as promptly as practicable, the legal transfer of all of the Purchased Assets and the Assumed Liabilities to Purchaser, and each party further covenants and agrees to use its reasonable best efforts to so effectuate such transfer. The parties further covenant and agree not to extend any waiting period associated with any Regulatory Approval or enter into any agreement with any Governmental Entity not to consummate the transactions contemplated by this Agreement, except with the prior written consent of the other party hereto and HSBC.

(d) The parties further covenant and agree that (i) with respect to any threatened or pending preliminary or permanent injunction or other order, decree or ruling or statute, rule, regulation or executive order that would adversely affect the ability of the parties hereto to consummate the transactions contemplated hereby, to use their respective best efforts to prevent the entry, enactment or promulgation thereof, as the case may be, and (ii) in the event that any action, suit, proceeding or investigation is commenced after the date hereof challenging any of the parties' rights to consummate the transactions contemplated by this Agreement, the parties shall use their best efforts, and take all actions necessary and appropriate, to contest such action, suit, proceeding or investigation.

(e) Promptly upon the execution of this Agreement and subject to Applicable Law, Purchaser and Assignor will reasonably coordinate in good faith with each other and HSBC in respect of any communications with parties whose consent is required. Assignor and Purchaser, in consultation with each other and HSBC, shall as promptly as practicable following the date hereof develop a communications and action plan (which plan shall be designed to communicate promptly and follow up with all such parties with respect to, and to obtain, all such required consents), and shall keep each other and HSBC reasonably informed regarding the progress and status of such efforts.

(f) Each party represents, warrants and agrees that any information furnished by it for inclusion in any regulatory application will to its Knowledge be true and complete in all material respects as of the date so furnished.

Section 7.3 Further Assurances . The parties agree that, from time to time, whether before, on or after the Closing Date, each of them will execute and deliver such further instruments of assignment and directions for conveyance and transfer and take such other action as may be reasonably necessary to carry out the purposes and intents of this Agreement.

Section 7.4 Notice of Changes . (a) Purchaser shall promptly advise Assignor and HSBC, and Assignor shall promptly advise Purchaser and HSBC of (i) any change or event that would or would be reasonably likely to cause or constitute a material breach of any of Purchaser's or Assignor's, as applicable, representations, warranties or covenants contained herein, or (ii) to the extent permitted by Applicable Law and to the Knowledge of Purchaser or Assignor, as applicable, any governmental complaints, any change or event, including investigations or hearings (or communications indicating that the same may be contemplated) or the institution or the threat of significant litigation, that would reasonably be expected to prevent or materially delay the consummation of the transactions contemplated hereby.

(b) Notwithstanding anything to the contrary herein, a party's good-faith failure to comply with its obligations under this Section 7.4 shall not provide the other party hereto or any of such other party's Affiliates with a right not to effect the transactions contemplated by this Agreement, except, in each case, to the extent that the underlying material breach of a representation, warranty or covenant would independently provide such right.

Section 7.5 Confidentiality . Each party to this Agreement shall hold, and shall cause its respective directors, officers, employees, agents, consultants and advisors to hold, in strict confidence, except to the extent necessary to discharge obligations pursuant to Section 7.2 or unless compelled to disclose by judicial or administrative process or, based on the advice of its counsel, by other requirements of Applicable Law or the applicable requirements of any regulatory agency or relevant stock exchange, all non-public records, books, contracts, instruments, computer data and other data and information (collectively, " Information ") concerning the other party or concerning HSBC (or, if required under a contract with a third party, such third party) furnished to it by such other party or by HSBC or its representatives pursuant to the Confidentiality Agreement or otherwise in connection with the transactions contemplated by this Agreement (except to the extent that such information can be shown to have been (i) previously known by such party on a non-confidential basis, (ii) in the public domain through no fault of such party or (iii) later lawfully acquired from other sources by the party to which it was furnished), and neither Assignor nor Purchaser shall release or disclose such Information to any other person (other than HSBC), except its auditors, attorneys, financial advisors, bankers, other consultants and advisors with a duty of confidentiality and, to the extent permitted above, any Governmental Entity. To the extent permitted by Applicable Law, each party will notify the other party and HSBC promptly upon becoming aware that any of the Confidential Information has been disclosed to or obtained by a third party (otherwise than as permitted by this Section 7.5 ). The Confidentiality Agreement as between Assignor and Purchaser is hereby terminated, it being understood , that the Confidentiality Agreement shall continue in full force and effect as between Purchaser and HSBC.

Section 7.6 Publicity; Notices . Until the Closing Date, the parties hereto shall coordinate with each other and with HSBC as soon as practicable in advance as to (i) the form and content of any external communication, including any communication intended for dissemination or to reach, or reasonably expected to be disseminated or to reach, members of the public or Banking Center Customers regarding the transactions contemplated by this Agreement and (ii) the form and content of any communication from Purchaser to the Business Employees or Affiliated Employees. Neither party shall disseminate any such communication without adequate advance notice and the prior review of the other party and of HSBC, which review shall not be unreasonably delayed, except that nothing contained in this Agreement shall prevent the parties hereto from publishing any press release or from making any and all public disclosures which it reasonably determines to be legally required to comply with any applicable securities laws or regulations or requests of governmental agencies or authorities; provided that, to the extent possible under the circumstances, the party making such disclosure consults with the other party and with HSBC, and considers in good faith the views of the other party and of HSBC, before doing so.

Section 7.7 Restricted Assignments . Notwithstanding anything in this Agreement to the contrary, this Agreement shall not constitute an agreement to assign any Purchased Asset, Assumed Agreement, Assumed Deposits or other Assumed Liability, or any claim or right or any benefit arising thereunder or resulting therefrom if an attempted assignment thereof, without the consent of a third party thereto, would constitute a breach thereof or in any way affect the rights of an HSBC Seller or its Subsidiaries thereunder or be contrary to Applicable Law. If any such consent or approval is not obtained, Assignor will use commercially reasonable efforts to cause the HSBC Seller to use its reasonable best efforts (which shall not require Assignor or such HSBC Seller to pay any money or other consideration to any Person or to initiate any claim or proceeding against any Person) to secure an arrangement reasonably satisfactory to Purchaser ensuring that Purchaser will receive the benefits under the agreement for which such consent is being sought following the Closing; provided , however , that Assignor shall have no obligation to obtain or to cause the HSBC Seller to obtain such consent or approval or to provide or cause an HSBC Seller to provide such an alternative arrangement other than the undertaking to use reasonable best efforts to obtain or provide the same as set forth in this Section 7.7 and Purchaser shall remain obligated to close the transactions contemplated herein, subject to the other provisions hereof, and, shall have no remedy for failure of Assignor or the HSBC Seller to obtain any such consent or approval or to provide any such alternative arrangement.

Section 7.8 Transition Coordinators; Cooperation with Transition . Subject to Applicable Law, from the date hereof until the earlier of the Closing Date and the termination of this Agreement, Assignor will cooperate with Purchaser and use commercially reasonable efforts to cause the HSBC Sellers to cooperate with Purchaser to provide current information regarding material activities of the Transferred Business, and Purchaser and Assignor shall cooperate with and assist each other and HSBC in planning and implementing necessary and appropriate policies and procedures in connection with the transition of the ownership of the Transferred Business from the HSBC Sellers to Purchaser. In connection therewith, Assignor and Purchaser shall each as promptly as practicable after the execution of this Agreement designate certain of their respective employees as “transition coordinators.”

Section 7.9 Non-Competition and Non-Solicitation . (a) Except as set forth in Schedule 7.9(a), Assignor will not agree to an amendment to or waiver of Section 7.9(a) of the Primary Purchase Agreement with respect to any of the following counties in New York State without the written consent of Purchaser insofar as any such amendment or waiver would adversely affect the Transferred Business: Cayuga, Chemung, Tioga, Tomkins, Schuyler, Steuben, Seneca, Ontario, Yates, Livingston, Wyoming, Genesee, Orleans, and Monroe.

(b) From the date hereof until the Closing Date, Purchaser and its Affiliates shall not, directly or indirectly, solicit for employment (other than as expressly permitted by this Agreement) or hire (i) any Business Employees and Wealth Management Employees who are not hourly wage (non-exempt) employees, (ii) any employees of the HSBC Sellers or their Affiliates who are or will be engaged in the preparation for or implementation of any Conversion or the transfer of any of the Transferred Business, Purchased Assets or Assumed Liabilities, or who are or will be otherwise involved in providing services under the Transition Services Agreement (iii) any employees of HSBC Mortgage Corp. who are not otherwise identified on Schedule 7.9(b) and (iv) employees of HSBC Sellers or their Affiliates as of the date hereof who become or who are expected to become employees of Assignor before the Closing Date. For purposes of monitoring Section 7.9(b)(i) and (ii) , all individuals described in (i) and (ii) are identified on a Schedule 7.9(b) previously delivered to Assignor thirty (30) calendar days following the execution of the Primary Purchase Agreement and which may be updated from time to time by HSBC Sellers.

(c) During the period beginning on the Closing Date and ending on the first (1st) anniversary of the Closing Date:

(1) Purchaser and its Affiliates shall not, directly or indirectly, solicit for employment or hire any Retained Employee or any employees of Assignor; provided that this Section 7.9(c)(1) shall not prohibit Purchaser or any of its Affiliates from (i) engaging in solicitation by means of a general purpose advertisement not specifically targeted at the Retained Employees or employees of Assignor or hiring any Retained Employee or employee of Assignor as a result of such general purpose advertisement or (ii) hiring any Retained Employee or employees of Assignor who was terminated by any HSBC Seller or Assignor, as applicable, after the Closing Date; and

(2) Assignor shall not, directly or indirectly, solicit for employment or hire any Transferred Business Employee or employee of Purchaser; provided that this Section 7.9(c)(2) shall not prohibit Assignor from (i) engaging in solicitation by means of a general purpose advertisement not specifically targeted at the Transferred Business Employees or employees of Purchaser or hiring any Transferred Business Employee or employee of Purchaser as a result of such general purpose advertisement or (ii) hiring any Transferred Business Employee or employee of Purchaser who was terminated by Purchaser or any of its Affiliates after the Closing Date.

(d) During the period beginning on the date hereof and ending on the first (1st) anniversary of the Closing Date, Purchaser and its Affiliates shall not, directly or indirectly, (i) use any information regarding the Retained Businesses in their possession as a result of the transactions contemplated by this Agreement, including as part of the books and records that are Purchased Assets, to solicit or engage in other efforts directed to or targeted at any customer or customers of the Retained Businesses or the Non-Assigned Transferred Business with respect to providing Banking Related Services similar to those of the Retained Businesses or the Non-Assigned Transferred Business or (ii) use such information to take any other actions that are designed to induce any customer of the Retained Businesses or the Non-Assigned Transferred Business to transfer any portion of such customer's Relationships with HSBC or Assignor, as applicable, with respect to the Retained Businesses or the Non-Assigned Transferred Business, as applicable, to a similar business of Purchaser or its Affiliates; provided that nothing in this Section 7.9(d) shall be construed as limiting the ability of Purchaser to (x) respond to unsolicited requests by customers of the Retained Businesses or the Non-Assigned Transferred Business; (y) service customers of the Retained Businesses or the Non-Assigned Transferred Business who also, as of the date hereof, are customers of Purchaser or its Affiliates; or (z) offer or continue to offer Banking Related Services that are similar to the Retained Businesses or the Non-Assigned Transferred Business.

(b) Each of Purchaser and Assignor understands and acknowledges that (i) it would be difficult to calculate damages to the applicable party and to HSBC from any breach of the obligations of the other party under this Section 7.9 , (ii) injury to Purchaser, Assignor or the

HSBC Sellers, as applicable, from any such breach would be irreparable and impossible to measure and (iii) the remedy at law for any breach or threatened breach of this Section 7.9 would therefore be an inadequate remedy and, accordingly, Purchaser and Assignor (and HSBC as a third party beneficiary) shall, in addition to all other available remedies (including, without limitation, seeking such damages as either can show it has sustained by reason of such breach and/or the exercise of all other rights either has under this Agreement), be entitled to seek injunctive relief, specific performance and other equitable remedies without the necessity of showing actual damages or posting bond.

(c) Purchaser and Assignor understand and acknowledge that the restrictive covenants and other agreements contained in this Section 7.9 are an essential part of this Agreement and the transactions contemplated hereby and thereby. It is the intention of the parties that, if any of the restrictions or covenants contained herein are held to cover a geographic area or to be for a length of time that is not permitted by Applicable Law, or is in way construed to be too broad or to any extent invalid, such provision shall not be construed to be null, void and of no effect, but to the extent that such provision would then be valid or enforceable under Applicable Law, such provision shall be construed and interpreted or reformed to provide for a restriction or covenant having the maximum enforceable geographic area, time period and other provisions as shall be valid and enforceable under Applicable Law.

(d) For the avoidance of doubt, none of the restrictions imposed by applicable subsections of this Section 7.9 shall apply to any Person that is an Affiliate of a party to this Agreement if such Person ceases to be an Affiliate of such party.

(e) Purchaser shall take any commercially reasonable actions to cooperate and facilitate Assignor's ability to retain and/or continue to service Banking Center Customers with regard to the Credit Card Accounts and Receivables including Card Rewards and Enhancements.

Section 7.10 Distribution Agreements . Purchaser agrees to enter into (i) one or more distribution agreements with HSBC and/or its applicable Affiliates, on terms mutually agreeable to them, to allow the continued distribution by Purchaser and its Affiliates and the continued servicing by HSBC and its Affiliates of asset management and other investment products of HSBC and its Affiliates currently held by wealth management customers of the Transferred Business and (ii) such distribution or servicing arrangements, on terms mutually agreeable to them, as would allow for the portability of third-party asset management, annuity and other investment products currently held by wealth management customers of the Transferred Business.

Section 7.11 Arrangements with Respect to Employee Pension Plans, IRAs and Keogh Plans . On or before the Closing Date, Assignor will cause HSBC to cause notice to be sent to each depositor of an Assumed Deposit held by HSBC or any of its Subsidiaries in an IRA and each "employer" who established an Assumed Deposit pursuant to a Keogh plan and each depositor that is an Employee Pension Plan, regarding the resignation of HSBC as IRA custodian or Keogh plan or Employee Pension Plan trustee, as applicable (as provided for in Section 7.12 of the Primary Purchase Agreement). Such resignation shall be effective as of the date that is thirty (30) days following the date of the notice or, if later, the Closing Date. If a depositor of an

Assumed Deposit held by HSBC in an IRA or an employer who established an Assumed Deposit pursuant to a Keogh plan, Employee Pension Plan or other retirement plan fails to appoint another trustee or custodian for such account within this period, such depositor or employer will, to the extent permitted by Applicable Law, be deemed to have appointed Purchaser as successor trustee or custodian for the deposit account. Upon its appointment as successor trustee or custodian for such accounts, as applicable, Purchaser shall perform the services and carry out the duties and obligations required of it under the applicable plans, the Code and Applicable Law. If, notwithstanding the foregoing, as of the Closing Date, Purchaser shall be unable to retain deposit liabilities in respect of an Employee Pension Plan, IRA, Keogh Plan or other retirement plan, such deposit liabilities shall be considered "Excluded Deposits."

Section 7.12 Updated Schedules . (a) On the fifth (5th) day prior to the Closing Date anticipated by the parties, Assignor will or will cause HSBC to deliver to Purchaser updated versions of the following schedules so that they are as of a date no earlier than last day of the month preceding the Closing Date (such date, the " Update Date "): Schedule 1.1(a) (Assumed Deposits), Schedule 1.1(c)(i) (Business Employees), Schedule 1.1(c)(ii) (Affiliated Employees), Schedule 1.1(h) (Purchased Overdrafts), Schedule 1.1(l) (Transferred Business Banking Relationships), Schedule 1.1(m) (Transferred Wealth Management Relationships), Schedule 2.1(a)(1) (Purchased Real Property), Schedule 2.1 (a)(2) (Real Property Leases), Schedule 2.1(a)(5)(i) (Purchased ATMs), Schedule 2.1(a)(5)(ii) (ATM Real Property Leases), Schedule 2.1(a)(6) (Purchased Loans), Schedule 2.1(a)(8) (CRA Assets), Schedule 2.1(a)(9) (Assumed Letters of Credit). Purchaser acknowledges that the updated versions of the foregoing Schedules shall be prepared using the same methodology and criteria used in preparing the Schedules attached to this Agreement, subject to changes resulting from updates to the household allocations of customers to branches by HSBC consistent with the "householding" methodology and change in the householding made by HSBC Sellers in the Department of Justice divestiture Banking Centers in Buffalo.

(b) In connection with delivery of the Final Closing Statement Assignor shall deliver to Purchaser updated versions of the following schedules, so that they are as of the Closing Date (such schedules, collectively, the " Final Schedules "): Schedule 1.1(a) (Assumed Deposits), Schedule 1.1(c)(i) (Business Employees), Schedule 1.1(c)(ii) (Affiliated Employees), Schedule 1.1(h) (Purchased Overdrafts), Schedule 1.1(l) (Transferred Business Banking Relationships), Schedule 1.1(m) (Transferred Wealth Management Relationships), Schedule 2.1(a)(1) (Purchased Real Property), Schedule 2.1(a)(2) (Real Property Leases), Schedule 2.1(a)(5)(i) (Purchased ATMs), Schedule 2.1(a)(5)(ii) (ATM Real Property Leases), Schedule 2.1(a)(6) (Purchased Loans), Schedule 2.1(a)(8) (CRA Assets), Schedule 2.1(a)(9) (Assumed Letters of Credit). Purchaser acknowledges that the updated versions of the foregoing Schedules shall be prepared using the same methodology and criteria used in preparing the Schedules attached to this Agreement, subject to changes resulting from updates to the household allocations of customers to branches by HSBC consistent with the "householding" methodology and change in the householding made by HSBC Sellers in the Department of Justice divestiture Banking Centers in Buffalo.

## ARTICLE VIII

## FURTHER AGREEMENTS

Section 8.1 Conduct of the Transferred Business Prior to the Closing . (a) From the date hereof until the earlier of the Closing Date and the termination of this Agreement, Assignor will use commercially reasonable efforts to cause the HSBC Sellers, consistent with the other provisions of this Agreement: (i) to use reasonable best efforts to, and cause their applicable Subsidiaries to use their respective reasonable best efforts to, conduct the Transferred Business in the ordinary course consistent with past practice and maintain, generally, their existing relations and goodwill with Banking Center Customers and vendors and suppliers to the Transferred Business; (ii) to use their ordinary course efforts to, and cause their applicable Subsidiaries to use their respective ordinary course efforts to, consistent with historical and customary past practices, preserve in all material respects, and with respect to the Banking Centers, the mix, type and aggregate amount of the Purchased Assets and Assumed Liabilities, including the Assumed Deposits, provided that the agreements in this Section 8.1 and the agreement of the HSBC Sellers in Section 8.1 of the Primary Purchase Agreement shall not be construed as any promise, representation or guarantee by Assignor or the HSBC Sellers that such mix, type and amount will in fact be maintained and may in fact be materially different as of the Closing Date, and the occurrence of such event shall not, in and of itself, be considered a breach of the obligations of Assignor or the HSBC Sellers' obligations under this Section 8.1(a) or Section 8.1 of the Primary Purchase Agreement; and (iii) to continue to maintain the Banking Centers in accordance with its national pricing strategy, except that HSBC may in its sole discretion adjust its rates and pricing to respond to actions taken in the market by Assignor.

(b) From the date hereof until the earlier of the Closing Date and the termination of this Agreement, Assignor will not agree to an amendment to Section 8.1(b) of the Primary Purchase Agreement that would materially adversely affect the Transferred Business, Purchased Assets or Assumed Liabilities, taken as a whole.

Section 8.2 Real Property Leases and ATM Leases . (a) Assignor will use commercially reasonable efforts to cause HSBC to use its reasonable best efforts (which shall not require Assignor or HSBC to pay any money or other consideration to any Person or to initiate any claim or proceeding against any Person) to cause every landlord of a Real Property Lease or ATM Real Property Lease, the consent of which is required under the terms of the applicable Real Property Lease or ATM Real Property Lease to the assignment of such Real Property Lease or ATM Real Property Lease to Purchaser, to execute in favor of Purchaser a Landlord Consent.

(b) If, despite the efforts contemplated by Section 8.2(a), a Landlord Consent to assignment of a Real Property Lease or ATM Real Property Lease cannot be obtained, or cannot be obtained without the payment of an assignment fee or similar lump sum or rent increase, Assignor shall cause HSBC, if permitted without the consent of the landlord under the Real Property Lease or ATM Real Property Lease, to sublease the Business Premises or ATM location to Purchaser pursuant to a sublease agreement which shall be, to the extent permitted, for the remainder of the existing term of the Real Property Lease or ATM Real Property Lease, as applicable, and which shall provide for Purchaser to perform all of the obligations of HSBC under such Real Property Lease or ATM Real Property Lease and which otherwise shall contain mutually agreeable terms (a " Sublease Agreement ").

(c) Purchaser shall use its reasonable best efforts to cooperate with HSBC's attempts to obtain each Landlord Consent or its approval of a Sublease Agreement, but shall not be obligated to pay any consideration or grant any concession in connection therewith.

(d) Notwithstanding anything to the contrary contained in this Agreement, if HSBC is unable to obtain for Purchaser the right to occupy a Business Premise, whether pursuant to a Landlord Consent or a Sublease Agreement or otherwise, Purchaser shall not be entitled to terminate this Agreement and Purchaser shall remain obligated to perform all of its obligations hereunder, including, without limitation, the assumption of the Assumed Deposits without any reduction or adjustment to the consideration to be paid by Purchaser as provided in this Agreement.

Section 8.3 UCC-1 Assignment and Other Documents . (a) Assignor will use commercially reasonable efforts to cause HSBC to use its reasonable best efforts to deliver to Purchaser at the Closing all signed UCC-1 financing statements and UCC-3 assignments of financing statements, endorsed notes, participations, assignments of mortgages in recordable form and all other documentation necessary to effect the assignment of the Purchased Loans (including all related collateral) and the Assumed Letters of Credit to Purchaser. The out-of-pocket costs and expenses of preparing and filing any such documentation that are allocated to Assignor under Section 8.3 of the Primary Purchase Agreement shall be split equally between Assignor and Purchaser.

(b) Purchaser acknowledges HSBC's agreement in Section 8.3(b) of the Primary Purchase Agreement.

Section 8.4 Letters of Credit . In the event that any Assumed Letter of Credit cannot be assigned to Purchaser, on the Closing Date, Purchaser agrees to enter into a participation agreement with HSBC in customary form reasonably satisfactory to Purchaser and HSBC pursuant to which Purchaser shall acquire and assume all of HSBC's rights and obligations under such Assumed Letters of Credit and become entitled to all reimbursements thereunder.

Section 8.5 Form of Transfer . Assignor and Purchaser may by mutual written agreement at any time, with the consent of HSBC, change the method of transferring the Transferred Business from HSBC to Purchaser in order to achieve, in a more efficient manner, the business, financial accounting, regulatory and tax objectives of Assignor and Purchaser in connection with the transactions contemplated by this Agreement; provided , however , no such change shall alter or change the amount of consideration to be paid by Purchaser as provided in this Agreement.

Section 8.6 Conversion Plan, Data Processing and Related Matters

(a) The parties hereto agree to cooperate with each other and with HSBC to employ their reasonable best efforts to plan, execute and complete the Conversion in an orderly and efficient manner pursuant to the Conversion Plan. As promptly as practicable after the date

hereof, Purchaser and Assignor shall each appoint qualified staff members to act as project managers for the Conversion (each, a " Conversion Project Manager "). Such Conversion Project Managers shall act as the principal contacts between the parties and with HSBC representatives on matters relating to the Conversion, and shall coordinate the assignment of personnel as required and generally facilitate the planning, execution and completion of the Conversion pursuant to the Conversion Plan. In addition to any conversion of the data and systems files as part of the Conversion pursuant to the Conversion Plan, the parties shall reasonably cooperate with each other and with HSBC in performing such tasks as may be outlined in the Conversion Plan (as defined below), including the collection and input of relevant data, development of new operating procedures and design of forms, in each case, as mutually agreed by the parties.

(b) Purchaser and Assignor shall each bear all out-of-pocket costs and expenses associated with their respective area of responsibility as defined in the Conversion Plan, including costs and expenses incurred in converting, moving, storing, archiving, adapting or otherwise transferring or facilitating the transfer of any data, information, securities, records, files and systems from the systems and facilities of the HSBC Sellers and their respective Affiliates to the systems and facilities of Purchaser and its Affiliates (including costs with respect to computer programs, data processing, deconversion, data extraction, third-party charges and filing fees) provided, however, that, notwithstanding anything to the contrary in this Section 8.6 or otherwise in this Agreement, Purchaser shall not be liable hereunder for any termination fees, penalties or other break costs incurred by the HSBC Sellers or any of their respective Subsidiaries as a result of the Conversion. Purchaser and Assignor each agrees to promptly reimburse the other in accordance with the Conversion Plan. The agreement of the parties in this Section 8.6(b) does not alter the agreement of Assignor in Section 8.6(b) of the Primary Purchase Agreement.

(c) In connection with the conversion activities described in subsections (a) and (b) immediately above, and subject to Applicable Law and Exhibit A , it is further agreed that:

(1) Purchaser will review, subject to Section 7.1, current operations of the Transferred Business and Purchaser and Assignor shall cooperate with each other and with HSBC and use their reasonable best efforts to develop a mutually agreeable written plan within forty-five (45) days of the date hereof (as it may be amended from time to time, the " Conversion Plan "), which Conversion Plan shall (i) set forth the plan, procedures, scheduling methodology, resources and expenditures required to fully effect the Conversion by the end of the weekend immediately after the Closing Date (or such other date as may be agreed by the parties), (ii) include interim target dates for the completion of integral items to the Conversion; (iii) provide that conversion items integral to the operation of the Transferred Business shall have the earliest target completion dates in the Conversion Plan and (iv) specify the appropriate procedures to allocate the Primary Purchased Assets and Primary Assumed Liabilities between Purchaser and Assignor;

(2) as of the Closing Date, Assignor will use commercially reasonable efforts to cause the HSBC Sellers to provide Purchaser with existing customer, account and transaction data feeds related to the Transferred Business in order to allow Purchaser to comply with applicable legal and contractual anti-money laundering and privacy requirements on and after the Closing Date; and

(3) Assignor will use commercially reasonable efforts to cause the HSBC Sellers to cooperate in good faith with Purchaser to take all reasonably necessary actions to facilitate the orderly transfer of the Transferred Wealth Management Relationships to Purchaser on the Closing Date.

(d) The parties agree to cooperate with each other and with HSBC to schedule arrangements for change in displays and advertisements at the Banking Centers such that on the next Business Day following the Closing Date, no Signage shall be displayed at the Banking Centers, either internally or externally. To the extent that any Signage shall remain at a Banking Center, Purchaser shall use its reasonable best efforts to remove such Signage prior to the next Business Day following the Closing Date and to retain such Signage for later collection by the HSBC Sellers.

(e) The parties agree to address certain transitional matters addressed in Exhibit A in accordance with the provisions of Exhibit A and to coordinate with HSBC with respect to those matters.

Section 8.7 HSBC Intellectual Property . (a) Except as specifically provided in this Section 8.7 , Purchaser acknowledges and agrees that none of Purchaser or its Affiliates is purchasing, acquiring, receiving a license to or otherwise obtaining any right, title or interest in, to or under any Intellectual Property owned or licensed by the HSBC Sellers or any of their respective Affiliates, including the HSBC Entity Names.

(b) Except as provided in this Section 8.7 , as of and following the Closing, Purchaser shall, and shall cause its Affiliates to, cease and discontinue promptly after the Closing any and all uses of any and all Intellectual Property owned or licensed by the HSBC Sellers or any of their respective Affiliates, including any HSBC Entity Names. Except as provided in this Section 8.7 , Purchaser agrees that, as of and following the Closing, none of Purchaser nor any of its Affiliates shall have any right, title or interest in, or any authority or license to use or allow others to use in any manner whatsoever, any Intellectual Property owned or licensed by the HSBC Sellers or their respective Affiliates, and any such right, title, interest, authority, license or sublicense or other arrangement relating thereto (whether written or oral) existing prior to the Closing, shall automatically terminate simultaneously with and effective as of the Closing. Notwithstanding the foregoing and only to the extent that use of labeling, stationery, business forms, supplies, ATM cards, debit cards, gift cards, checks, deposit slips and envelopes (but excluding any advertising, marketing or other promotional materials) existing on the Business Premises, in the inventory of Purchaser or any of its Affiliates or in the possession of a Banking Center Customer, in each case, that bear an HSBC Entity Name as of the Closing (the " Business Material ") cannot be commercially reasonably avoided after the Closing by Purchaser and its Affiliates, Purchaser and such Affiliates shall have, subject to the execution by Purchaser and such Affiliates of the License Agreement, a limited, non-transferable, non-sublicensable, royalty-free, non-exclusive right to use and deplete the Business Materials for a thirty- (30) day period following the Closing Date (such right, the " HSBC Seller Name License " and such period, the " Transitional Period "); provided , however , that (i) none of Purchaser or any of its Affiliates shall

take any action that could reasonably be expected to impair the value of or goodwill associated with the HSBC Entity Names, (ii) Purchaser and its Affiliates shall use the Business Materials and make any use of the HSBC Entity Names pursuant to this Section 8.7 in substantially the same forms, and for substantially the same purposes, as an HSBC Seller is using such HSBC Entity Names in connection with the operation and conduct of the Transferred Business immediately prior to the Closing, but not including any advertising, marketing or other promotional activities and (iii) Purchaser and its Affiliates shall use their reasonable best efforts to minimize their respective use of the HSBC Entity Names and shall cease using the HSBC Entity Names on such Business Materials as set forth in the License Agreement and in any event within the Transitional Period. For clarity, the foregoing activities during the Transitional Period will be for wind-down purposes only, and none of Purchaser or any of its Affiliates shall actively use the HSBC Entity Names in any advertising, marketing or other promotional activities during the Transitional Period.

(c) Purchaser, for itself and its Affiliates, acknowledges and agrees that, (i) as between the parties hereto, the HSBC Sellers and their respective Affiliates own or have the exclusive right to use any and all of the HSBC Entity Names and, except as otherwise expressly provided in this Section 8.7 , none of Purchaser or any of its Affiliates shall, as of the Closing, have any rights in or to the HSBC Entity Names, (ii) none of Purchaser or any of its Affiliates shall contest the ownership or validity of any rights of the HSBC Sellers or any of their respective Affiliates in or to the HSBC Entity Names, and (iii) none of Purchaser or any of its Affiliates shall adopt, use, register or attempt to register any of the HSBC Entity Names or instruct others to do so. Purchaser, for itself and its Affiliates, agrees and shall ensure that any use of the HSBC Entity Names as permitted in this Section 8.7 shall be only with respect to goods and services of a level of quality equal to or greater than the quality of goods and services with respect to which the HSBC Sellers and their respective Affiliates used such HSBC Entity Names prior to the Closing. Purchaser, for itself and its Affiliates, agrees that, after the Closing, none of Purchaser or any of its Affiliates, will expressly, or willingly by implication, do business as or represent themselves as any HSBC Seller or any Affiliate of the HSBC Sellers and the personnel of Purchaser or any of its Affiliates shall not, and shall have no authority to, as of the Closing, hold themselves out as officers, employees or agents of the HSBC Sellers or any of their respective Affiliates.

(d) Purchaser, on behalf of itself and its Affiliates, agrees that Purchaser and its Affiliates shall indemnify and hold harmless Assignor and the HSBC Sellers and their respective Affiliates from and against all Damages that arise out of, relate to or result from use of the HSBC Entity Names by Purchaser during the Transitional Period.

Section 8.8 Wrong Pocket Assets . Unless otherwise specifically provided in Exhibit A , if at any time or from time to time after the Closing Date, Assignor, on the one hand, or Purchaser, on the other, shall receive or otherwise possess any asset (including cash) that should belong to another Person pursuant to this Agreement, Assignor or Purchaser agrees to promptly transfer, or cause to be transferred, such asset to the Person so entitled thereto.

Section 8.9 Environmental Matters. In the event that within forty-five days (45) after the date of this Agreement Purchaser delivers to Assignor a written notice that identifies environmental matters or conditions at the Purchased Real Property that Purchaser believes constitute actual or potential violations of, or Liabilities under, Environmental Laws (" Environmental Conditions "), then, prior to the Closing, Purchaser and Assignor, together with their respective consultants and counsel, shall cooperate in good faith to jointly develop a plan to eliminate or remediate such Environmental Conditions after the Closing (a " Remediation Plan "); provided , however , that (i) the Remediation Plan shall provide that Purchaser shall have the sole right to direct and control all such elimination or remediation activities, which, for clarity, shall not commence until after the Closing Date, through contractors and consultants selected by Purchaser in its sole discretion and (ii) if Purchaser and Assignor are unable to agree on a Remediation Plan prior to the Closing, then Purchaser shall have the sole right to develop the Remediation Plan. Each of Purchaser and Assignor shall be solely responsible for its own costs and the costs of its consultants and counsel in connection with the activities undertaken pursuant to this Section 8.9 , provided that Qualifying Remediation Costs shall be allocated between Purchaser and Assignor as provided below. A cost will constitute a " Qualifying Remediation Cost " only if the cost would reasonably be incurred, in accordance with the Remediation Plan, to investigate or remediate an Environmental Condition or to restore the Purchased Real Property following such remediation. Each of Purchaser and Assignor agrees to fund fifty percent (50%) of the first $200,000 of Qualifying Remediation Costs. In the event that Qualifying Remediation Costs exceed $200,000 and are less than $500,000, then Assignor shall fund seventy five percent (75%) of such Qualifying Remediation Costs and Purchaser shall fund twenty five percent (25%) of such Qualifying Remediation Costs (i.e., the costs in excess of $200,000 and less than $500,000). In the event that Qualifying Remediation Costs exceed $500,000, then Assignor shall fund ninety percent (90%) of such excess Qualifying Remediation Costs and Purchaser shall fund ten percent (10%) of such excess Qualifying Remediation Costs (i.e., the costs in excess of $500,000). In no event shall Assignor be required to pay for Qualifying Remediation Costs in respect of the Purchased Real Property in an aggregate amount that exceeds $1,000,000.

## ARTICLE IX

## EMPLOYMENT AND BENEFIT MATTERS

Section 9.1 Transferred Business Employees . (a) *Offers of Employment* . Subject to Applicable Law, at least thirty (30) days (unless an earlier date is required by Applicable Law) prior to the Closing Date and effective as of the Closing Date, (i) Purchaser shall make, and shall use reasonable best efforts to cause to be accepted, a Comparable Job Offer to all Business Employees and Wealth Management Employees (excluding Retained Employees) and (ii) Purchaser shall make, and shall use reasonable best efforts to cause to be accepted, a Comparable Job Offer to all such Affiliated Employees (other than the Wealth Management Employees) whom Purchaser reasonably determines, in good faith, are likely to meet Purchaser's reasonable employment qualifications in respect of Purchaser's business needs following the Closing Date both in terms of the transactions contemplated by this Agreement and Purchaser's internal business needs outside the context of such transactions; provided , however , that the Purchaser shall provide to Assignor, who shall provide to HSBC, within thirty (30) days following the date of this Agreement, a list of such Affiliated Employees to whom Purchaser shall make a Comparable Job Offer. Purchaser's employment of the Transferred Business Employees shall be deemed to commence at 11:59 p.m. on the Closing Date, without regard to whether the Transferred Business Employee is actively at work on the Closing Date in the case of an employee who on the Closing Date is absent from work due to a vacation, jury duty, funeral leave or personal day. Notwithstanding the foregoing, to the extent that a Business

Employee or an Affiliated Employee who has accepted Purchaser's offer is not available to perform services on the Closing Date because on the Closing Date such employee is on sick leave, short-term disability, workers compensation leave, military leave, leave of absence under the Family Medical Leave Act or other leave of absence approved by an HSBC Seller or one of its Affiliates (other than a vacation, jury duty, funeral leave or personal day), he or she shall remain an employee of the HSBC Sellers or one of their respective Affiliates (except as otherwise required by Applicable Law); provided that Purchaser shall hire such Business Employee or Affiliated Employee, if such Business Employee of Affiliated Employee returns to work no later than the date that is the earlier of the scheduled return date (including any approved extensions thereto) and six (6) months from the date of commencement of such leave, unless such Employee is entitled to reemployment under the Uniformed Services Employment and Reemployment Act, in which case Purchaser shall not be obligated hire such Employee unless the return date is no later than twelve (12) months following the Closing Date, and, for purposes of this Agreement, such Employee shall become a Transferred Business Employee as of the date active employment with Purchaser commences and, to the extent applicable, references in this Section 9.1 to the "Closing Date" shall relate to the date on which active employment commences. Those Business Employees and Affiliated Employees who do not accept Comparable Job Offer from Purchaser shall not be considered Transferred Business Employees for any purpose of this Agreement. Each of the Transferred Business Employees shall be provided by the Purchaser with an aggregate annual amount of paid time-off under the plans of the Purchaser equal to such Transferred Business Employee's current aggregate annual amount of paid time-off, which, for clarity, takes into account and grandfathers all service with the HSBC Sellers and their Affiliates (including vacation time, personal time and sick time); provided that the Purchaser may allocate such aggregate annual amount of paid time-off in a manner consistent with the policies of the Purchaser.

(b) *Termination of Employment with the HSBC Sellers* . As of the Closing Date, and as provided for in the Primary Purchase Agreement, the Transferred Business Employees shall cease active participation in each Employee Plan and shall have a "separation from service" as that term is defined by Section 409A of the Code and the regulations promulgated thereunder. As provided for in the Primary Purchase Agreement, (i) the HSBC Sellers and their respective Affiliates shall retain all assets and Liabilities for the Business Employees and the Affiliated Employees, respectively, under the Employee Plans and (ii) the HSBC Sellers and their respective Affiliates shall be liable for all eligible claims for benefits under the Employee Plans. For purposes of this Agreement, the following claims shall be deemed to be incurred as follows: (i) life, accidental death and dismemberment, business travel accident, disability and workers compensation insurance benefits, upon the event giving rise to such benefits; and (ii) health, vision, dental and/or prescription drug benefits, on the date such services, materials or supplies were provided. As provided for in Section 9.1(b) of the Primary Purchase Agreement, prior to the Closing Date, the HSBC Sellers shall request "good leaver" status from the Remuneration Committee of HSBC Holdings plc with respect to any outstanding awards under the HSBC Holdings plc Share Plan.

(c) *Benefits Following the Closing Date* . Effective as of the Closing Date, Purchaser shall provide the Transferred Business Employees with the same employee benefit plans and programs as those that are provided to similarly situated employees of Purchaser (both by job classification or status and by geographic location), provided that, notwithstanding the

provisions of this Section 9.1(c) or the provisions of Section 9.1(a) (with respect to Purchaser's obligations to make Comparable Job Offers), Purchaser shall not be required to provide benefits under any defined benefit pension plan unless and until a defined benefit pension plan is offered to similarly situated employees of Purchaser or, in the case of a defined benefit pension plan that is closed to new participants, such closed plan is opened to additional participants and generally available to similarly situated employees of Purchaser. For purposes of determining (i) eligibility to participate in and vesting under applicable employee benefit plans of Purchaser or its Affiliates (other than under any employee stock ownership or option plan), (ii) the banking privileges and perquisites applicable to the Transferred Business Employees, (iii) retirement eligibility under any Purchaser plan providing for the grant of equity awards, (iv) for benefit accrual purposes for paid time-off (including vacation time, personal time and sick time) and, if applicable, severance benefits and (v) the level of pay credits under a cash balance plan, in each case, as applicable, each Transferred Business Employee shall be credited with the years of service he or she has been credited with under any comparable Employee Plans; provided that such service shall not be recognized for purposes of (x) grandfathering and/or benefit accruals under any Purchaser defined benefit retirement plan, (y) retiree medical benefits (but it shall be recognized for access-only retiree medical, if applicable) or (z) any employee stock ownership or option plan. Purchaser shall (i) deem satisfied any preexisting conditions and waiting periods under the welfare benefit plans of Purchaser that provide healthcare benefits in which the Transferred Business Employees are eligible to participate to the same extent that such conditions and waiting periods were satisfied under a comparable Employee Plan and (y) subject to the HSBC Sellers providing Purchaser with the applicable information with respect to each Transferred Business Employee in a form that Purchaser determines is administratively feasible to take into account under its plans, cause such plans to honor any expenses incurred by such Transferred Business Employees and their eligible dependents under comparable Employee Plans that are healthcare benefit plans during the portion of the calendar year in which they become Transferred Business Employees for purposes of satisfying applicable deductible, co-insurance, maximum out-of-pocket, and similar expenses, to the same extent that such expenses were recognized under the comparable Employee Plan. Purchaser shall not provide any payment or incentive to any Transferred Business Employee to induce such employee to elect continued participation in any healthcare benefit plan of the HSBC Sellers.

(d) *Severance* . (i) Termination of Transferred Business Employees Following the Closing Date . Purchaser shall pay, or cause to be paid, severance and provide benefits in accordance with the severance schedule set forth on Schedule 9.1(d)(i)(A) , to each Transferred Business Employee whose employment is terminated by Purchaser or any Affiliate of Purchaser without "cause" (within the meaning set forth on Schedule 9.1(d)(i)(B) ) within twelve (12) months after the Closing Date, subject to the execution, delivery and non-revocation of a release of claims in favor of Purchaser, the HSBC Sellers and Assignor and the respective Affiliates of Purchaser, the HSBC Sellers and Assignor.

(ii) Termination of Business Employees who do not become Transferred Business Employees . With respect to Business Employees and Affiliated Employees who do not become Transferred Business Employees for any reason (other than due to having rejected a Comparable Job Offer), (A) Purchaser shall be responsible for reimbursing the HSBC Sellers or their respective Affiliates, as applicable (or reimbursing Assignor if Assignor has directly reimbursed the HSBC Sellers or their Affiliates under the Primary

Purchase Agreement), for any severance benefits but not greater than those described on Schedule 9.1(d)(i)(A) to the extent a Business Employee or Affiliated Employee rejects an offer of employment from Purchaser that was not a Comparable Job Offer and (B) the HSBC Sellers and their respective Affiliates shall retain and shall satisfy, as provided for in the Primary Purchase Agreement, all severance benefits payable to any other Business Employees or Affiliated Employees, respectively. Except as may otherwise be required by Applicable Law, none of the HSBC Sellers, Assignor or Purchaser or any of their respective Affiliates shall pay or provide severance benefits to any Business Employee and Affiliated Employee who receives a Comparable Job Offer from Purchaser and does not accept such offer. Nothing in this Section 9.1(d)(ii) is intended to conflict with the provisions of Section 9.1(g) , but in the event of an inconsistency, Section 9.1(d)(ii) shall govern. Subject to Applicable Law, the HSBC Sellers, their applicable Affiliates and Purchaser shall cooperate to take commercially reasonable steps to reduce, to the extent possible, the likelihood that severance benefits will be required to be paid to any Business Employees or Affiliated Employees who do not become Transferred Business Employees; provided , however , that, in no event, shall Purchaser, Assignor or the HSBC Sellers be required to find alternative employment for such employees at Purchaser, Assignor or the HSBC Sellers or one of their respective Affiliates.

(e) *Retirement Plans* . Effective as of the Closing Date, to the extent permitted by Applicable Law, and as provided for in Section 9.1 (e) of the Primary Purchase Agreement, the HSBC Sellers shall take action to provide that the account balances and accrued benefits, as applicable, of all Transferred Business Employees under the tax-qualified employee savings plan(s) (the " HSBC's Savings Plan ") and pension plan(s) that are sponsored by the HSBC Sellers or any of their respective Affiliates in the United States in which the Transferred Business Employees participated immediately prior to the Closing Date shall vest in full. Purchaser shall take commercially reasonable action to permit Purchaser's tax-qualified employee savings plan(s) maintained in the United States and in which Transferred Business Employees participate to accept rollover contributions of "eligible rollover distributions" (within the meaning of Section 402(c)(4) of the Code) for the benefit of participating Transferred Business Employees.

(f) *Annual Incentives* . (i) In accordance with Section 9.1(f) of the Primary Purchase Agreement, the HSBC Sellers shall be liable for the payment of all formulaic incentive bonuses and annual discretionary bonuses to the Transferred Business Employees with respect to the calendar year commencing on January 1, 2011 and ending on December 31, 2011. In addition, in accordance with Section 9.1(f) of the Primary Purchase Agreement, the HSBC Sellers shall be liable for the payment of any formulaic incentive bonuses, including monthly, quarterly and semi-annual incentive bonuses, to the Transferred Business Employees with respect to the period commencing on January 1, 2012 and ending on the Closing Date. Purchaser acknowledges that such payments shall be made consistent with past practice of the applicable HSBC Seller, notwithstanding that Transferred Business Employees may not be employed by the HSBC Sellers or any of their respective Affiliates at the time of payment.

(ii) Purchaser shall provide Transferred Business Employees an annual discretionary bonus opportunity prorated for calendar year 2012, based upon the number of days elapsed between the Closing Date and December 31, 2012 (with the amount, if any, determined consistent with Purchaser's internal methodology for awarding annual discretionary bonuses). Purchaser acknowledges that HSBC shall be responsible for and shall pay to the

Transferred Business Employees a prorated portion of the annual discretionary bonuses accrued for the Transferred Business Employees prior to the Closing Date, calculated using accruals for performance year 2011, based upon the number of days elapsed between January 1, 2012 and the Closing Date. For purposes of clarity, and as provided for in Section 9.1(f) of the Primary Purchase Agreement, the HSBC Sellers and their respective Affiliates shall retain all liabilities for, and shall be responsible for the payment of, any formulaic incentive bonus amounts payable to the Transferred Business Employees for performance periods occurring prior to Closing Date under any formulaic incentive plans maintained by the HSBC Sellers or their Affiliates (for example, under any monthly, quarterly or commissions-based plans), and such formulaic incentive plans shall not be taken into consideration when determining the obligations of the Purchaser and the HSBC Sellers under this Section 9.1(f)(ii) .

(g) *WARN Act* . The parties hereto agree to cooperate in good faith, including by sharing information about terminations of employment in a timely manner, to determine whether any notification may be required under the WARN Act as a result of the transactions contemplated by this Agreement. Purchaser shall be responsible for providing any notice (or pay in lieu of notice) required pursuant to the WARN Act with respect to a layoff or plant closing involving Transferred Business Employees that occurs on or after the Closing Date. Subject to Section 9.1(d)(ii) , and as provided for in Section 9.1(g) of the Primary Purchase Agreement, the HSBC Sellers and their respective Affiliates shall be responsible for providing any such notice (or pay in lieu of notice) with respect to a layoff or plant closing occurring prior to, on or after the Closing Date and involving Business Employees or Affiliated Employees, respectively who do not become Transferred Business Employees.

(h) *Employee Communications* . Any communications by Purchaser with the Business Employees and/or Affiliated Employees prior to the Closing Date shall be subject to and in compliance with the terms of this Agreement. Written communications from Purchaser to Business Employees and/or Affiliated Employees shall be subject to prior review, comment and approval by the HSBC Sellers and their respective Affiliates. Purchaser acknowledges that in Section 9.1(h) of the Primary Purchase Agreement, the HSBC Sellers have agreed not to make any promises or commitments to the Business Employees or Affiliated Employees with respect to employment by Purchaser or the terms and conditions thereof.

(i) *Banking Privileges* . Purchaser agrees to provide the Transferred Business Employees with the same banking privileges, if any, that Purchaser generally provides to similarly situated employees of Purchaser (both by job classification or status and by geographic location).

(j) *No Third-Party Rights* . No provision of this Section 9.1 shall create any third-party beneficiary rights in any Business Employee or Affiliated Employee (including any beneficiary or dependent thereof) nor is it intended to amend or alter any benefit plan of Purchaser, the HSBC Sellers or any of their respective Affiliates, or limit the ability of the Purchaser or its Affiliates to amend their benefits plans in any respect at any time nor guarantee any Transferred Business Employee the right to continued employment for any period or with any Person.

(k) *Wage Reporting* . Purchaser and Assignor agree to (and Assignor agrees to cause the HSBC Sellers to) utilize the standard procedure set forth in Revenue Procedure 2004-53 with respect to wage reporting.

(l) *Sign-On Awards* . Purchaser agrees to pay to each Transferred Business Employee a one-time cash sign-on award payment in the amount of (i) $500 for each Transferred Business Employee who is a full-time employee and (ii) $250 for each Transferred Business Employee who is a part-time employee (the "Sign-On Payment"). The Sign-On Payment shall be paid by the Purchaser to each Transferred Business Employee as soon as reasonably practicable following the Closing Date, but in no event later than 30 days following the Closing Date. The Purchaser shall be liable for all costs associated with the payment of the Sign-On Payments.

Section 9.2 Transferred Business Employees . Notwithstanding anything in Section 9.1 to the contrary, Purchaser agrees to work together with HSBC and reasonably to cooperate with HSBC (and as appropriate with Assignor) to delay the separation from the HSBC Sellers and the start date with Purchaser for any Transferred Business Employees who are necessary to assist the HSBC Sellers in fulfilling their obligations under the Transition Services Agreement.

## ARTICLE X

## TAX MATTERS

Section 10.1 Tax Indemnification . (a) Purchaser shall pay or cause to be paid, shall be liable for, and shall indemnify, defend and hold Assignor and the HSBC Sellers and their respective Affiliates harmless from and against any and all Taxes relating to the Transferred Business other than Excluded Taxes.

(b) Payment in full of any amount due from Purchaser or Assignor to the appropriate party, including the HSBC Sellers, under this Section 10.1 shall be made to the affected party in immediately available funds at least two (2) Business Days before the date payment of the Taxes to which such payment relates is due, or, if no Tax is payable, within fifteen (15) days after written demand is made for such payment.

Section 10.2 Refunds, Credits and Carrybacks . (a) Purchaser acknowledges and agrees that the HSBC Sellers shall be entitled to any refunds or credits of or against any Excluded Taxes. Purchaser shall be entitled to any refunds or credits of or against any Taxes relating to the Transferred Business, other than refunds or credits of or against Excluded Taxes.

(b) Purchaser shall promptly forward, on behalf of Assignor, to the HSBC Sellers or reimburse the HSBC Sellers for (or reimburse Assignor if Assignor has made payments directly to the HSBC Sellers in respect of) any refunds or credits due to the HSBC Sellers (pursuant to the terms of this Article X ) after receipt thereof, and Assignor will forward or will use commercially reasonable efforts to cause the HSBC Sellers to promptly forward, on behalf of Assignor, to Purchaser or reimburse Purchaser for any refunds or credits due Purchaser (pursuant to the terms of this Article X ) after receipt thereof.

Section 10.3 Cooperation . Each party hereto shall, and shall cause its Affiliates to, and Assignor shall use commercially reasonable efforts to cause the HSBC Sellers to, provide such cooperation, documentation and information relating to the Transferred Business as any of them, or the HSBC Sellers, reasonably may request in: (i) filing any Tax Return, amended Tax Return or claim for refund, (ii) determining a liability for Taxes or an indemnity obligation under this Article X or a right to refund of Taxes, (iii) conducting any audit, examination, contest, litigation or other proceeding by or against any Taxing Authority, (iv) determining an allocation of Taxes between a Pre-Closing Period and Post-Closing Period or (v) effecting any other tax provision in this Agreement (including this Article X ) or in the Primary Purchase Agreement (including Article X thereof). Each party (or HSBC, as provided for in Section 10.3 of the Primary Purchase Agreement) will retain all Tax Returns, schedules and work papers, and all material records and other documents relating to Taxes relating to the Transferred Business for Tax periods ending on or prior to the Closing Date until the later of (x) the expiration of the statute of limitations for the Tax periods to which the Tax Returns or other documents relate or (y) eight (8) years following the due date (without extension) for such Tax Returns. Thereafter, the party holding such Tax Returns or other documents (or HSBC, as provided for in Section 10.3 of the Primary Purchase Agreement) may dispose of them after offering the other party reasonable notice and opportunity to take possession of such Tax Returns and other documents at such other party's own expense. Each party (or HSBC, to the extent provided for in Section 10.3 of the Primary Purchase Agreement) shall make its employees reasonably available on a mutually convenient basis at its cost to provide explanation of any documents or information so provided.

Section 10.4 Contest Provisions . Each of Purchaser and Assignor shall, and Assignor shall use commercially reasonable efforts to cause the HSBC Sellers to, promptly notify the others, as applicable, in writing upon receipt of notice of any pending or threatened audits or assessments with respect to Taxes for which such other party (or such other party's Affiliates) may be liable hereunder. Assignor acknowledges and agrees that the HSBC Sellers shall be entitled to participate at their expense in the defense of and, at its option, take control of the complete defense of, any Tax audit or administrative or court proceeding relating to Taxes for which it may be liable, and to employ counsel and other advisors of its choice at its expense. Neither party may agree to settle any claim for Taxes for which the other or the HSBC Sellers may be liable without the prior written consent of such other party or the HSBC Sellers, as applicable, which consent shall not be unreasonably withheld.

Section 10.5 Transfer Taxes . (a) Assignor and Purchaser acknowledge that all Transfer Taxes that are payable or that arise as a result of the consummation of the transactions contemplated by the Primary Purchase Agreement shall be paid in accordance with the Primary Purchase Agreement. In order to effectuate the provisions of this Section 10.5 , Assignor and Purchaser agree that any Tax Returns that must be filed in connection with such Transfer Taxes shall be prepared and filed by the party primarily or customarily responsible under Applicable Law for filing such Tax Returns, and such party will use its reasonable best efforts to provide such Tax Returns to the other party (and HSBC, as applicable under the Primary Purchase Agreement), at least ten (10) Business Days prior to the date such Tax Returns are due to be filed. Such Tax Returns shall be prepared consistent with the Allocation Statement pursuant to Section 3.4(a) . Purchaser and Assignor agree to cooperate in the timely completion and filing of all such Tax Returns. Purchaser agrees to timely sign and deliver any certificates or forms as

may be necessary or appropriate to establish an exemption from (or otherwise reduce) such Transfer Taxes. Purchaser agrees to timely file Tax Returns with respect to such Transfer Taxes to the extent that the filing of such Tax Returns is the responsibility of Purchaser under this Section 10.5 . For the avoidance of doubt, any Transfer Taxes resulting from any transfer after the Closing Date of any Purchased Asset or Assumed Liability, or any other property owned after the Closing Date by Purchaser or any of its Affiliates shall be borne by Purchaser and any Tax Returns relating thereto shall be prepared and filed by Purchaser. The parties, subject to the Primary Purchase Agreement with HSBC, shall attempt in good faith to agree, on or prior to the Closing Date, on the fair market value of the Business Premises to be transferred and shall prepare and file any Tax Returns required to be filed by them (or either of them) with respect to Transfer Taxes on a basis consistent with any such agreed valuation.

(b) The parties agree that each of them shall have the right to seek a refund of any and all Transfer Taxes paid by it for which it is responsible pursuant to this Section 10.5 at its own expense (subject to the last sentence of this Section 10.5(b) ). If so requested, the other party shall cooperate in good faith with the party, seeking such refund and will cooperate with the HSBC Sellers with respect to any refund the HSBC Sellers may seek under Section 10.5(a) of the Primary Purchase Agreement. Any refund of Transfer Taxes (and any reasonable out-of-pocket expenses incurred by the parties, in obtaining such refund, provided, in the case of fees and disbursements paid to any accounting firm, such expenses were incurred after providing reasonable advance notice to and consulting in good faith with the other party) shall be shared between the parties, in accordance with the portion of such Tax paid by each such party, and any refund shall be shared with the HSBC Sellers to the extent the HSBC Sellers are required to pay the Tax relating to the refund under the Primary Purchase Agreement.

Section 10.6 Coordination . Notwithstanding anything in this Agreement to the contrary, in the event there is a conflict between Article X and any provision contained in any other article of this Agreement, Article X shall control.

Section 10.7 Tax Treatment of Payments . Assignor and Purchaser and their respective Affiliates shall treat any and all payments under this Article X or Article XIII as an adjustment to the consideration for Tax purposes unless they are required to treat such payments otherwise by applicable Tax laws.

Section 10.8 Limitations and Survival . Notwithstanding anything in this Agreement to the contrary, the indemnification provisions of Section 10.1 are not subject to the limitations of Article XIII and shall survive the Closing until the expiration of the applicable statutes of limitation.

Section 10.9 No Double Recovery . For the avoidance of doubt, neither Purchaser nor Assignor shall be entitled to receive indemnification from the other in respect of all or any portion of any Loss more than once, in each case, whether proceeding under this Article X or Article XIII .

## ARTICLE XI

## CLOSING CONDITIONS

Section 11.1 Conditions to Obligations of Each Party to Close . The respective obligations of each party to effect the transactions contemplated by this Agreement are subject to the satisfaction or, where legally permitted, waiver by such party, prior to or at the Closing, of each of the following conditions:

(a) No statute, rule, regulation, executive order, decree, ruling, permanent injunction or other permanent order shall have become effective (and final and nonappealable) permanently restraining, enjoining or otherwise prohibiting or making illegal the consummation of the transactions contemplated hereby.

(b) All Regulatory Approvals set forth on Schedule 11.1(b) (the " Required Government Approvals ") shall have been obtained, and any applicable waiting periods relating thereto shall have expired or been terminated early.

(c) The Primary Closing (as defined in the Primary Purchase Agreement) shall have occurred.

(d) Assignor shall have received confirmation from HSBC that in HSBC's reasonable judgment this Agreement complies with Section 7.11 of the Primary Purchase Agreement and with all conditions to Assignment in the Primary Purchase Agreement.

Section 11.2 Conditions to Obligation of Assignor to Effect the Closing . The obligation of Assignor to effect the transactions contemplated by this Agreement is subject to the satisfaction or waiver (in the sole discretion of Assignor), prior to or at the Closing, of each of the following conditions:

(a) All of the covenants and other agreements required by this Agreement to be complied with and performed by Purchaser on or before the Closing Date shall have been duly complied with and performed in all material respects.

(b) Each of the representations and warranties of Purchaser contained in Article VI shall be true and correct as of the Closing Date as though made on and as of the Closing Date, except (i) that those representations and warranties which address matters only as of a particular date shall be true and correct as of such particular date; and (ii) where the failure of such representations and warranties in the aggregate to be so true and correct has not had, and would not reasonably be expected to result in, a material adverse effect on Purchaser's ability to consummate the transactions contemplated by this Agreement (disregarding for purposes of this clause (ii) any qualification in the text of the relevant representation or warranty as to materiality, material adverse effect or Knowledge).

(c) Assignor shall have received at the Closing a certificate dated the Closing Date and validly executed on behalf of Purchaser by an appropriate officer certifying that the conditions specified in Section 11.2(a) and Section 11.2(b) have been satisfied.

Section 11.3 Conditions to Obligation of Purchaser to Effect the Closing . Purchaser's obligation to effect the transactions contemplated by this Agreement is subject to the satisfaction or waiver (in Purchaser's sole discretion), prior to or at the Closing, of each of the following conditions:

(a) All of the covenants and agreements required by this Agreement and the Transition Services Agreement among Assignor, Purchaser and the HSBC Sellers to be complied with and performed by Assignor and the HSBC Sellers on or before the Closing Date, shall have been duly complied with and performed in all material respects.

(b) Each of the representations and warranties of Assignor contained in Article V shall be true and correct as of the Closing Date as though made on and as of the Closing Date, except (i) that those representations and warranties which address matters only as of a particular date shall be true and correct as of such particular date; and (ii) where the failure of such representations and warranties in the aggregate to be so true and correct has not had, and would not reasonably be expected to result in, a Material Adverse Effect (disregarding for purposes of this clause (ii) any qualification in the text of the relevant representation or warranty as to materiality, Material Adverse Effect or Knowledge).

(c) Purchaser shall have received at the Closing a certificate dated the Closing Date and validly executed on behalf of Assignor by an appropriate officer of Assignor certifying that the conditions specified in Section 11.3(a) and Section 11.3(b) , to the extent applicable to Assignor, have been satisfied.

(d) No event shall have occurred and no facts or conditions shall exist that individually or in the aggregate, have had, or would reasonably be expected to have, a Material Adverse Effect.

## ARTICLE XII

## TERMINATION

Section 12.1 Termination . This Agreement may be terminated at any time prior to the Closing Date:

(a) by mutual written consent of Purchaser and Assignor;

(b) by Purchaser or Assignor if (i) any Governmental Entity that must grant a Required Government Approval has denied such Required Government Approval, and such denial has become final and nonappealable or (ii) any Governmental Entity of competent jurisdiction shall have issued a final nonappealable order enjoining or otherwise prohibiting the consummation of the transactions contemplated by this Agreement or the Primary Purchase Agreement, unless, in either case, such denial of approval or issuance of such order arises out of, or results from, a material breach by the party seeking to terminate this Agreement of any representation, warranty, covenant or agreement of such party in this Agreement;

(c) by Purchaser or by Assignor, if the Closing shall not have occurred on or before the Outside Date; unless the failure of the Closing to occur by such date arises out of, or results from, a material breach by the party seeking to terminate this Agreement of any representation, warranty, covenant or agreement of such party in this Agreement; and

(d) (i) by Purchaser, if Assignor has breached any of its covenants or agreements or any of its representations or warranties contained in this Agreement, which breach, individually or in the aggregate, would cause the conditions set forth in Section 11.3(a) or Section 11.3(b) to be not satisfied, and such breach is not cured within forty-five (45) days following written notice to Assignor or cannot, by its nature, be cured prior to the Outside Date; provided that Purchaser is not then in material breach of any representation, warranty, covenant or other agreement contained in this Agreement, or (ii) by Assignor, if Purchaser has breached any of its covenants or agreements or any of its representations or warranties contained in this Agreement, which breach, individually or in the aggregate, would cause the conditions set forth in Section 11.2(a) or Section 11.2(b) to not be satisfied, and such breach is not cured within forty-five (45) days following written notice to Purchaser, or cannot, by its nature, be cured prior to the Outside Date; provided that Assignor is not then in material breach of any representation, warranty, covenant or other agreement contained in this Agreement.

(e) In addition, this Agreement will automatically terminate upon termination of the Primary Purchase Agreement pursuant to its terms.

Section 12.2 Effect of Termination . In the event of termination of this Agreement as provided in Section 12.1 , this Agreement shall forthwith become void and have no effect, and none of Assignor, Purchaser, HSBC, any of their respective Affiliates or any of the officers, directors or stockholders of any of them shall have any liability of any nature whatsoever hereunder, or in connection with the transactions contemplated hereby, except (i) the confidentiality provisions of Section 7.5 shall survive any termination of this Agreement, and (ii) notwithstanding anything to the contrary contained in this Agreement, none of Purchaser or Assignor shall be relieved or released from any liabilities or damages arising out of its willful breach of any provision of this Agreement.

## ARTICLE XIII

## SURVIVAL; INDEMNIFICATION

Section 13.1 Survival of Representations and Warranties . The representations and warranties contained in this Agreement shall survive the Closing for the period set forth in this Section 13.1 . All representations and warranties contained in this Agreement and all claims with respect thereto shall terminate on the later of (a) the first (1 st ) anniversary of the Closing Date and (b) the date that is eighteen (18) months after the Primary Closing Date, except that (i) the representations and warranties contained in Sections 5.1 , 5.2 , 5.7 , 6.1 , 6.2 and 6.7 shall survive until the expiration of the applicable statute of limitations; it being understood that in the event notice of any claim for indemnification under this Article XIII has been given (within the meaning of Section 13.4 ) within the applicable survival period, the representations and warranties that are the subject of such indemnification claim shall survive with respect to such claim until such time as such claim is finally resolved. The agreements and covenants contained in this Agreement that by their terms contemplate performance after the Closing Date shall survive the Closing in accordance with their terms.

Section 13.2 Indemnification by Assignor . (a) Assignor hereby agrees that from and after the Closing it shall indemnify, defend and hold harmless Purchaser and its respective Affiliates, and their respective directors, officers, employees (other than the Transferred Business Employees), agents and their heirs, successors and permitted assigns, each in their capacity as such (the " Purchaser Indemnified Parties ") from, against and in respect of any damages, losses, charges, Liabilities, claims, demands, actions, suits, proceedings, payments, judgments, settlements, assessments, deficiencies, interest, penalties, and costs and expenses (including removal costs, remediation costs, closure costs, fines, penalties and expenses of investigation and ongoing monitoring, reasonable attorneys' fees, and reasonable out of pocket disbursements) (collectively, " Losses ") imposed on, sustained, incurred or suffered by, or asserted against, any of the Purchaser Indemnified Parties, whether in respect of third-party claims, claims between the parties hereto, or otherwise, directly or indirectly relating to, or arising out of:

(1) any breach of any representation or warranty made by Assignor under Article V for the period such representation or warranty survives, it being understood that for purposes of this Section 13.2 any qualifications in the text of any such representation or warranty relating to materiality, Material Adverse Effect, or Knowledge shall be disregarded for purposes of determining whether such representation or warranty was breached or the amount of Losses;

(2) any breach of any covenant or agreement of Assignor contained in this Agreement; or

(3) any of (i) the Excluded Liabilities, (ii) Liens that are not Permitted Liens, (iii) the conduct of the Retained Business after the Closing Date or (iv) the conduct of the Non-Assigned Transferred Business after the Closing.

(b) Assignor shall not be liable to the Purchaser Indemnified Parties for (i) any Losses in respect of Section 13.2(a)(1) for any individual claim (or group of directly related claims) less than twenty thousand dollars ($20,000) (each a " de minimis loss ") or (ii) any Losses in respect of Section 13.2(a)(1) unless the Losses therefrom exceed an aggregate amount (including all Losses attributable to Assignor) equal to two hundred fifty thousand dollars ($250,000), and then only for Losses in excess of that amount and up to an aggregate amount equal to twenty-five percent (25%) of the Purchaser Premium.

Section 13.3 Indemnification by Purchaser . (a) Purchaser hereby agrees that from and after the Closing it shall indemnify, defend and hold harmless Assignor, any of its Affiliates, and each of their respective directors, officers, agents and their heirs, successors and permitted assigns, each in their capacity as such (the " Assignor Indemnified Parties " and collectively, with the Purchaser Indemnified Parties, the " Indemnified Parties ") from, against and in respect of any Losses imposed on, sustained, incurred or suffered by, or asserted against, any of the Assignor Indemnified Parties, whether in respect of third-party claims, claims between the parties hereto, or otherwise, directly or indirectly (including any Losses sustained by HSBC for which Assignor must indemnify HSBC pursuant to the Primary Purchase Agreement), relating to, arising out of or resulting from:

(1) any breach of any representation or warranty made by Purchaser under Article VI for the period such representation or warranty survives, it being understood that for purposes of this Section 13.3 any qualifications in the text of any such representation or warranty relating to materiality, material adverse effect, or Knowledge shall be disregarded for purposes of determining whether such representation or warranty was breached;

(2) any breach of a covenant or agreement of Purchaser contained in this Agreement; and

(3) any of the Assumed Liabilities or the conduct of the Transferred Business after the Closing Date.

(b) Purchaser shall not be liable to the Assignor Indemnified Parties for (i) a de minimis loss in respect of Section 13.3(a)(1) or (ii) any Losses with respect to the matters contained in Section 13.3(a)(1) unless the Losses therefrom exceed an aggregate amount equal to two hundred fifty thousand dollars ($250,000), and then only for Losses in excess of that amount and up to an aggregate amount equal to twenty-five percent (25%) of the Purchaser Premium.

Section 13.4 Third-Party Claim Indemnification Procedures . (a) In the event that any written claim or demand for which an indemnifying party (an " Indemnifying Party ") may have liability to any Indemnified Party hereunder, other than those relating to Taxes (which are the exclusive subject of Article X ), is asserted against or sought to be collected from any Indemnified Party by a third party (a " Third-Party Claim "), such Indemnified Party shall promptly, but in no event more than ten (10) days following such Indemnified Party's receipt of a Third-Party Claim, notify the Indemnifying Party in writing of such Third-Party Claim, the amount or the estimated amount of damages sought thereunder to the extent then ascertainable (which estimate shall not be conclusive of the final amount of such Third-Party Claim), any other remedy sought thereunder, any relevant time constraints relating thereto and, to the extent practicable, any other material details pertaining thereto (a " Claim Notice "); provided , however , that the failure timely to give a Claim Notice shall affect the rights of an Indemnified Party hereunder only to the extent that such failure has a material prejudicial effect on the defenses or other rights available to the Indemnifying Party with respect to such Third-Party Claim. The Indemnifying Party shall have thirty (30) days (or such lesser number of days set forth in the Claim Notice as may be required by court proceeding in the event of a litigated matter) after receipt of the Claim Notice (the " Notice Period ") to notify the Indemnified Party that it desires to assume the defense of the Indemnified Party against such Third-Party Claim.

(b) In the event that the Indemnifying Party notifies the Indemnified Party within the Notice Period that it desires to defend the Indemnified Party against a Third-Party Claim, the Indemnifying Party shall have the right to defend the Indemnified Party by appropriate proceedings and shall have the sole power to direct and control such defense at its expense. Once the Indemnifying Party has duly assumed the defense of a Third-Party Claim, the Indemnified Party shall have the right, but not the obligation, to participate in any such defense and to employ separate counsel of its choosing. The Indemnified Party shall participate in any such defense at its expense unless the Indemnifying Party and the Indemnified Party are both named parties to the proceedings and the Indemnified Party shall have reasonably concluded,

based on the written advice of counsel, that representation of both parties by the same counsel would be inappropriate due to actual or potential differing material interests between them. The Indemnifying Party shall not, without the prior written consent of the Indemnified Party, settle, compromise or offer to settle or compromise any Third-Party Claim; provided , however , that no such prior written consent of the Indemnified Party shall be required to any proposed settlement that involves only the payment of money by the Indemnifying Party, includes as an unconditional term thereof the granting by the person asserting such claim or bringing such action of an unconditional release from liability to all Indemnified Parties with respect to such claim and does not include any admission of culpability.

(c) If the Indemnifying Party elects not to defend the Indemnified Party against a Third-Party Claim, whether by not giving the Indemnified Party timely notice of its desire to so defend or otherwise, the Indemnified Party shall have the right but not the obligation to assume its own defense; it being understood that the Indemnified Party's right to indemnification for a Third-Party Claim shall not be adversely affected by assuming the defense of such Third-Party Claim. The Indemnified Party shall not settle a Third-Party Claim without the consent of the Indemnifying Party and/or its respective insurer.

(d) The Indemnified Party and the Indemnifying Party shall cooperate in order to ensure the proper and adequate defense of a Third-Party Claim, including by providing access to each other's relevant business records and other documents, and employees.

(e) The Indemnified Party and the Indemnifying Party shall use reasonable best efforts to avoid production of confidential information (consistent with Applicable Law), and to cause all communications among employees, counsel and others representing any party to a Third-Party Claim to be made so as to preserve any applicable attorney-client or work-product privileges.

Section 13.5 Consequential Damages . Notwithstanding anything to the contrary contained in this Agreement, no Person shall be liable under this Article XIII for any consequential, punitive, special, incidental or indirect damages, including lost profits, except to the extent awarded by a court of competent jurisdiction in connection with a Third-Party Claim.

Section 13.6 Adjustments to Losses . (a) In calculating the amount of any Loss, the proceeds actually received by the Indemnified Party or any of its Affiliates under any insurance policy or pursuant to any claim, recovery, settlement or payment by or against any other Person in each case relating to the Third-Party Claim, net of any actual costs, expenses or premiums incurred in connection with securing or obtaining such proceeds, shall be deducted. Without limiting the generality or effect of any other provision hereof, each Indemnified Party and Indemnifying Party shall duly execute upon request all instruments reasonably necessary to evidence and perfect the subrogation and subordination rights detailed herein, and otherwise cooperate in the prosecution of such claims.

(b) In calculating the amount of any Loss, there shall be deducted an amount equal to any net Tax benefit actually realized (including the utilization of a Tax loss or Tax credit carried forward) as a result of such Loss by the party claiming such Loss, and there shall be added an amount equal to any actual net Tax detriment resulting from such Loss.

(c) Reimbursement . If an Indemnified Party recovers an amount from a third-party in respect of a Loss that is the subject of indemnification hereunder after all or a portion of such Loss has been paid by an Indemnifying Party pursuant to this Article XIII , the Indemnified Party shall promptly remit to the Indemnifying Party the excess (if any) of (i) the amount paid by the Indemnifying Party in respect of such Loss, plus the amount received from the third party in respect thereof, less (ii) the full amount of Loss.

Section 13.7 Payments . The Indemnifying Party shall pay all amounts payable pursuant to this Article XIII , by wire transfer of immediately available funds, promptly following receipt from an Indemnified Party of a bill, together with all accompanying reasonably detailed back-up documentation, for a Loss that is the subject of indemnification hereunder, unless the Indemnifying Party in good faith disputes the Loss, in which event it shall so notify the Indemnified Party. In any event, the Indemnifying Party shall pay to the Indemnified Party, by wire transfer of immediately available funds, the amount of any Loss for which it is liable hereunder no later than three (3) days following any final determination of such Loss and the Indemnifying Party's liability therefor. A "final determination" shall exist when (i) the parties to the dispute have reached an agreement in writing, (ii) a court of competent jurisdiction shall have entered a final and non-appealable order or judgment, or (iii) an arbitration or like panel shall have rendered a final non-appealable determination with respect to disputes the parties have agreed to submit thereto.

Section 13.8 Mitigation . Each Indemnified Party shall use its reasonable best efforts to mitigate any indemnifiable Loss. In the event an Indemnified Party fails to so mitigate an indemnifiable Loss, the Indemnifying Party shall have no liability for any portion of such Loss that reasonably could have been avoided had the Indemnified Person made such efforts.

Section 13.9 Survival of Indemnity . The obligation of Purchaser and Assignor to indemnify under this Article XIII as to claims covered by Section 13.2(a)(1) and Section 13.3(a)(1) , as applicable, shall expire on the applicable expiration date of the applicable representation or warranty, as provided in Section 13.1 , and shall not apply to any claims made after such date, except that the obligation of Purchaser and Assignor to indemnify with respect to bona fide claims for indemnity made in writing by Assignor Indemnified Parties and Purchaser Indemnified Parties, as applicable, prior to such expiration shall continue until final resolution of such claims.

Section 13.10 Remedies Exclusive . Except as otherwise specifically provided herein or in the case of fraud or willful misconduct, the remedies provided in this Article XIII shall be the exclusive remedies of the parties hereto from and after the Closing in connection with any breach of a representation or warranty, or non-performance, partial or total, of any covenant or agreement contained herein except as to Taxes, as to which the provisions of Article X shall control exclusively.

Section 13.11 No Indemnification by HSBC Sellers of Purchasers . It is understood and agreed by Purchaser that no HSBC Seller shall have any obligation whatsoever (including under Article X) to indemnify Purchaser for any matter whatsoever arising in connection with, or arising after, Purchaser's purchase and assumption of the Transferred Business, including the Purchased Assets and the Assumed Liabilities.

Section 13.12 Purchaser's Release of HSBC . Purchaser hereby releases the HSBC Sellers and their respective Affiliates and waives any claims which Purchaser may now or hereafter have against any HSBC Seller or any of their respective Affiliates relating to the physical condition of the Purchased Real Property from and after the Closing.

## ARTICLE XIV

## MISCELLANEOUS

Section 14.1 Entire Agreement; Amendment . All Exhibits (attached hereto and as executed) and Schedules hereto shall be deemed to be incorporated into and made part of this Agreement. This Agreement, together with the Exhibits and Schedules hereto, the Settlement Procedures Agreement and the Transition Services Agreement, contain the entire agreement and understanding among the parties with respect to the subject matter hereof (and supersede any prior agreements, arrangements or understandings among the parties with respect to the subject matter hereof) and there are no agreements, representations, or warranties which are not set forth herein. No provision of this Agreement may be amended or waived except (i) by a writing signed by Assignor and Purchaser and (ii) with the prior written consent of the HSBC Sellers (which consent shall not be unreasonably withheld, delayed or conditioned); provided that no amendment to this Agreement shall diminish the obligations or liabilities of Assignor or the rights of the HSBC Sellers under the Primary Purchase Agreement or as third party beneficiaries of this Agreement.

Section 14.2 Binding Effect; Assignment; Third-Party Beneficiaries . Except as otherwise provided in this Agreement, this Agreement shall be binding upon and inure to the benefit of the parties hereto and their respective successors and assigns. Except as expressly provided herein, this Agreement and all rights hereunder may not be assigned by any party hereto except by prior written consent of the other party hereto; provided that Purchaser may assign its right to acquire any asset and/or the obligation to pay all or part of the consideration and to assume any liability to any wholly owned Subsidiary without the prior written consent of the other party hereto; provided , further, that Purchaser agrees to guarantee the performance of any such wholly owned Subsidiary. The parties intend that this Agreement shall not benefit or create any right or cause of action in or on behalf of any Person other than the parties hereto; provided that the HSBC Sellers are express third party beneficiaries of this Agreement and shall have the right to enforce the provisions of this Agreement against any party hereto to the same extent as if they were a party to this Agreement but only to the extent the provisions sought to be enforced by the HSBC Sellers do not enlarge their rights or expand the obligations or liabilities of Assignor under the Primary Purchase Agreement; provided that nothing in this Agreement shall diminish or offset Assignor's obligations to the HSBC Sellers with respect to the Transferred Business, Purchased Assets or Assumed Liabilities.

Section 14.3 Specific Performance . The parties hereto acknowledge and agree that (i) monetary damages could not adequately compensate any party hereto in the event of a breach of this Agreement by any other party which results in the failure of the transactions contemplated by this Agreement to be consummated by the Outside Date; (ii) the non-breaching party would suffer irreparable harm in the event of such a breach with such an effect; and (iii) the

non-breaching party (or by the HSBC Sellers, as a third-party beneficiaries) shall have, in addition to any other rights or remedies it may have at law or in equity, specific performance and injunctive relief as a remedy for the enforcement hereof. The parties agree to not seek, and agree to waive, any requirement for the securing or posting of a bond in connection with a party seeking or obtaining any relief pursuant to this Section 14.3 .

Section 14.4 Counterparts . This Agreement may be executed in any number of counterparts, each of which shall be deemed to be an original as against any party whose signature appears thereon, and all of which shall together constitute one and the same instrument. This Agreement shall become binding when two or more counterparts hereof, individually or taken together, shall bear the signatures of all of the parties reflected hereon as the signatories. The execution and delivery of this Agreement may be effected by facsimile or any other electronic means such as ".pdf" or ".tiff" files.

Section 14.5 Notices . All notices, request, demands and other communications required hereunder shall be in writing and shall be deemed to have been duly given or made if delivered personally, sent by facsimile transmission or telex confirmed in writing within two (2) Business Days, or sent by registered or certified mail, postage prepaid, as follows:

If to Assignor addressed to:

Oliver H. Sommer
Executive Vice President, Corporate Development
First Niagara Financial Group, Inc.
726 Exchange Street, Suite 618
Buffalo, NY 14210
Facsimile: (716) 819-5157

with a copy to:

John Mineo
SVP, General Counsel & Corporate Secretary
First Niagara Financial Group, Inc.
726 Exchange Street, Suite 618
Buffalo, NY 14210
Facsimile: (716) 819-5158

with an additional copy to:

Michael Friedman, Esq.
Pepper Hamilton LLP
3000 Two Logan Square
Eighteenth and Arch Streets
Philadelphia, PA 19103-2799
Facsimile: (215) 981-4750

and if to Purchaser addressed to:

Peter G. Humphrey
President and Chief Executive Officer
Five Star Bank
220 Liberty Street
Warsaw, NY 14569
Facsimile: (585) 786-1108

with a copy to:

John L. Rizzo
General Counsel
Five Star Bank
220 Liberty Street
Warsaw, NY 14569
Facsimile: (585) 786-1108

with an additional copy to:

James M. Jenkins, Esq.
Harter Secrest & Emery LLP
1600 Bausch & Lomb Place
Rochester, NY 14604
Facsimile: (585) 232-6500

Any party may change the address or fax number to which such communications are to be sent to it by giving written notice of change of address to the other party in the manner provided above for giving notice.

Section 14.6 Provisions Separable . The provisions of this Agreement are independent of and separable from each other, and no provision shall be affected or rendered invalid or unenforceable by virtue of the fact that for any reason any other or others of them may be invalid or unenforceable in whole or in part.

Section 14.7 Expenses . Except as otherwise expressly set forth herein, all fees and expenses payable in connection with the consummation of the transactions contemplated by this Agreement shall be the sole liability of the party incurring such expense.

Section 14.8 Deadlines . If the last day of the time period for the giving of any notice or the taking of any action required under this Agreement falls on a Saturday, Sunday or legal holiday or a date on which banks in the State of New York are authorized by law to close, the time period for giving such notice or taking such action shall be extended through the next Business Day following the original expiration date of such.

Section 14.9 Scope of Agreements . This Agreement shall not create any partnership, joint venture or other similar arrangement between Assignor or any of its Affiliates, on the one hand, and Purchaser or any of its Affiliates, on the other hand.

Section 14.10 Delays or Omissions . Any waiver, permit, consent or approval of any kind or character of any breach or default under this Agreement, or any waiver of any provision or condition of this Agreement shall be effective only to the extent specifically set forth in writing. Notwithstanding any provision set forth herein, no party hereto shall be required to take any action or refrain from taking any action that would cause it to violate any Applicable Law, statute, legal restriction, regulation, rule or order or any Governmental Entity.

Section 14.11 Waiver of Jury Trial . EACH PARTY HERETO HEREBY WAIVES TRIAL BY JURY IN ANY ACTION, PROCEEDING OR COUNTERCLAIM BROUGHT BY ANY OF THEM AGAINST THE OTHER ARISING OUT OF OR IN ANY WAY CONNECTED WITH THIS AGREEMENT, OR ANY OTHER AGREEMENTS EXECUTED IN CONNECTION HEREWITH, OR THE ADMINISTRATION THEREOF OR ANY OF THE TRANSACTIONS CONTEMPLATED HEREIN OR THEREIN. NO PARTY TO THIS AGREEMENT SHALL SEEK A JURY TRIAL IN ANY LAWSUIT, PROCEEDING, COUNTERCLAIM, OR ANY OTHER LITIGATION PROCEDURE BASED UPON, OR ARISING OUT OF, THIS AGREEMENT OR ANY RELATED INSTRUMENTS OR THE RELATIONSHIP BETWEEN THE PARTIES. NO PARTY WILL SEEK TO CONSOLIDATE ANY SUCH ACTION, IN WHICH A JURY TRIAL HAS BEEN WAIVED, WITH ANY OTHER ACTION IN WHICH A JURY TRIAL CANNOT BE OR HAS NOT BEEN WAIVED. THE PROVISIONS OF THIS SECTION HAVE BEEN FULLY DISCUSSED BY THE PARTIES HERETO, AND THESE PROVISIONS SHALL BE SUBJECT TO NO EXCEPTIONS. NO PARTY HAS IN ANY WAY AGREED WITH OR REPRESENTED TO ANY OTHER PARTY THAT THE PROVISIONS OF THIS SECTION WILL NOT BE FULLY ENFORCED IN ALL INSTANCES.

Section 14.12 Governing Law; Consent to Jurisdiction . The execution, interpretation, and performance of this Agreement shall be governed by the laws of the State of New York without giving effect to any conflict of laws provision or rule (whether of the State of New York or any other jurisdiction) that would cause the application of the law of any other jurisdiction other than the State of New York. EACH PARTY HERETO, TO THE EXTENT IT MAY LAWFULLY DO SO, HEREBY SUBMITS TO THE JURISDICTION OF ANY COURT OF THE STATE OF NEW YORK LOCATED IN THE BOROUGH OF MANHATTAN IN NEW YORK CITY AND THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK, AS WELL AS TO THE JURISDICTION OF ALL COURTS FROM WHICH AN APPEAL MAY BE TAKEN OR OTHER REVIEW SOUGHT FROM THE AFORESAID COURTS, FOR THE PURPOSE OF ANY SUIT, ACTION OR OTHER PROCEEDING ARISING OUT OF SUCH PARTY'S OBLIGATIONS UNDER OR WITH RESPECT TO THIS AGREEMENT OR ANY OF THE AGREEMENTS, INSTRUMENTS OR DOCUMENTS CONTEMPLATED HEREBY AND EXPRESSLY WAIVES ANY AND ALL OBJECTIONS IT MAY HAVE AS TO VENUE IN ANY OF SUCH COURTS.

[ ***Remainder of page left intentionally blank*** ]

IN WITNESS WHEREOF, each of the parties hereto has caused this Assignment, Purchase and Assumption Agreement to be duly executed as an instrument under seal by its officer thereunto duly authorized as of the date first above written.

FIRST NIAGARA BANK, NATIONAL ASSOCIATION

By: _____
Name:
Title:

FIVE STAR BANK

By: _____
Name:
Title:

**Exhibit 10.25**

# PURCHASE AND ASSUMPTION AGREEMENT

by and among

**FIRST NIAGARA BANK, NATIONAL ASSOCIATION**

and

**FIVE STAR BANK**

**JANUARY 19, 2012**

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Exhibit 3.2 Form of Closing Statement

This PURCHASE AND ASSUMPTION AGREEMENT, dated as of January 19, 2012, is between First Niagara Bank, National Association, a national banking association with its principal office in Buffalo, New York (" Seller "), and Five Star Bank, a New York State chartered bank with its principal office in Warsaw, New York (" Purchaser ").

RECITALS

WHEREAS, Seller desires to sell, and Purchaser desires to acquire, certain assets associated with the Banking Centers (as defined below) in accordance with the terms and provisions of this Agreement;

WHEREAS, Seller desire to transfer to Purchaser, and Purchaser desires to assume from Seller, certain liabilities associated with the Banking Centers in accordance with the terms and provisions of this Agreement;

WHEREAS, on the date hereof, Seller and Purchaser are executing and delivering the Assignment, Purchase and Assumption Agreement dated as of the date hereof (the " HSBC Assignment Agreement "), pursuant to which (i) Seller has assigned to Purchaser Seller's right to purchase selected assets and Seller's obligation to purchase related liabilities and (ii) Purchaser has agreed to acquire such selected assets and assume such related liabilities on and subject to the terms and conditions of the HSBC Assignment Agreement;

WHEREAS, Purchaser and Seller acknowledge that each intends to continue to provide retail and business banking services in the geographic regions served by the Banking Centers, subject to any limitations set forth herein.

NOW, THEREFORE, in consideration of and subject to each of the covenants, representations, warranties, terms and conditions hereinafter set forth, the receipt and sufficiency of which are hereby acknowledged, the parties, intending to be legally bound, hereby agree as follows:

## ARTICLE I

## DEFINITIONS; CONSTRUCTION

Section 1.1 Definitions . For purposes of this Agreement, the parties covenant and agree to the following definitions and other terms:

" Accrued Interest and Fees " shall mean (i) with respect to the Assumed Deposits, the interest, fees, costs, and other charges (whether billed or unbilled) that have been accrued but not yet paid, credited or charged to the Assumed Deposits; and (ii) with respect to the Purchased Assets, the interest, dividends, fees, costs, and other charges (whether billed or unbilled) that have been accrued but not yet paid, credited or charged to the Purchased Assets, in each case as set forth in the general ledger of Seller maintained in the ordinary course of business of Seller in accordance with the internal controls and procedures of Seller, consistently applied.

" Additional Excluded Assets " shall have the meaning specified in Section 2.1(b)(9) .

" Adjustment Payment Date " shall have the meaning specified in Section 3.3(d) .

" Affiliate " shall mean, with respect to any Person, any other Person that directly, or through one or more intermediaries, Controls, is Controlled by or is under common Control with, such Person.

" Aggregate Asset Amount " shall have the meaning specified in Section 3.1(b)(2) .

" Agreement " shall mean this Purchase and Assumption Agreement, including the Schedules and Exhibits hereto, as may be amended and/or restated from time to time.

" Allocation Statement " shall have the meaning specified in Section 3.4(a) .

" Applicable Law " shall mean any federal, state, local, domestic or foreign law, including common law, statute, ordinance, rule, regulation, code, order, judgment, injunction or decree enacted, issued, promulgated, enforced or entered by, or any formal interpretive letter issued by, a Government Entity.

" Appraised Value " shall mean, with respect to any real property, the fair market value (assuming current use) of such real property as determined by the appraisal of an independent third-party appraiser mutually selected by Seller and Purchaser to be completed prior to the Closing Date, whose fee shall be split fifty percent/fifty percent (50%/50%) between Seller and Purchaser; provided that if an appraisal cannot be completed prior to the Closing Date, the Appraised Value shall be a fair market value (assuming current use) mutually agreed to by Seller and Purchaser.

" Assignment and Assumption Agreement " shall have the meaning specified in Section 4.2(a)(5) .

" Assumed Agreements " shall have the meaning specified in Section 2.1(a)(10) .

" Assumed Contracts " shall have the meaning specified in Section 2.1(a)(10) .

" Assumed Deposits " shall mean deposits (as defined in 12 U.S.C. § 1813(l)) that are held by Seller and allocated on the records of Seller to the Banking Centers, including demand deposits, savings accounts, money market deposit accounts, mutual fund and reserve fund sweep accounts, negotiable order of withdrawal accounts, certificates of deposit, deposits acquired through the telephone or the internet or other electronic media and, subject to Section 7.10 , IRA, Employee Pension Plan and Keogh accounts, including any debit accounts related thereto, in each case, that are listed on Schedule 1.1(a) (as updated pursuant to Section 7.11 ), excluding : (i) deposits by government agencies; (ii) structured deposits; (iii) brokered deposits; (iv) unclaimed deposits subject to unclaimed property statute/escheatment; and (v) deposits constituting money orders, certified and official checks and other items in the process of clearing.

" Assumed Letters of Credit " shall have the meaning specified in Section 2.1(a)(9) .

" Assumed Liabilities " shall have the meaning specified in Section 2.2(a) .

" ATM " shall mean an automated teller machine.

" ATM Real Property Leases " shall have the meaning specified in Section 2.1(a)(5) .

" Banking Centers " shall mean the branches and offices, including any related drive-thru teller facilities, of Seller and its Subsidiaries listed on Schedule 1.1(b) .

" Banking Center Customers " shall mean, individually and collectively, (i) the Persons named as the owners of the deposit accounts relating to the Assumed Deposits, (ii) the primary obligors under the Purchased Loans, and (iii) other Persons who receive Banking Related Services at the Banking Centers as reflected on the records of Seller, provided that Banking Center Customers shall not include customers in their relationship with a Banking Center that relates to Excluded Business Activities.

" Banking Center Employees " shall mean, as of any particular date: (i) the persons actively employed as of such date by Seller or any of its Subsidiaries principally in connection with the Banking Centers; and (ii) the persons employed as of such date by Seller or any of its Subsidiaries principally in connection with the Banking Centers who are absent from work on account of vacation, jury duty, funeral leave, personal day, sickness, short-term disability, workers compensation leave, military leave, leave under the Family Medical Leave Act or other approved leave of absence or for whom an obligation to return to active employment exists under a contractual obligation or law, in each case, that are listed on Schedule 1.1(c)(i) (as updated pursuant to Section 7.11 ).

" Banking Center Premises " shall mean, as applicable, the Purchased Real Property and/or the real property subject to a Real Property Lease.

" Banking Related Services " shall mean banking and banking-related services, brokerage, custody, financial planning, insurance, estate planning, tax planning, liquidity or cash management, lending (including commercial real estate lending), issuance of credit cards and similar products, investment advisory, investment banking, asset management and trust and fiduciary services.

" Bill of Sale " shall have the meaning specified in Section 4.2(a)(4) .

" Business Day " shall mean any day excluding Saturday, Sunday and any day on which banking institutions located in New York State are authorized or required by Applicable Law or other governmental action to be closed.

" Business Material " shall have the meaning specified in Section 8.7(b) .

" Capital Action " shall have the meaning specified in Section 7.2(b) .

" Cash on Hand " shall have the meaning specified in Section 2.1(a)(12) .

" Claim Notice " shall have the meaning specified in Section 13.4(a) .

" Close of Business " shall mean the local time that the Banking Centers close to the public.

" Closing " shall have the meaning specified in Section 4.1 .

" Closing Date " shall have the meaning specified in Section 4.1 .

" Closing Payment " shall have the meaning specified in Section 3.1(b) .

" Closing Statement " shall have the meaning specified in Section 3.2(a) .

" Closing Statement Date " shall have the meaning specified in Section 3.2(a) .

" Code " shall mean the Internal Revenue Code of 1986, as amended, and the regulations thereunder.

" Comparable Job Offer " shall mean an offer of employment with Purchaser or an Affiliate of Purchaser that sets forth the following terms of employment from the Closing Date through at least December 31, 2012: (i) a position requiring substantially comparable skills and abilities as the employee's position immediately prior to the Closing Date (it being understood that whether a position is managerial or non-managerial shall not in and of itself preclude an offer from being a Comparable Job Offer), (ii) does not involve a significant change in work schedule, (iii) has benefits that are comparable to those of similarly situated employees of Purchaser, (iv) has an annual aggregate total compensation (the combination of annual base salary or rate of pay and incentive and commission arrangements) opportunity per performance period that is comparable to the aggregate total compensation opportunity per performance period in effect for such employee immediately prior to the Closing, (v) is at a work location not more than thirty-five (35) miles from such employee's work location immediately prior to the Closing Date, and (vi) includes a work status (full or part-time) that is not changed from that in effect immediately prior to the Closing Date.

" Confidentiality Agreement " shall mean the confidentiality agreement, dated as of August 10, 2011, among First Niagara Financial Group Inc., HSBC and Financial Institutions, Inc., the sole shareholder of Purchaser.

" Contract " shall mean any written agreement, contract, arrangement, bond note, commitment, franchise, indemnity, indenture, instrument, lease or license, together with any exhibits, schedules or documents executed or delivered in connection therewith and any modifications, amendments, restatements or other supplements thereto.

" Control " and the correlative terms "Controlling" and "Controlled" shall mean, as used with respect to any Person, possession of the power to direct or cause the direction of the management and policies of such Person, directly or indirectly, whether through the ownership of voting securities, by contract or otherwise.

" Controlled Group Liability " shall mean any and all liabilities with respect to any employee benefit plan of Seller or its ERISA Affiliates, including (i) under Title IV of ERISA, (ii) under Section 302 of ERISA, (iii) under sections 412, 430 and 4971 of the Code, (iv) under any promise to provide retiree welfare coverage, and (v) as a result of a failure to comply with the continuation coverage requirements of Section 601 et seq . of ERISA and Section 4980B of the Code.

" Conversion " shall mean the conversion of the processing, reporting, payment and other systems associated with the Banking Centers from the systems of Seller to the systems of Purchaser.

" Conversion Plan " shall have the meaning specified in Section 8.6(c)(1) .

" Conversion Project Manager " shall have the meaning specified in Section 8.6(a) .

" CRA " shall mean the Community Reinvestment Act of 1977, as amended.

" CRA Assets " shall have the meaning specified in Section 2.1(a)(8) .

" Credit Card Accounts and Receivables " shall mean the accounts and Receivables related to the credit cards issued by Seller or an Affiliate of Seller to its customers, including Banking Center Customers.

" Credit Documents " shall mean all documents evidencing or securing a Purchased Loan or Assumed Letter of Credit, in the possession of Seller or its Subsidiaries (regardless of where located, including in file or imaging systems of Seller or its Subsidiaries), including, without limitation, all original notes, reimbursment agreements, security agreements, deeds of trust, mortgages, loan agreements, and corresponding reports, certifications and isclosures required by Applicable Law, guarantees, sureties and insurance policies (including title insurance policies), applications and credit information, financial information, insurance information, signature cards, all information on obligors and borrowers and guarantors, taxpayer identification number certifications and records relating thereto, and all modifications, waivers and consents relating to any of the foregoing.

" Damages " shall mean all actions, costs, damages, disbursements, obligations, penalties, liabilities, losses, expenses, assessments, judgments, settlements or deficiencies (including any interest, penalties, investigation, legal, accounting and other reasonable out-of-pocket costs and expenses incurred in the investigation, collection, prosecution and defense of any action, suit, proceeding or claim and amounts paid in settlement, but not including indirect, incidental, exemplary, special, consequential or punitive damages that are imposed upon or otherwise incurred by the indemnified party).

" de minimis loss " shall have the meaning specified in Section 13.2(b) .

" Designated Footprint " shall mean those areas that are within five (5) miles of any of the Banking Centers.

" Disclosure Schedule " shall mean, with respect to Purchaser or Seller, a schedule delivered by it to the other upon the execution and delivery of this Agreement setting forth, among other things, items the disclosure of which is required under this Agreement, either in response to an express disclosure requirement contained in a provision of this Agreement or as an exception to one or more of the representations and warranties or covenants contained in this Agreement; provided that the mere inclusion of an item in a Disclosure Schedule as an exception to a representation will not be considered an admission by the disclosing party that such item (or any non-disclosed item or information of comparable or greater significance) represents a material exception or fact, event or circumstance or that such item has had or is expected to result in a Material Adverse Effect, as the case may be; provided , further , that an item disclosed by either party in such party's Disclosure Schedule shall be deemed to be a disclosure against any other representation, warranty or covenant of such party in this Agreement if such disclosure would reasonably appear on its face to be a disclosure thereunder if repeated thereunder.

" Employee Pension Plan " shall mean any employee pension plan for which Seller serves as a trustee, including, but not limited to, employee pension benefit plans as defined in Section 3(2) of ERISA, retirement plans qualified under the requirements of Section 401(a) of the Code, nonqualified deferred compensation plans, excess benefit plans and supplemental executive retirement plans.

" Employee Plans " shall have the meaning specified in Section 5.17(b) .

" Environment " shall mean any soil, surface waters, wetlands, groundwaters, sediments, surface or subsurface strata, ambient air and any other environmental medium.

" Environmental Law " shall mean any law, statute, regulation, rule, ordinance, by-law, order or other binding decision of any Governmental Entity regarding the protection of the Environment, Hazardous Materials, exposure to Hazardous Materials, worker health and safety and/or public health and safety.

" Environmental Objections " shall have the meaning specified in Section 8.10.

" ERISA " shall mean the Employee Retirement Income Security Act of 1974, as amended, and the regulations thereunder.

" ERISA Affiliate " shall mean, with respect to any entity, trade or business, any other entity, trade or business that is a member of a group described in Section 414(b), (c), (m) or (o) of the Code or Section 4001(b)(1) of ERISA that includes the first entity, trade or business, or that is a member of the same "controlled group" as the first entity, trade or business pursuant to Section 4001(a)(14) of ERISA.

" Excluded Assets " shall have the meaning specified in Section 2.1(b) .

" Excluded Business Activities " shall have the meaning specified in Section 2.1(c) .

" Excluded Contracts " shall mean any and all Contracts of Seller and its Affiliates that are not Assumed Contracts, including, but not limited to, Contracts that apply to operations of Seller or its Affiliates other than solely to the Banking Centers and all data processing Contracts, regardless of scope.

" Excluded Deposits " shall mean any and all deposits of Seller and its Affiliates that are not Assumed Deposits.

" Excluded Liabilities " shall have the meaning specified in Section 2.2(b) .

" Excluded Taxes " shall mean (A) any Income Taxes of Seller or any of its Subsidiaries (whether or not relating to the Banking Centers), (B) any Income Taxes of any member of an affiliated, consolidated, combined, or unitary group of which Seller or any of its Subsidiaries was a member on or prior to the Closing Date, including pursuant to Treasury Regulation Section 1.1502-6 or any analogous or similar state, local or non-U.S. law or regulation, (C) any Income Taxes of any other Person imposed on any of Seller or its Subsidiaries as a transferee or successor, by contract or pursuant to any law, rule or regulation, and (D) any Non-Income Taxes relating to the Banking Centers for any Pre-Closing Period, provided that the allocation of the amount of Non-Income Taxes between the Pre-Closing Period and the Post-Closing Period shall be determined (i) with respect to Transfer Taxes in accordance with Article X , (ii) with respect to real and personal property and other Non-Income Taxes imposed on a time basis (other than any Transfer Taxes) by allocating pro rata on a time basis and (iii) with respect to any Non-Income Taxes not imposed on a time basis, on a closing of the books method.

" FDI Act " shall mean the Federal Deposit Insurance Act, as amended.

" FDIC " shall mean the Federal Deposit Insurance Corporation.

" Federal Funds Rate " shall mean, for any day, the rate per annum (rounded upwards, if necessary, to the nearest 1/100th of 1%) equal to the average of the rates on overnight Federal funds transactions with members of the Federal Reserve System arranged by Federal funds brokers on such day, as published by the Federal Reserve Bank of New York on the Business Day next succeeding such day; provided that, if such day is not a Business Day or the Federal Funds Rate is not so published for any day, the Federal Funds Rate for such day shall be such rate on such transactions on the next Business Day as so published on the next succeeding Business Day.

" Final Closing Statement " shall have the meaning specified in Section 3.3(a) .

" Final Schedules " shall have the meaning specified in Section 7.11(b) .

" FINRA " shall mean the Financial Industry Regulatory Authority.

" GAAP " shall mean generally accepted accounting principles in the United States of America consistently applied.

" Governmental Entity " shall mean any federal, state, local, domestic or foreign agency, court, tribunal, administrative body, arbitration panel, department or other legislative, judicial, governmental, quasi-governmental entity or Self-Regulatory Organization.

" Hazardous Material " shall mean any pollutant, contaminant, hazardous substance, toxic substance, hazardous material or hazardous waste as defined under any Environmental Law, including any petroleum product, asbestos-containing material, polychlorinated biphenyl or radon, and any other substances that by their nature or use are subject to regulation under Environmental Laws.

" HSBC Assignment Agreement " shall have the meaning specified in the Preamble.

" HSR Act " shall mean the Hart-Scott-Rodino Antitrust Improvements Act of 1976.

" Income Tax " shall mean any federal, state, local, or non-U.S. income Tax.

" Indemnified Parties " shall have the meaning specified in Section 13.3(a) .

" Indemnifying Party " shall have the meaning specified in Section 13.4(a) .

" Information " shall have the meaning specified in Section 7.5 .

" Intellectual Property " shall mean (i) all intellectual property, industrial property, proprietary and similar rights in any jurisdiction owned or held for use under license, whether or not subject to statutory registration or protection, and whether now known or hereafter recognized in any jurisdiction, including such rights in and to: (A) Trademarks; (B) inventions and discoveries (whether or not reduced to practice), all improvements thereto, all patents (including utility and design patents, industrial designs and utility models), registrations, invention disclosures and applications therefor, including divisions, revisions, supplementary protection certificates, continuations, continuations-in-part and renewal applications, and including renewals, extensions, reissues and re-examinations thereof; (C) published and unpublished works of authorship (including databases and other compilations of information, computer and electronic data processing programs, software, both source code and object code, flow charts, diagrams, descriptive texts and similar items), copyrights therein and thereto, and registrations and applications therefor, and all renewals, extensions, restorations and reversions thereof; (D) trade secrets, confidential business and technical information and any other confidential information (including ideas, research and development, know-how, formulae, drawings, prototypes, models, designs, technology, compositions, manufacturing, production and other processes and techniques, schematics, technical data, engineering, production and other designs, drawings, engineering notebooks, industrial models, software and specifications, business methods, customer lists, representative lists and supplier lists, and any other information meeting the definition of a trade secret under the Uniform Trade Secrets Act or similar laws) and (E) moral rights, design rights, mask works and rights of privacy and publicity; and (ii) in the case of (i)(A) through (i)(E), all benefits, privileges, causes of action and remedies relating to any of the foregoing, whether before or hereafter accrued (including the rights to sue for all past, present or future infringements or other violations of any rights in the assigned and to settle and retain proceeds from any such actions).

" IRA " shall mean an account created by a trust for the benefit of an individual or his or her beneficiary and that complies with the provisions of Section 408 or 408A of the Code.

" Keogh " shall mean an account created by a trust for the benefit of employees (some or all of whom are owner-employees) and that complies with the provisions of Section 401 of the Code.

" Knowledge " shall mean (i) with respect to Purchaser, the actual knowledge, without independent investigation, of the officers of Purchaser listed on Schedule 1.1(e) and (ii) with respect to Seller, the actual knowledge, without independent investigation, of the officers of Seller listed on Schedule 1.1(f) . For purposes of this definition, an officer shall be deemed to have actual knowledge of facts that would be reasonably expected to come to the attention of such officer in the course of the management reporting practices of Purchaser or Seller, as applicable.

" Landlord Consent " shall mean the consent (or waiver) of a landlord under a Real Property Lease or ATM Real Property Lease, as applicable, as shall be required pursuant to the terms of such Real Property Lease or ATM Real Property Lease, as applicable, to assign or sublease the Banking Center Premises or ATM, as applicable, to Purchaser.

" Letter of Credit " shall mean any letter of credit, including any standby letter of credit, issued by Seller in favor of a Banking Center Customer.

" Liabilities " shall mean any and all debts, liabilities, commitments and obligations of any kind, whether fixed, contingent or absolute, matured or unmatured, liquidated or unliquidated, accrued or not accrued, asserted or not asserted, known or unknown, determined, determinable or otherwise, whenever or however arising (including whether arising out of any contract or tort based on negligence or strict liability) and whether or not the same would be required by GAAP to be reflected in financial statements or disclosed in the notes thereto.

" License Agreement " shall mean the license agreement between Seller and Purchaser, in a form to be agreed upon between Seller and Purchaser after the date of this Agreement, with each acting reasonably and in good faith.

" Lien " shall mean any mortgage, deed of trust, easement, declaration, restriction, pledge, hypothecation, assignment, deposit arrangement, option, equity interest, encumbrance, lien (statutory or other), preference, participation interest, priority or other security agreement or preferential arrangement of any kind or nature whatsoever relating to that property, including any conditional sale or other title retention agreement, any financing lease having substantially the same economic effect as any of the foregoing and the filing of any financing statement under the UCC or comparable law of any jurisdiction to evidence any of the foregoing; provided , however , that no Lien shall be deemed to be created by this Agreement.

" Loans " shall mean all loans or other extensions of credit, including, but not limited to, loans which have been partially charged off, interests in loan participations and assignments, customer liabilities on bankers acceptances as well as legally binding commitments and obligations to extend credit (including any unfunded or partially funded revolving loans, lines of credit, overdraft lines of credit and courtesy extensions or similar arrangements, and including short-term municipal investments (such as bond anticipation notes and revenue anticipation notes)), but excluding all Credit Card Accounts and Receivables.

" Losses " shall have the meaning specified in Section 13.2(a) .

" Material Adverse Effect " shall mean any circumstance or change in or effect on the Purchased Assets or the Assumed Liabilities that, individually or in the aggregate, with all other circumstances, changes or effects is materially adverse to, or would reasonably be expected to have a materially adverse effect on (a) the business, assets, properties, operations, results of operations or financial condition of the Purchased Assets, taken as a whole ( provided , however , that with respect to this clause (a) "Material Adverse Effect" shall not include effects to the extent resulting from (i) changes after the date of this Agreement in general economic, legal, regulatory or political conditions (including the outbreak or escalation of hostilities or acts of terrorism to the extent not directly impacting Purchased Assets); (ii) changes after the date of this Agreement in general financial and capital market conditions, including changes generally in prevailing interest rates; (iii) changes after the date of this Agreement in general industry conditions affecting financial institutions, including banks and broker-dealers; (iv) changes after the date of this Agreement in law, International Financial Reporting Standards, GAAP or regulatory accounting principles, or authoritative interpretations thereof; (v) any action or omission required to be taken or omitted to be taken pursuant to the express terms of this Agreement; and (vi) the public announcement of this Agreement, including the impact thereof on customers, suppliers and employees and others having business relationships with the Banking Centers and, in the case of clauses (i) through (iv), only to the extent that such items do not have a disproportionate adverse effect on Seller, the Purchased Assets or the Assumed Liabilities, taken as a whole); or (b) the ability of the Seller to perform its obligations under this Agreement or the other Transaction Documents, or timely consummate the transactions contemplated hereby and thereby.

" Necessary Permits " shall have the meaning specified in Section 5.16 .

" Net Book Value " shall mean the book value net of any associated allowance, reserve or other contra-asset account, as reflected in Seller's books and records, determined in accordance with GAAP consistently applied; provided , however , that no Federal, state, local, or foreign income tax assets or tax liabilities shall be reflected.

" Non-Income Taxes " shall mean Taxes other than Income Taxes.

" Nonperforming Loan " shall mean, as of the Close of Business on the Closing Date, any Loan with respect to which (i) any principal or interest on such loan or receivable shall be due and unpaid by the obligor thereunder for sixty (60) days or more prior to the Closing Date (other than loans guaranteed by the Veterans' Administration or the Federal Housing Administration), (ii) an obligor has filed or has had filed against such obligor proceedings in bankruptcy, trusteeship or receivership, (iii) the loans or receivables have been completely charged off, (iv) the balance is no longer owed by the obligor whether or not as a result of a settlement agreement between the obligor and Seller or any of its Subsidiaries or (v) in the case of a mortgage loan, the loan has been repurchased by Seller or any of its Subsidiaries.

" Notice Period " shall have the meaning specified in Section 13.4(a) .

" Outside Date " shall mean July 30, 2012.

" Permitted Liens " shall mean (i) Liens for Taxes, assessments or governmental charges or levies not yet due and payable or which although delinquent can be paid without penalty or are being contested in good faith by appropriate proceedings and for which adequate provision has been made on Seller's books and records; (ii) Liens resulting from a filing by a lessor as a precautionary filing for a lease; (iii) Liens imposed by law, such as carriers', warehousemen's and mechanics' Liens and other similar liens arising in the ordinary course which secure payment of obligations not more than thirty (30) days past due or which are being contested in good faith by appropriate proceedings and for which adequate provision has been made on Seller's books and records; (iv) purchase money security interests for the purchase or leasing of office equipment, computers, vehicles and other items of tangible personal property so long as the existence of such lease or other financing arrangement has been disclosed to the party to whom the applicable representation is made by express reference in the Disclosure Schedule and for which such lease or other financing arrangement is included in the Assumed Liabilities; (v) in the case of real property, zoning, building, subdivision, environmental regulations, entitlement or other land use regulations; and (vi) in the case of real property, easements, quasi-easements, licenses, covenants, rights-of-way, and rights of re-entry that are of record and that do not impede the ownership, operation or value of such real property in any material respect.

" Person " shall mean an individual, a corporation, a partnership, an association, a limited liability company, a Government Entity, a trust or other entity or organization.

" Personal Property Leases " shall have the meaning specified in Section 2.1(a)(4) .

" Phase I ESAs " shall have the meaning specified in Section 7.1(a).

" Post-Closing Period " shall mean any taxable period (or portion thereof) beginning after the Closing Date.

" Pre-Closing Period " shall mean any taxable period (or portion thereof) ending on (and including) the Closing Date or ending prior to the Closing Date.

" Premium " shall have the meaning specified in Section 3.1(b)(2)(i) .

" Previously Disclosed " means, as of any given date, that the existence of a fact or condition was disclosed by one party to the other party through a Disclosure Schedule.

" Purchased Assets " shall have the meaning specified in Section 2.1(a) .

" Purchased ATMs " shall have the meaning specified in Section 2.1(a)(5) .

" Purchased Loans " shall have the meaning specified in Section 2.1(a)(6) .

" Purchased Overdrafts " shall mean overdrafts (whether specifically extended or courtesy) of the book balance of any accounts listed on Schedule 1.1(h) (as updated pursuant to Section 7.11 ).

" Purchased Personal Property " shall have the meaning specified in Section 2.1(a)(3) .

" Purchased Real Property " shall have the meaning specified in Section 2.1(a)(1) .

" Purchaser " shall have the meaning specified in the Preamble.

" Purchaser Indemnified Parties " shall have the meaning specified in Section 13.2(a) .

" Purchaser Objection " shall have the meaning specified in Section 3.3(c) .

" Purchaser Regulatory Approvals " shall have the meaning specified in Section 6.3 .

" Real Property Leases " shall have the meaning specified in Section 2.1(a)(2) .

" Receivables " shall mean any amount posted as owing by an obligor under any credit card account, including any amounts owing for the payment of goods and services, cash advances, cash advance fees, access check fees, annual card membership fees, Accrued Interest and Fees and any other fee, expense or charge of every nature, kind and description whatsoever, less any amount owed by Seller or any of its Affiliates to the obligor as a credit balance, but only to the extent that such amounts owed by the obligor are owned by Seller or its Affiliates.

" Regulatory Approvals " shall mean, collectively, the Seller Regulatory Approvals and the Purchaser Regulatory Approvals.

" Related Person " shall mean, with respect to a Person, any other Person that is (i) an Affiliate of such Person, (ii) established for the benefit of such Person, or (iii) a member of such Person's immediate family.

" Relationships " shall mean any existing and future banking or other financial relationships with an identified Person or group of Persons and their Related Persons, including, but not limited to, any deposit, lending, investment, investment banking, asset management or financial advisory relationships and any accounts related thereto.

" Release " shall mean any release, migration, seepage, discharge, or disposal into the Environment, including, without limitation, as any of the foregoing may be defined in or pursuant to any Environmental Laws.

" Remedial Action " shall have the meaning specified in Section 7.2(b) .

" Required Government Approvals " shall have the meaning specified in Section 11.1(b) .

" Restricted Entities " shall have the meaning specified in Section 7.9(a) .

" Retained Employees " shall mean those employees of Seller or its Affiliates that will not or do not become Transferred Banking Center Employees on the Closing Date.

" Safe Deposit Agreements " shall have the meaning specified in Section 2.1(a)(7) .

" SBA " shall mean the United States Small Business Administration.

" SBA Loan " shall mean a Purchased Loan that is secured by an SBA guaranty whether in whole or in part; provided that no SBA Loan shall be considered a Purchased Loan unless and until such time as any required third-party (including the SBA) consents related to the transfer of such SBA Loan have been obtained.

" Self-Regulatory Organization " shall mean FINRA, the National Futures Association, the Chicago Board of Trade, the New York Stock Exchange, any national securities exchange (as defined in the Securities Exchange Act of 1934, as amended), any other securities exchange, futures exchange, contract market, any other exchange or corporation or similar self-regulatory body or organization.

" Seller " shall have the meaning specified in the Preamble.

" Seller Approvals " shall have the meaning specified in Section 5.3 .

" Seller Indemnified Parties " shall have the meaning specified in Section 13.3(a) .

" Seller Names " shall mean the names "FNFG," "First Niagara," the blue/white/gold logo of Seller and any Trademark, name or logo related thereto, or employing the word or phrase "FNFG," "First Niagara," or any derivation, variation, translation or adaptation thereof, and any Trademark, word, name or logo confusingly similar thereto or embodying any of the foregoing, whether alone or in combination with any other words, names, logos or trademarks, and whether registered or unregistered, including, but not limited to, the items listed on Schedule 2.1(b)(6) .

" Seller Name License " shall have the meaning specified in Section 8.7(b) .

" Seller Regulatory Approvals " shall have the meaning specified in Section 5.3 .

" Signage " shall mean any proprietary display, including a display bearing a Seller Name, used by Seller or its Affiliates at the Banking Centers to identify Seller's or its Affiliates' place(s) of business or to advertise Seller's or its Affiliates' products, services or brand.

" Sublease Agreement " shall have the meaning specified in Section 8.2(b) .

" Subsidiary " of a Person shall mean any other Person, of which such Person, directly or indirectly, owns securities or other ownership interest having (i) a majority of the economic interests of such entity or (ii) the ordinary voting power to elect a majority of the board of directors or such Person performing similar functions.

" Tax " shall mean any tax of any kind, including any federal, state, local and foreign income, profits, license, severance, occupation, windfall profits, capital gains, capital stock, transfer, registration, social security (or similar), production, franchise, gross receipts, payroll, sales, employment, use, property, excise, value added, estimated, stamp, alternative or add-on minimum, environmental, withholding and any other tax or like assessment, together with all interest, penalties and additions imposed with respect to such amounts and including any obligation to indemnify or otherwise assume or succeed to the tax liability of any other Person.

" Tax Return " shall mean any return, declaration, report, claim for refund or information return or statement filed or required to be filed with any Taxing Authority relating to Taxes, including any schedule or attachment thereto, and including any amendment thereof.

" Taxing Authority " shall mean any Governmental Entity having or purporting to exercise jurisdiction with respect to any Tax.

" Third-Party Claim " shall have the meaning specified in Section 13.4(a) .

" Trademarks " shall mean trademarks, service marks, certification marks, collective marks, Internet domain names, e-mail addresses, logos, product names and slogans, symbols, trade dress, assumed names, fictitious names, trade names, d/b/a's, brand names, business names, corporate names and any and every other form of trade identity and other indicia of origin, whether registered or unregistered, all applications and registrations for the foregoing, including all renewals of same, and all goodwill associated therewith and symbolized thereby.

" Transfer Taxes " shall mean all U.S. federal, state and local and all foreign or other excise, sales, use, value added, transfer (including real property transfer or gains), stamp, documentary, filing, recordation and other similar taxes and fees that may be imposed or assessed in connection with the transfer of the Purchased Assets as contemplated under this Agreement, together with any interest, additions or penalties with respect thereto and any interest in respect of such additions or penalties.

" Transferred Banking Center Employees " shall mean the Banking Center Employees who accept Purchaser's offer of employment.

" Transition Coordinators " shall have the meaning specified in Section 7.8 .

" Transition Services Agreement " shall mean a Transition Services Agreement in a form to be agreed upon between Seller and Purchaser after the date of this Agreement, with each acting reasonably and in good faith, to provide for timing and other matters commonly addressed in such agreements in connection with sales of bank branches.

" Transitional Period " shall have the meaning specified in Section 8.7(b) .

" UCC " shall mean the Uniform Commercial Code, as in effect in New York State or any other applicable state.

" Update Date " shall have the meaning specific in Section 7.11(a) .

" WARN Act " shall mean the federal Worker Adjustment and Retraining Notification Act, as amended, or any similar state, local, or foreign laws with respect to any event affecting Banking Center Employees.

Section 1.2 Interpretation . (a) Unless the context otherwise requires:

(1) references herein to specific Articles, Sections, Subsections, Exhibits or Schedules shall refer, respectively, to Articles, Sections, Subsections, Exhibits or Schedules of this Agreement;

(2) references to any agreement or other document are to such agreement or document as amended, modified, supplemented or replaced from time to time;

(3) references to any statute or regulation refer to such statute or regulation as amended, modified, supplemented or replaced from time to time (and, in the case of statutes, include any rules and regulations promulgated under the statute) and references to any Section of any statute or regulation include any successor to such section;

(4) references to any Government Entity include any successor to such Government Entity;

(5) the words “hereof,” “herein,” and “hereunder” and words of similar import, when used in this Agreement, shall refer to this Agreement as a whole and not to any particular provision of this Agreement;

(6) the terms defined in the singular have a comparable meaning when used in the plural, and vice versa;

(7) the terms “Dollars” and “$” mean U.S. Dollars;

(8) wherever the word “include,” “includes,” or “including” is used in this Agreement, it shall be deemed to be followed by the words “without limitation”; and

(9) references herein to any gender include the other gender.

(b) The table of contents and headings contained in this Agreement are for reference purposes only and do not limit or otherwise affect any of the provisions of this Agreement.

(c) The parties to this Agreement have participated jointly in the negotiation and drafting of this Agreement. In the event of an ambiguity or a question of intent or interpretation, this Agreement shall be construed as if drafted jointly by the parties, and no presumption or burden of proof shall arise favoring or disfavoring any party by virtue of the authorship of any provision of this Agreement.

## ARTICLE II

## PURCHASE AND SALE OF PURCHASED ASSETS AND ASSIGNMENT AND ASSUMPTION OF ASSUMED LIABILITIES

Section 2.1 Purchase and Sale of Purchased Assets . (a) *Purchased Assets.* At the Closing, and subject to the terms and conditions set forth herein, Seller will sell, assign, transfer, convey and deliver, or cause one or more of its Subsidiaries to sell, assign, transfer, convey and deliver, free and clear of Liens (other than Permitted Liens) to Purchaser, and Purchaser will purchase, acquire and accept from Seller or its applicable Subsidiaries, all right, title, interest and obligations of Seller or its applicable Subsidiaries in and to the following (collectively, the " Purchased Assets "):

(1) the real property listed on Schedule 2.1(a)(1) and related improvements and fixtures, together with all assignable real property rights, benefits and appurtenances thereto (the " Purchased Real Property ");

(2) subject to the receipt of any required third-party consents, the real property leases listed on Schedule 2.1(a)(2) (the " Real Property Leases ");

(3) the furniture, equipment, materials and supplies owned by Seller and its Subsidiaries as of the Closing Date and located at the Banking Center Premises, but excluding all proprietary systems or proprietary materials located in the Banking Center Premises (collectively, the " Purchased Personal Property ");

(4) subject to the receipt of any required third-party consents, the leases, subleases, licenses or other contracts associated with the furniture, equipment, materials and supplies leased by Seller and its Subsidiaries as of the Closing Date and located at the Banking Center Premises, all as identified on Schedule 2.1(a)(4) (collectively, the " Personal Property Leases ");

(5)(i) the ATM units and the real property on which such ATMs are located that are owned by Seller or any of its Subsidiaries at the Banking Centers, a list of which, as of the date hereof, is set forth on Schedule 2.1(a)(5)(i) (the " Purchased ATMs "), and (ii) subject to the receipt of any required third-party consents, all of Seller's or Seller's Subsidiaries' rights with respect to the leases pursuant to which Seller or any of its Subsidiaries leases real property on which ATMs are located at the Banking Centers, a list of which leases, as of the date hereof, is set forth on Schedule 2.1(a)(5)(ii) (the " ATM Real Property Leases ");

(6) the Loans (including servicing rights relating thereto of Seller or any of its Subsidiaries) made or purchased by Seller or any of its Subsidiaries and booked at the Banking Centers that are listed on Schedule 2.1(a)(6) , together with all Contracts evidencing or executed and delivered in connection with such Loans and including all obligations to make additional extensions of credit thereunder and all related collateral, excluding Nonperforming Loans (collectively, the " Purchased Loans ").

The parties agree that no Nonperforming Loans shall be included in the Purchased Loans;

(7) all safe deposit Contracts and leases for safe deposit boxes located at the Banking Centers (the " Safe Deposit Agreements ");

(8) the CRA-eligible loans, other than any Nonperforming Loans, listed on Schedule 2.1(a)(8) (the " CRA Assets ");

(9) subject to the receipt of any required third-party consents the Letters of Credit issued in favor of a Banking Center Customer by Seller or any of its Subsidiaries that are listed on Schedule 2.1(a)(9) together with all reimbursement agreements and related documents (including, but not limited to, any collateral documents) with respect to the Assumed Letters of Credit and all collateral in the possession of or otherwise granted to Seller or any of its Subsidiaries in connection therewith (collectively, the " Assumed Letters of Credit ").

(10) subject to the receipt of any required third-party consents, the rights of Seller or its Subsidiaries with respect to the operating Contracts under which goods or services are provided exclusively to or at the Banking Centers, all as identified on Schedule 2.1 (a)(10) (the " Assumed Contracts ," and together with the Real Property Leases, ATM Real Property Leases, Assumed Letters of Credit and Personal Property Leases, the " Assumed Agreements ");

(11) all books, records and other data primarily relating to the Banking Centers, including all files (including suspicious activity reports to the extent permitted by Applicable Law), customer and supplier lists, mailing lists, accounting records, documentation or records primarily relating to the administration of the Assumed Agreements and the Assumed Deposits, real property files with respect to Purchased Real Property and Real Property Leases (including lease documentation, maintenance records, plans and permits, to the extent in the possession of Seller or any of its Subsidiaries), personnel files and records for any Transferred Banking Center Employees (to the extent permitted under Applicable Law and as reasonably agreed upon by Purchaser and Seller), technical and other data primarily relating to the Banking Centers other than (i) Forms W-8 and W-9 and similar tax forms provided to Seller or any of its Subsidiaries by customers of the Banking Centers, income tax records of Seller or any of its Subsidiaries, (ii) personnel files and records for any Retained Employees and (iii) books and records to the extent relating to accounts that have terminated prior to Closing; provided , however , that Seller and its Subsidiaries shall have the right to retain copies of all such books, records and other data that are part of the Purchased Assets to the extent reasonably necessary for, and solely for use in connection with, tax, regulatory, litigation or other legitimate, non-competitive purposes;

(12) all U.S. cash on hand at the Banking Centers at the Close of Business on the Closing Date, including vault cash, petty cash, tellers' cash, prepaid postage, bank orders, checks, certified checks and cash equivalents (exclusive of the contents of any

safe deposit boxes) located at the Banking Centers, as determined by a cash count to be mutually conducted by Seller and Purchaser and excluding any cash contained in ATMs not physically located at the Banking Centers and cash contained in security vehicles or otherwise maintained in vaults by vendors on behalf of Seller or Seller's Subsidiaries, whether or not associated with the Banking Centers (the " Cash on Hand "); and

(13) the Purchased Overdrafts.

(b) *Excluded Assets* . Notwithstanding anything to the contrary contained in Section 2.1(a) , Purchaser will not purchase, assume or otherwise acquire, and Seller and its Affiliates will retain all the rights, title and interest in and to, any and all assets of Seller and its Affiliates that are not included in the Purchased Assets (collectively, the " Excluded Assets "), including, by way of example only, the following assets, properties, rights, Contracts and claims, wherever located, whether tangible or intangible, real, personal or mixed:

(1) all assets, properties, rights, Contracts and claims, including Loans and extensions of credit in process, wherever located, whether tangible or intangible, real, personal or mixed, primarily related to the Banking Centers;

(2) other than the Real Property Leases and ATM Real Property Leases, all leases, subleases, licenses or other Contracts pursuant to which Seller or any of its Affiliates leases, subleases or licenses real property;

(3) all Nonperforming Loans and Loans to Retained Employees;

(4) the Excluded Contracts;

(5) all assets related to employee benefit arrangements of Seller or any of its Affiliates, including the Employee Plans;

(6) all Intellectual Property of Seller and its Affiliates, including all right, title and interest in and to all proprietary or licensed software, systems or programs or computer software agreements of Seller and its Affiliates, including any rights (ownership, licensed or otherwise) to any of the Seller Names and any other Trademarks or logos of Seller or its Affiliates, including those identified on Schedule 2.1(b)(6) ;

(7) all books, records and other data that cannot, without unreasonable effort or expense, be separated from books and records maintained by Seller or its Affiliates in connection with the retained businesses or to the extent that such books, records and other data relate to Excluded Assets, Excluded Liabilities or Banking Center Employees who do not become Transferred Banking Center Employees, and all personnel files and records; provided that, to the extent permitted under, and in accordance with, Section 7.1(b) , Seller shall provide Purchaser with access to any such books, records and other data for which the above-referenced separation would cause Seller to incur unreasonable effort or expense;

(8) all licenses, charters, and legal entities of Seller or its Affiliates; and

(9) the assets listed on and operations described on Schedule 2.1(b)(9) (collectively, the " Additional Excluded Assets "); and

(10) the Credit Card Accounts and Receivables.

(c) Purchaser understands and agrees that it is purchasing only the Purchased Assets (and assuming only the Assumed Liabilities) specified in this Agreement and, except as may be expressly provided for in this Agreement, Purchaser has no interest in any other Relationship which Seller or any of its Affiliates has or may have with any Banking Center Customer or any other customer of Seller or any of its Affiliates. Purchaser further understands and agrees that Seller and its Affiliates are retaining any and all rights and claims which any of them may have, including, but not limited to, indemnification or reimbursement rights, with respect to the Purchased Assets and the Assumed Liabilities, to the extent that such rights or claims relate to the conduct of the Banking Centers prior to the Closing Date, unless such rights or claims relate to liabilities, duties, responsibilities and obligations of Seller or any of its Affiliates arising or accruing on or prior to the Closing Date which are included in the Assumed Liabilities. Purchaser and Seller further acknowledge and agree that Seller is not transferring to Purchaser and Purchaser will not acquire any of Seller's or Seller's Affiliates' current or future Relationships (wherever conducted) associated with any of (i) their "commercial real estate" line of business; (ii) their "corporate lending" line of business; (iii) their "commercial leasing" line of business; (iv) their "municipal" line of business; or (v) their private client services line of business, in all of their respective phases (collectively, the " Excluded Business Activities "), and, notwithstanding anything to the contrary in Section 7.9 , neither Seller nor any of its Affiliates shall be restricted from engaging in the Excluded Business Activities, including within the markets where the Banking Centers are located. For clarity, Seller differentiates between the above-referenced "corporate lending" line of business and its "business banking" line of business (sometimes referred to as "small business" lending). Seller's corporate lending line of business consists of loans to businesses with annual revenues at or above $15 million or aggregate loan exposures (including commitments under lines of credit and under letters of credit) to Seller and its Affiliates, determined on a consolidated basis, of $5.0 million or more whereas the business banking line of business concentrates on loans to businesses that do not fall within either of the above parameters. The "business banking" line of business is not part of the Excluded Business Activities.

(d) Purchaser and Seller acknowledge and agree that the Purchased Assets include the wealth management business conducted, as part of retail operations, at the Banking Centers (i.e., the business of providing financial planning, insurance, investment advisory and similar services through financial advisors or licensed bankers located in the Banking Centers).

Section 2.2 Assumption of Liabilities . (a) *Assumed Liabilities.* From and after the Closing, Purchaser will assume, and will pay, perform and discharge as they become due, all of the following liabilities and obligations of Seller solely to the extent such liabilities and obligations are required to be satisfied, paid or performed after the Closing Date (collectively, the " Assumed Liabilities "):

(1) the Assumed Deposits;

(2) the Assumed Agreements, except (i) for any liability or obligation under such Assumed Agreements (x) to be performed prior to the Closing Date or (y) arising from a breach of, or default under, any such Assumed Agreements by Seller or its Affiliates and (ii) for any liability or obligation listed on Schedule 2.2(a)(2) ;

(3) all liabilities and obligations, including all compensation, benefits, severance, workers' compensation and welfare benefit claims and employment-related liabilities, accruing after the Closing Date that relate to or arise from the employment of the Transferred Banking Center Employees by Purchaser after the Closing Date, but excluding any Liabilities with respect to the Employee Plans;

(4) any Accrued Interest and Fees on the Assumed Deposits; and

(5) any Liability, duty or obligation of any nature whatsoever, whether accrued, absolute, primary or secondary, contingent or otherwise, direct or indirect, asserted or unasserted, known or unknown that arises based on the conduct of the Banking Centers after the Closing Date or the use of the Purchased Assets after the Closing Date or the Assumed Liabilities, of whatever kind or nature, primary or secondary, direct or indirect.

Purchaser's obligations under this Section 2.2(a) shall not be subject to offset or reduction by reason of any actual or alleged breach of any representation, warranty or covenant contained in this Agreement or any document delivered in connection herewith or any right or alleged right to indemnification hereunder or thereunder. All periodic fees or charges shall be shared on a proportionate basis as of the Closing Date in accordance with Section 3.3(b) .

(b) *Excluded Liabilities* . Notwithstanding anything to the contrary set forth in Section 2.2(a), other than the Assumed Liabilities, neither Purchaser nor any of its Subsidiaries will assume or be bound by any Liability, duty or obligation of any of Seller or any of its Affiliates, and Seller and its Affiliates shall retain all Liabilities, duties and obligations (including Controlled Group Liability) other than the Assumed Liabilities (collectively, the " Excluded Liabilities ").

Section 2.3 Sale and Transfer of Servicing . Purchased Loans shall be sold on a servicing-released basis (and without limitation, any related escrow deposits shall be transferred to Purchaser). As of the Closing Date, all rights, obligations, liabilities and responsibilities with respect to the servicing of the Purchased Loans after the Closing Date will be assumed by Purchaser.

## ARTICLE III

## CLOSING PAYMENT AND ADJUSTMENTS

Section 3.1 Closing Payment . (a) On the Closing Date, Purchaser shall acquire the Purchased Assets and shall assume the Assumed Liabilities.

(b) Pursuant to Section 3.2(b) , on the Closing Date, Seller shall pay, or cause to be paid, to Purchaser (or, in the event that the payment calculated pursuant hereto is a negative number, Purchaser shall pay to Seller (for the credit of Seller) the absolute value of such figure) by electronic wire transfer in an amount in U.S. dollars (the " Closing Payment ") equal to:

(1) an amount, as set forth on the Closing Statement (as defined in Section 3.2(a) ), equal to the sum of (i) the aggregate balance of the Assumed Deposits, plus Accrued Interest and Fees thereon, and (ii) the Net Book Value of the other Assumed Liabilities, MINUS

(2) an amount (the " Aggregate Asset Amount ") equal to the sum of the following, as set forth on the Closing Statement (as defined in Section 3.2(a) ):

(i) an amount equal to four percent (4.0%) of the average daily balance (including Accrued Interest and Fees) of the Assumed Deposits for the calendar month immediately preceding the month in which the Closing occurs and this amount shall be subject to adjustment (and adjusted) as indicated in Section 3.2 (the " Premium "); PLUS

(ii) the aggregate face amount of Cash on Hand as of the Close of Business on the Closing Date; PLUS

(iii) the aggregate Appraised Value of the Purchased Real Property; PLUS

(iv) the sum of (x) the unpaid principal balance of the Purchased Loans and Purchased Overdrafts, as of the Close of Business on the Closing Date, in each case, plus Accrued Interest thereon, and (y) the aggregate Net Book Values, as of the Close of Business on the Closing Date, of each of the following: the Purchased Personal Property; the Purchased ATMs; and the Assumed Letters of Credit.

Section 3.2 Closing Statement and Closing Payment . (a) *Closing Statement* . For the Closing, Seller shall prepare a statement substantially in the form of Exhibit 3.2 (a " Closing Statement ") showing the Aggregate Asset Amount and the calculation thereof, reflecting the Purchased Assets and Assumed Liabilities, as of the Update Date (the " Closing Statement Date ").

(b) *Closing Payment.* At the Closing, Seller agrees to pay to Purchaser (or, if applicable, Purchaser agrees to pay to Seller for the account of Seller) the Closing Payment, calculated pursuant to Section 3.1(b) , reflected on the Closing Statement. The amount paid at the Closing shall be subject to subsequent adjustment based on the Final Closing Statement, prepared pursuant to Section 3.3 . The amount so paid on the Closing Date, including on account of the Premium, shall be subject to adjustment based on the Final Closing Statement with the Premium computed based on the month-to-date average daily balance (including Accrued Interest and Fees) of the Assumed Deposits for the calendar month in which the Closing occurs up to and including the Closing Date.

Section 3.3 Final Closing Statement, Allocation of Fees and Expenses, and Post-Closing Adjustment . (a) *Final Closing Statement.* Not later than thirty (30) Business Days after the Closing Date, Seller shall deliver to Purchaser a statement, as of the Close of Business on the Closing Date, and prepared in accordance with GAAP applied consistently with the practices used in the preparation of the Closing Statement except as and to the extent that this Agreement provides for different valuation methodologies for particular categories of Purchased Assets and Assumed Liabilities, showing the Aggregate Asset Amount and the calculation thereof, reflecting the Purchased Assets and Assumed Liabilities, as of the Close of Business on the Closing Date (as reflected on the Final Schedules), and reflecting such other adjustments as are appropriate in accordance with Section 3.3(b) (the " Final Closing Statement "). Seller shall afford Purchaser and its accountants and attorneys the opportunity to review all work papers and documentation used by Seller in preparing the Final Closing Statement.

(b) *Allocation of Fees and Expenses.* Except as otherwise provided herein, to effect the intention of the parties that the economics of the Banking Centers shall be for the account of Seller up to the Close of Business on the Closing Date and thereafter shall be for the account of Purchaser, all fees and expenses with respect to the Banking Centers that related to both the period before and the period after the Closing Date, shall be prorated between Purchaser, on the one hand, and Seller, on the other hand, based on the full amount of the latest available bills or statements on the basis of a three hundred sixty-five (365)-day calendar year (except to the extent accrued on a three hundred sixty (360)-day calendar year, in which case proration shall be based on a three hundred sixty (360)-day calendar year) as of the Close of Business on the Closing Date. In furtherance of the foregoing, all operating expenses related to the Banking Centers, as the case may be, including, but not limited to, rent, utility, maintenance, and service expenses attributable to operations of the Banking Centers until the Close of Business on the Closing Date shall be paid by and shall be the obligation of Seller. All of such expenses attributable to operations of the Banking Centers after the Close of Business on the Closing Date shall be paid by and be the obligation of Purchaser. All real and personal property, use and other Taxes imposed on a time basis with respect to the Banking Centers shall be prorated between Purchaser, on the one hand, and Seller, on the other hand, in the same manner based on the full amount of the Tax for the relevant period, unless such amount is not reasonably ascertainable, in which case the full amount of the Tax for the prior period shall be used. Any rental income from subtenants or other third-party occupants of real property shall also be prorated between Purchaser, on the one hand, and Seller, on the other hand, as of the Close of Business on the Closing Date. To the extent that any Tax, fees or expenses described in this Section 3.3(b) are not discovered or the actual amount thereof is not known prior to the final determination of the Final Closing Statement, the parties shall cooperate with one another so that Seller and Purchaser each pays its appropriate share of any such fee or expense, depending upon whether such fee or expense relates to the period before or after the Close of Business on the Closing Date.

(c) Except as otherwise expressly provided herein, the determination of the Final Closing Statement shall be final and binding on the parties hereto, unless, within thirty (30) days after receipt by Purchaser of the Final Closing Statement, Purchaser shall notify Seller in writing of its disagreement with any amount included therein or omitted therefrom (a " Purchaser Objection "), in which case, if the parties are unable to resolve the disputed items within ten (10) Business Days of the receipt by Seller of notice of such disagreement, such items shall be

determined by a nationally recognized independent accounting firm selected by mutual agreement between Seller and Purchaser; provided , however , that in the event the fees of such firm as estimated by such firm would exceed fifty percent (50%) of the net amount in dispute, the parties agree that such firm will not be engaged by either party and that such net amount in dispute will be equally apportioned between Seller and Purchaser. Such accounting firm shall be instructed to resolve the disputed items within ten (10) Business Days of engagement, to the extent reasonably practicable. The determination of such accounting firm shall be final and binding on the parties hereto. The fees of any such accounting firm shall be divided equally between Seller and Purchaser.

(d) Not later than the Close of Business on the second (2 nd ) Business Day following the final determination of the Final Closing Statement, pursuant to Section 3.3(c) (the " Adjustment Payment Date "), Seller and Purchaser shall effect the transfer of any funds as may be necessary to reflect changes in the Purchased Assets and Assumed Liabilities between the Closing Statement and the Final Closing Statement and resulting changes in the Closing Payment and/or Premium, together with interest thereon computed from the Closing Date up to, but not including, the Adjustment Payment Date, at the Federal Funds Rate; provided , however , that if a Purchaser Objection is timely made, within two (2) Business Days of the date of such Purchaser Objection, Seller and Purchaser shall effect the transfer of any funds as may be necessary to reflect the undisputed portion of the changes in the Purchased Assets and Assumed Liabilities between the Closing Statement and the Final Closing Statement and resulting adjustments to the Closing Payment and/or Premium, together with interest thereon computed from the Closing Date up to, but not including, the date of such payment at the Federal Funds Rate.

Section 3.4 Allocation of Consideration . (a) Within sixty (60) days after the Adjustment Payment Date, (i) Seller shall prepare and deliver to Purchaser a draft of a statement (an " Allocation Statement ") setting forth its proposed calculation of the aggregate amount of consideration paid by Purchaser, in respect of the Purchased Assets conveyed at the Closing, and the proposed allocation in the form required in Section 1060 of the Code of such aggregate amount among the Purchased Assets. If within thirty (30) days after Purchaser's receipt of the draft Allocation Statement, Purchaser shall not have objected in writing to such draft statement, then such draft statement shall become the Allocation Statement. In the event that Purchaser objects in writing within such thirty- (30) day period, Seller and Purchaser shall negotiate in good faith to resolve the dispute.

(b) The parties hereto agree to report the allocation of the total consideration among the Purchased Assets in a manner consistent with the Allocation Statement, and agree to act consistently in the preparation and filing of all Tax Returns (including filing Form 8594 with their respective federal income Tax Returns for the taxable year that includes the Closing Date and any other forms or statements required by the Code, Treasury regulations, the Internal Revenue Service or any applicable state or local Taxing Authority) and in the course of any Tax audit, Tax review or Tax litigation relating thereto; provided that neither Seller nor any of its Affiliates nor Purchaser or any of its Affiliates will be obligated to litigate any challenge to such allocation of the aggregate consideration by a Taxing Authority.

## ARTICLE IV

## THE CLOSING

Section 4.1 Closing Time and Place . The consummation of the transfer of the Purchased Assets and the Assumed Liabilities, and the payment of the Closing Payment, in each case as contemplated by this Agreement, shall take place at a closing (the " Closing "), to be held at 10:00 a.m., New York time, at the offices of Seller in Buffalo, New York, on (i) the last day of a month that is not earlier than the later of January 31, 2012 or the second Business Day following the satisfaction or waiver of all conditions set forth in Article XI (excluding any such conditions that by their nature are to be satisfied at the Closing, but subject to the satisfaction or waiver of such conditions), or (ii) such other date as Purchaser and Seller may agree in writing (in either case, the " Closing Date "). The Closing shall be deemed effective as of 11:59 p.m., New York time, on the Closing Date. If the Closing Date occurs on a day other than a Business Day, any wire transfers that otherwise would have been made on the Closing Date shall be evidenced on the Closing Date through arrangements mutually agreed by the parties, and such wire transfers shall occur on the first Business Day following the Closing Date.

Section 4.2 Closing Documents . (a) *Deliveries of Seller* . At the Closing, Seller shall deliver the following documents to Purchaser, all of which shall be in a form reasonably satisfactory to Purchaser:

(1) the updated Schedules contemplated by Section 7.11 ;

(2) the officers' certificates contemplated by Section 11.3(c) ;

(3) a bargain and sale deed without a covenant against grantor's acts (or its substantive equivalent) for the Purchased Real Property;

(4) a bill of sale, in a form to be agreed upon between Seller and Purchaser after the date of this Agreement, with each acting reasonably and in good faith (the " Bill of Sale "), transferring to Purchaser free and clear of Liens (other than Permitted Liens) all of the right, title and interest of Seller and its Subsidiaries in and to the Purchased Assets;

(5) an Assignment and Assumption Agreement, in a form to be agreed upon between Seller and Purchaser after the date of this Agreement, with each acting reasonably and in good faith, (the " Assignment and Assumption Agreement "), assigning the right, title and interest of Seller and its Subsidiaries in and to the Purchased Assets, free and clear of Liens (other than Permitted Liens) and providing for the assumption of the Assumed Liabilities by Purchaser;

(6) an affidavit pursuant to Section 1445 of the Code certifying to the non-foreign status of each of Seller and each of its Subsidiaries conveying real property located in the United States hereunder;

(7) the Purchased Loans, duly and properly endorsed to Purchaser by Seller, together with all notes, guarantees, agreements and other evidence thereof and all

collateral and security interests securing the Purchased Loans in the possession of Seller or its Subsidiaries and all necessary assignments (if applicable, in recordable form), endorsements and other instruments of conveyance as may be necessary under the circumstances; provided that all such assignments, endorsements and other instruments of conveyance shall be without recourse as to collection to Seller;

(8) subject to the relevant provisions of the License Agreement possession of, or access to, all Credit Documents in whatever form or medium (including imaged documents), all collateral in the custody or possession of Seller or its Subsidiaries, and all funds held in escrow, in each case, relating to the Purchased Loans or the Assumed Letters of Credit; and

(9) all other documents and instruments reasonably necessary to (i) transfer the Purchased Assets to Purchaser, (ii) reflect the assumption of the Assumed Liabilities by Purchaser or (iii) effectuate the other transactions to be taken by Seller contemplated by this Agreement.

(b) *Deliveries of Purchaser*. At the Closing, Purchaser shall deliver the following documents to Seller, all of which shall be in form reasonably satisfactory to Seller:

(1) the officer's certificate contemplated by Section 11.2(c) ;

(2) the duly executed Assignment and Assumption Agreement;

(3) the executed Bill of Sale; and

(4) all other documents and instruments reasonably necessary to (i) receive the Purchased Assets from Seller or any of its Subsidiaries, (ii) assume the Assumed Liabilities from Seller or any of its Subsidiaries or (iii) effectuate the other transactions to be taken by Purchaser contemplated by this Agreement.

Section 4.3 Delivery of Purchased Assets . Seller shall deliver to Purchaser at the Close of Business on a Closing Date (or at such other date if mutually agreed to by Purchaser and Seller) all of the fixed assets and other tangible personal property to the extent not located on or at the Banking Center Premises (including real property files, Cash on Hand, and keys to safe deposit boxes) constituting Purchased Assets.

## ARTICLE V

## REPRESENTATIONS AND WARRANTIES OF SELLER

Except as Previously Disclosed, Seller represents and warrants to Purchaser, as of the date hereof (or as of such other date as may be expressly provided in any representation or warranty), as follows:

Section 5.1 Organization . Seller is a national banking association duly organized, validly existing and in good standing under the laws of the United States. Seller has all requisite corporate power and authority to own the Purchased Assets and carry on its business

at the Banking Centers as currently conducted by it and is duly qualified to do business as a foreign corporation or other entity in each jurisdiction where its ownership of the Purchased Assets and its conduct of business at the Banking Centers as currently conducted by it requires such qualification, except where the failure to be so qualified or be in good standing in such other jurisdiction would not, individually or in the aggregate, have a Material Adverse Effect. Seller will have a net worth following the Closing Date that is sufficient to enable it to fulfill its obligations under this Agreement.

Section 5.2 Authority; Capacity . Seller has the power and authority to enter into and perform this Agreement and any other documents executed pursuant hereto. This Agreement and any other documents or instruments executed pursuant hereto and the execution, delivery and performance hereof and thereof have been duly authorized and approved by all necessary corporate action on the part of Seller, and this Agreement and the instruments and documents executed pursuant hereto constitute, or when executed will constitute, the valid and binding obligations of Seller, enforceable against it in accordance with their terms, except as enforcement may be limited by receivership, conservatorship and supervisory powers of bank regulatory agencies generally as well as by bankruptcy, insolvency, reorganization, moratorium or other laws of general applicability relating to or affecting creditors' rights, or the limiting effect of rules of law governing specific performance, equitable relief and other equitable remedies or the waiver of rights or remedies.

Section 5.3 Consents and Approvals . None of Seller or any of its Subsidiaries is required to obtain any order, permit, consent, approval or authorization of, or required to make any declaration or filing with, any Governmental Entity or third party in connection with the execution and delivery of this Agreement and the transactions contemplated hereby, except (i) as may be required pursuant to the Contracts listed on Schedule 5.3(i) , (ii) compliance with the applicable requirements of the HSR Act and the approvals or non-objections of the Governmental Entity listed on Schedule 5.3(ii) (the " Seller Regulatory Approvals ") (such approvals contemplated by the foregoing clauses (i) and (ii) being hereafter referred to as the " Seller Approvals ") and (iii) other consents or approvals, the failure of which to obtain would not reasonably be expected to, individually or in the aggregate, have a Material Adverse Effect.

Section 5.4 No Breaches; Defaults . Assuming receipt of the approvals referenced in Section 5.3 , the execution and delivery of this Agreement and the instruments and documents executed pursuant hereto by Seller do not, and the consummation of the transactions contemplated by this Agreement will not (i) result in a breach, violation of or default under any law, rule, regulation, judgment, order, governmental permit or license of to which Seller or its Subsidiaries is a party or by which it is bound, except such breaches, violations or defaults that would not, individually or in the aggregate, have a Material Adverse Effect or (ii) constitute a breach or violation of or a default under the articles of association, certificate of incorporation or bylaws of Seller.

Section 5.5 Compliance with Law . Except as disclosed on Schedule 5.5 , each of Seller and its Subsidiaries: (i) is in compliance in all material respects with Applicable Law applicable to the Banking Centers, Purchased Assets and Assumed Liabilities; (ii) has conducted and is conducting business at the Banking Centers (including, without limitation, all matters relating to the Banking Center Employees and the Banking Center Premises) in compliance in all

material respects with Applicable Law including, without limitation, all regulations, orders, and opinions of the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation; and (iii) has properly administered in all material respects all accounts at the Banking Centers for which it acts as a fiduciary, including accounts for which it serves as a trustee, agent, custodian, personal representative, guardian, conservator or investment advisor, in accordance with the terms of the agreements governing such accounts and Applicable Law, provided that the environmental matters addressed by Section 5.19 shall be governed exclusively by Section 5.19 and not this Section 5.5 and compliance with law matters specifically addressed elsewhere in this Article V shall be governed by such specific representations and not this Section 5.5 . Except as would not, individually or in the aggregate, result in a material adverse effect, neither Seller nor any of its Subsidiaries is subject to any order or ruling directed to it by, or memorandum of understanding with, any Governmental Entity. Seller received a rating of satisfactory or higher in its most recent examination with respect to the CRA and has no reason to believe that it will not maintain at least a satisfactory rating following its next CRA examination.

Section 5.6 Litigation and Related Matters . Except as disclosed on Schedule 5.6 , there are no actions, suits, or proceedings, whether civil, criminal or administrative, pending as of the date of this Agreement or, to the Knowledge of Seller, threatened as of the date of the Agreement which would reasonably be expected to, individually or in the aggregate, materially adversely affect (i) the Purchased Assets or Assumed Liabilities, (ii) business at the Banking Centers (including, without limitation, all matters relating to the Banking Center Employees and the Banking Center Premises), or (iii) accounts at the Banking Centers for which it acts as a fiduciary, including accounts for which it serves as a trustee, agent, custodian, personal representative, guardian, conservator or investment advisor. Except as disclosed on Schedule 5.6 , there are no actions, suits, or proceedings, whether civil, criminal or administrative, pending as of the date of this Agreement or, to the Knowledge of Seller, threatened as of the date of the Agreement against or affecting Seller which would (i) reasonably be expected to, individually or in the aggregate, have a Material Adverse Effect or (ii) prevent or materially delay Seller from being able to perform the material obligations of Seller under this Agreement.

Section 5.7 No Brokers or Finders . Except for Goldman, Sachs & Co. and Sandler O'Neill & Partners, L.P., whose fees will be paid by Seller or an Affiliate of Seller, there is no investment banker, broker, finder or other intermediary that has been retained by or is authorized to act on behalf of Seller or any of its Affiliates who might be entitled to any fee or commission from Seller or its Affiliates in connection with the transactions contemplated hereby.

Section 5.8 Operations . Since March 31, 2011, and except as otherwise expressly contemplated by this Agreement, Seller and its Subsidiaries have in all material respects operated the Banking Centers only in, and have not engaged in any material transaction other than in, the ordinary course of business consistent with past practice. Since March 31, 2011, there has not been any event, occurrence or circumstance that has had or that would reasonably be expected to have, individually or in the aggregate, a Material Adverse Effect.

Section 5.9 Real Property Leases . (a) Seller has provided Purchaser with true and correct copies of all Real Property Leases and a list of all of the tenants or other occupants of the Banking Center Premises subject to a Real Property Lease as of the date set forth on such list.

(b) Each Real Property Lease is in full force and effect in all material respects, and, neither Seller nor, to Seller's Knowledge, the landlord is in default under any of its respective obligations thereunder.

(c) Except as would not, individually or in the aggregate, reasonably be expected to have a Material Adverse Effect, neither Seller nor any of its Subsidiaries has received any written notice of a condemnation proceeding relating to any real property that is subject to a Real Property Lease that would materially affect a property or its intended use.

Section 5.10 Purchased Real Property . (a) Seller and its applicable Subsidiaries have good and marketable title to the Purchased Real Property, free and clear of all Liens, except for Permitted Liens. On the Closing Date, Seller and its applicable Subsidiaries will convey good and marketable title to the Purchased Real Property free and clear of all Liens, except for Permitted Liens.

(b) Except as disclosed on Schedule 5.10 , to the Knowledge of Seller, neither Seller nor any of its Subsidiaries has received any written notice of a condemnation proceeding relating to the Purchased Real Property.

(c) There are no outstanding agreements, options, rights of first refusal or commitments of any nature obligating Seller or any of its Subsidiaries to transfer any of the Purchased Real Property or rights or interests therein to any other Person.

Section 5.11 Assumed Deposits . Seller has the right to transfer or assign each of the Assumed Deposits to Purchaser. The Assumed Deposits have been solicited, originated and administered in accordance with the terms of the respective governing documents and all Applicable Law and regulations, in each case, in all material respects. The Assumed Deposits are insured by the FDIC to the fullest extent permitted in accordance with the FDI Act and Seller and its Subsidiaries have paid all assessments due thereunder. Each of the agreements relating to the Assumed Deposits is valid, binding, and enforceable upon its respective parties in accordance with its terms except as enforceability may be limited by bankruptcy, insolvency, reorganization, moratorium, or other similar laws affecting creditors' rights, and by the exercise of judicial discretion in accordance with general principles applicable to equitable and similar remedies.

Section 5.12 Purchased Loans (a) Each Purchased Loan (i) is evidenced by notes, agreements, or other evidences of indebtedness that are true, genuine and what they purport to be, materially complete and correct sets of originals of which (or, to the extent an original is not necessary for the enforcement thereof, true, correct and complete copies thereof) are included in the Credit Documents which will be delivered, or made available, to Purchaser pursuant to Section 2.1(a) ; (ii) constitutes a legal, valid and binding obligation of the respective borrower(s) or obligor(s), enforceable, to the Knowledge of Seller, by the holder thereof in accordance with its terms subject, as to enforcement, to applicable bankruptcy, insolvency, reorganization, liquidation and other similar laws and equitable principles relating to or affecting

the enforcement of creditors' rights generally, (iii) is free from all material claims, defenses, rights of rescission, any discount, allowance, set-off, counterclaim, presently pending bankruptcy or other defenses by the borrower, and (iv) complies in all material respects with Applicable Law, including all applicable lending laws and regulations.

(b) Each Purchased Loan (i) was originated by Seller or a Subsidiary of Seller (or, in the case of a Purchased Loan that was purchased by Seller or a Subsidiary of Seller, by the Person making such Purchased Loan): (x) in the ordinary course of business at the time such Purchased Loan was made; and (y) in accordance with Applicable Law, in all material respects; and (ii) to the extent it is identified as secured in Schedule 2.1(a)(6) , is secured by a valid, perfected and enforceable Lien on the secured property described in the applicable security agreement.

(c) Each Purchased Loan has been originated, created, maintained, serviced and administered in all material respects in accordance with (i) Applicable Law; (ii) Seller's or its applicable Subsidiaries' written loan servicing and operating procedures as in effect from time to time; and (iii) the respective loan document governing each Purchased Loan.

(d) Immediately following the sale of each Purchased Loan, Purchaser will own such Purchased Loan free and clear of any encumbrance, equity, participation interest, Lien, pledge, charge, claim or security interest.

(e) To Seller's Knowledge, neither the borrower nor any guarantor of any of the Purchased Loans is in bankruptcy and, there are no facts, circumstances or conditions with respect to any such Purchased Loans, the collateral therefor or the borrower's credit standing, that could reasonably be expected to cause any such Purchased Loans to become delinquent or adversely affect the collectability, the value or the marketability of such Purchased Loans.

(f) None of the rights or remedies under the documentation relating to the Purchased Loans has been amended, modified, waived, subordinated or otherwise altered by Seller or any of its Subsidiaries, except as evidenced by a written instrument which is a part of the file with respect to the Purchased Loan and appropriately recorded as necessary to establish all rights of mortgagee into assignee.

(g) Seller may transfer or assign the Purchased Loans to Purchaser without the approval or consent of any obligor thereunder and without creating any breach of any agreement pursuant to which another party has purchased a participating interest in the Purchased Loan.

(h) Subject to obtaining any required consent from any third party, including the SBA, with respect to each SBA Loan that is subject to a guaranty, such guaranty is in full force and effect and is freely transferrable as an incident to the sale of each SBA Loan.

(i) None of the Purchased Loans are serviced by third parties, and there are no obligations, agreements or understandings that could result in any Purchased Loan becoming subject to any such third party servicing.

(j) Except as set forth in this Section 5.12 , Seller does not make any representation or warranty to Purchaser relating to the Purchased Loans.

Section 5.13 Intentionally Omitted

Section 5.14 Assumed Contracts . To the Knowledge of Seller, each party to any Assumed Contract to which it or any of its Subsidiaries is a party has performed in all material respects its obligations thereunder to the extent that such obligations to perform have accrued, no party is in default under such Assumed Contracts and none of such Assumed Contracts was entered into outside the ordinary course of business of Seller or its Subsidiaries. Each such Assumed Contract constitutes the legal, valid and binding obligation of Seller or its Subsidiaries, and, to the Knowledge of Seller, the respective third party, and is enforceable in accordance with its terms subject as to enforcement, to applicable bankruptcy, insolvency, reorganization, liquidation and other similar laws and equitable principles relating to or affecting the enforcement of creditors' rights generally.

Section 5.15 Regulatory Matters . There are no pending, or to the Knowledge of Seller, threatened disputes or controversies between Seller and any federal, state or local governmental authority that (i) would reasonably be expected to prevent or materially delay Seller from being able to perform their obligations under this Agreement or (ii) would reasonably be expected to impair the validity or consummation of this Agreement or the transactions contemplated hereby. Seller has not received any notice from any Governmental Entity indicating that such Governmental Entity would oppose or not promptly grant or issue its consent or approval, if requested, with respect to the transactions contemplated hereby and has no reason to believe that, if requested, any Governmental Entity required to approve the transactions contemplated hereby would oppose or not promptly grant or issue its consent or approval.

Section 5.16 Necessary Permits . Except as set forth on Schedule 5.16 , Seller and its Subsidiaries have all material permits, licenses, orders, ratings and approvals of all Governmental Entities necessary for them to operate the Banking Centers substantially as presently operated (the " Necessary Permits "), and (i) all of the Necessary Permits are in full force and effect in all material respects, and (ii) to the Knowledge of Seller, no suspension or cancellation of any Necessary Permit has been threatened.

Section 5.17 Banking Center Employees and Benefits . (a) Schedule 1.1(c)(i) lists, as of January 13, 2012, all Banking Center Employees who are identified as employed at the Banking Centers by the internal records of Seller, as well as the position, corporate and functional title, status as exempt or non-exempt, identification number, hire date, status as full or part-time, status as active or on leave, if on leave, the date leave commenced, geographic location and remuneration (including base salary, base wage, commission schedule and prior year's incentive award, in each case, as applicable) of each such Banking Center Employee. Within five (5) Business Days prior to the Closing Date, and at such other dates as reasonably requested by the Purchaser, but no more frequently than once every thirty (30) days, Seller shall update Schedule 1.1(c)(i) in electronic format, to reflect any newly hired Banking Center Employees, those Banking Center Employees whose employment has terminated, and any other change in the other information on Schedule 1.1(c)(i) ; provided , however , that no updated information shall be provided with respect to those Banking Center Employees previously listed on Schedule 1.1(c)(i) who have rejected a Comparable Job Offer or who have not received a Comparable Job Offer from Purchaser as of such date.

(b) Schedule 5.17(b) lists all of the employee benefit and compensation plans, programs, agreements and arrangements, including all pension, retirement, retainer, retiree medical, profit-sharing, thrift, savings, deferred compensation, bonus, compensation, consulting, retention, indemnification, incentive, equity-based, change in control, severance, welfare, fringe benefit, perquisite and similar plans sponsored, maintained or contributed to by Seller or any of its ERISA Affiliates and in which any Banking Center Employee is eligible to participate (the " Employee Plans "). Except as set forth on Schedule 5.17(b) , no Employee Plan is subject to Title IV of ERISA or Section 412 of the Code or provides for medical or health benefits on a self-insured basis, or provides for or continues medical or health benefits, or life insurance or other benefits (through insurance or otherwise) for any Person or any dependent or beneficiary of any Person after such Person's retirement or other termination of employment except as may be required by COBRA or applicable state law. No Employee Plan is a "multiemployer plan," as defined in Section 3(37) of ERISA, and there has been no communication to any Person that could reasonably be expected to promise or guarantee any such benefits. Each Employee Plan has been maintained, funded and administered in accordance with its terms and any applicable collective bargaining agreement, and each Employee Plan, Seller and each ERISA Affiliate, is in compliance with the applicable provisions of ERISA, the Code and all laws applicable thereto. Seller has made available to Purchaser copies of the plan documents, Annual Returns (Form 5500), most recent summary plan descriptions and annual enrollment guides with respect to the Employee Plans.

(c) Each Banking Center Employee who is required by Applicable Law to be licensed to sell non-deposit investment products, including insurance and securities, is validly licensed and in good standing with each applicable regulator, including FINRA and the state insurance regulators.

Section 5.18 Labor Contracts and Relations . Except as set forth on Schedule 5.18 , with respect to Banking Center Employees, none of Seller or any of its Subsidiaries is a party to any collective bargaining agreement, contract, or other agreement or understanding with a labor union or labor organization, and none of Seller or any of its Subsidiaries is the subject of a proceeding asserting it has committed an unfair labor practice or seeking to compel it to bargain with any labor organization as to wages and conditions of employment, nor, to the Knowledge of Seller, is any such proceeding threatened, nor is there any strike or other labor dispute by the Banking Center Employees pending or threatened, nor does Seller have Knowledge of any activity involving any Banking Center Employees seeking to certify a collective bargaining unit or engaging in union organizational activity.

Section 5.19 Environmental Matters. Except as set forth on Schedule 5.19:

(a) Seller and its Subsidiaries are currently in compliance in all material respects with all Environmental Laws applicable to any Banking Center Premises, and with respect to any operations or activities conducted by Seller or any of its Subsidiaries on such Banking Center Premises. Neither Seller nor any of its Subsidiaries has received any written notice that there has been any failure to comply with Environmental Laws applicable to the Banking Center Premises, and with respect to any operations or activities conducted by Seller or any of its Subsidiaries on such premises except any such notice with respect to a failure to comply which has been fully resolved.

(b) Seller and its Subsidiaries have all material environmental permits and approvals required under Environmental Laws for all facilities and improvements and any operations or activities presently conducted by Seller or any of its Subsidiaries at the Banking Center Premises, and, Seller and its Subsidiaries are currently in compliance with all such permits and approvals.

(c) There is no suit, claim, demand, action, consent order, or proceeding pending or, to the Knowledge of Seller, threatened in which Seller or any of its Subsidiaries or, with respect to threatened proceedings, could reasonably be expected to be named as a defendant, responsible party or potentially responsible party for alleged noncompliance with any Environmental Laws or for any other Liabilities under Environmental Laws related to the Purchased Assets.

(d) There have been no Releases into the Environment of any Hazardous Materials in, on, from, under or affecting any Banking Center Premises which have had, or would reasonably be expected to have, an adverse impact on the use or occupancy of such Banking Center Premises and/or which would result in any Liabilities under Environmental Laws.

(e) Seller has provided to Purchaser true and complete copies of all documentation in its possession or under its control pertaining to environmental conditions at the Banking Center Premises.

Section 5.20 Books and Records . With respect to each Assumed Agreement and all accounts related thereto, the accounting, financial and other books and records kept by Seller and its Subsidiaries are in all material respects complete and accurate and have been maintained in the ordinary course of business and in compliance with in all material respects with Applicable Law. The books and records included within the Purchased Assets include all customary branch, customer and customer-related information reasonably necessary to service the Assumed Deposits and Purchased Loans on an ongoing basis, and to otherwise operate the business being acquired under this Agreement in substantially the manner currently operated by Seller.

Section 5.21 Safe Deposit Boxes . Each of Seller and its Subsidiaries is in compliance, in all material respects, with the terms and conditions of the Safe Deposit Agreements.

Section 5.22 Insurance Coverage . The business and operations of the Banking Centers are insured against such risks and in such amounts and with such coverage deemed appropriate by management of Seller and not in a manner materially inconsistent with industry practice for a global financial institution. Since January 1, 2010, all premiums payable under all insurance policies and fidelity bonds that currently cover the assets, business, operations and employees of the Banking Centers have been timely paid in all material respects, and Seller and its Subsidiaries have otherwise complied in all material respects with the terms and conditions of all such policies and bonds. Since January 1, 2010, there is no material claim by Seller or any of its Subsidiaries related to the Banking Centers pending under any such policies or bonds as to which coverage has been denied by the underwriters of such policies or bonds applicable to the

Banking Centers. To the Knowledge of Seller, no insurer has threatened a termination of coverage under any such policies or bonds, except notices required to be given by Applicable Law prior to the expiration of any policy or bond advising that coverage will terminate by its terms if such policy or bond is not renewed.

Section 5.23 Taxes . (a) All Tax Returns required to have been filed with respect to the Purchased Assets (such Tax Returns, the " Tax Returns ") have been filed with the appropriate Taxing Authority; each such Tax Return is true, complete and correct in all material respects. All Taxes shown to be due on such Tax Returns, and all Taxes due and attributable to the Purchased Assets, have been timely paid, withheld and timely paid to the appropriate Taxing Authority, or reflected in an appropriate tax reserve in accordance with GAAP on the financial statements of Seller, other than those Taxes the failure of which to be paid would not result in a Lien on the Purchased Assets or become a liability of Purchaser.

(b) No notice of deficiency or assessment of Taxes has been received from any Taxing Authority with respect to the Purchased Assets. There is no material dispute or claim concerning any Tax relating to the Purchased Assets either (A) claimed or raised by any Taxing Authority in writing or (B) of which Seller has Knowledge. There are no Liens on any of the Purchased Assets that arose in connection with any failure (or alleged failure) to pay any Tax (whether or not such Tax relates to the Purchased Assets).

Section 5.24 Limitations on and Disclaimer of Representations and Warranties and Purchaser's Release in Connection Therewith . Except as otherwise expressly set forth in this Agreement:

(a) Seller makes no representations or warranties, express or implied, as to the physical condition of the Purchased Personal Property.

(b) Except with regard to environmental conditions (as set forth in Section 5.19 ), Seller makes no representations or warranties, express or implied, of any type or nature with respect to the physical condition of the Purchased Real Property which is being sold " AS IS ," " WHERE IS " without recourse and with all faults, without any obligation on the part of Seller.

(c) Except as specifically provided for in this Agreement, Seller disclaims and make no representations or warranties whatsoever with respect to the Banking Centers, Purchased Assets or Assumed Liabilities, express or implied.

Section 5.25 Financing . On the Closing Date, Seller will have sufficient cash, available lines of credit or other sources of immediately available funds to enable it to make the Closing Payment and to promptly pay any other amounts to be paid by it under this Agreement on the Closing Date.

## ARTICLE VI

## REPRESENTATIONS AND WARRANTIES OF PURCHASER

Except as Previously Disclosed, Purchaser hereby represents and warrants to Seller, as of the date hereof (or as of such other date as may be expressly provided in any representation or warranty), as follows:

Section 6.1 Organization . Purchaser is a bank duly organized, validly existing and in good standing under the laws of the State of New York. Purchaser has all the requisite corporate power and corporate authority, as well as all requisite licenses, franchises, permits, qualifications and similar permissions and authorities, to own the Purchased Assets, assume the Assumed Liabilities and to carry on the business at the Banking Centers and is duly qualified to do business in and is in good standing as a foreign corporation or other entity in each jurisdiction where the ownership of the Purchased Assets and the conduct of the Banking Centers requires such qualification, except where the failure to be so qualified or be in good standing would not, individually or in the aggregate, have a material adverse effect on Purchaser.

Section 6.2 Authority; Capacity . Purchaser has the power and authority to enter into and perform this Agreement and any instruments or other documents executed pursuant hereto. This Agreement and any instruments or other documents executed pursuant hereto, and the execution, delivery and performance hereof and thereof have been duly authorized and approved by all necessary corporate action on the part of Purchaser, and this Agreement and the instruments and documents executed pursuant hereto constitutes, or when executed will constitute, the valid and binding obligations of Purchaser, enforceable against Purchaser in accordance with its terms, except as enforcement may be limited by receivership, conservatorship and supervisory powers of bank regulatory agencies generally as well as bankruptcy, insolvency, reorganization, moratorium or other laws of general applicability relating to or affecting creditors' rights, or the limiting effect of rules of law governing specific performance, equitable relief and other equitable remedies or the waiver of rights or remedies.

Section 6.3 Consents and Approvals .

(a) Neither Purchaser nor any of its Affiliates is required to obtain any order, permit, consent, approval or authorization of, nor required to make any material declaration or filing with, any Governmental Entity or third-party in connection with the execution and delivery of this Agreement or the consummation of the transactions contemplated hereby, except compliance with the applicable requirements of the HSR Act and the approvals or non-objections of the Governmental Entities set forth on Schedule 6.3(a) (such approvals, the " Purchaser Regulatory Approvals ").

(b) There are no pending, or to the Knowledge of Purchaser, threatened disputes or controversies between Purchaser or any of its Affiliates and any Governmental Entity, including, without limitation, with respect to capital requirements, that (i) would reasonably be expected to prevent or delay Purchaser from being able to perform its obligations under this Agreement or (ii) would reasonably be expected to impair the validity or consummation of this Agreement or the transactions contemplated hereby. Purchaser has not

received any indication from any Governmental Entity that such Governmental Entity would oppose or refuse to grant or issue its consent or approval, if required, with respect to the transactions contemplated hereby and has no reason to believe that, if requested, any Governmental Entity required to approve the transactions contemplated hereby would oppose or not promptly grant or issue its consent or approval.

(c) As of the date hereof, both currently and after giving effect to the transactions contemplated hereby (on a pro forma basis): (i) Purchaser is and will be at least "well-capitalized", as defined in the FDI Act; and (ii) Purchaser meets all capital requirements, standards and ratios required by each state or federal bank regulator with jurisdiction over Purchaser, including, without limitation, any such higher requirement, standard or ratio as applied to Purchaser by state or federal bank regulator, and no such regulator has indicated that it will condition any of the Purchaser Regulatory Approvals upon an increase in Purchaser's capital or compliance with any capital requirement, standard or ratio.

(d) The deposits of Purchaser and its Subsidiaries are insured by the FDIC to the fullest extent permitted by law, and all premiums and assessments required to be paid in connection therewith have been paid when due by Purchaser.

(e) Purchaser was rated at least satisfactory following its most recent CRA examination by the regulatory agency responsible for its supervision and has no reason to believe that it will not maintain at least a satisfactory rating following its next CRA examination. Purchaser has received no notice of and has no Knowledge of any planned or threatened objection by any community group to the transactions contemplated hereby.

Section 6.4 No Breaches; Defaults . Assuming the receipt of all regulatory approvals referenced in Section 6.3(a) , the execution and delivery of this Agreement and any instruments or other documents executed pursuant hereto by Purchaser do not and the consummation of the transactions contemplated by this Agreement, will not constitute: (i) a breach or violation of or default under any law, rule, regulation, judgment, order, governmental permit or license of Purchaser or to which it is subject, which breach, violation or default would prevent or materially delay Purchaser from being able to perform its obligations under this Agreement in all material respects, or (ii) a breach or violation of or a default under the articles of association (or certificate of incorporation, as applicable) or bylaws of Purchaser.

Section 6.5 Litigation and Related Matters . There are no actions, suits, or proceedings, whether civil, criminal or administrative, pending or, to the Knowledge of Purchaser, threatened against or affecting Purchaser which could materially impede, delay or prevent Purchaser or any of its Subsidiaries from entering into this Agreement or performing its terms.

Section 6.6 Compliance with Laws and Regulations . Except as set forth in Schedule 6.6, each of Purchaser and its Subsidiaries have conducted and are conducting their business in all material respects in compliance with all Applicable Law, including, without limitation, all regulations, orders, and opinions of the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation and the New York Department of Financial Services, and, except as would not, individually or in the aggregate, result in a material adverse effect, neither Purchaser nor any of its Subsidiaries is subject to any order or ruling directed to it by, or memorandum of understanding with, any Governmental Entity.

Section 6.7 No Brokers or Finders . Except for Keefe, Bruyette & Woods, Inc., whose fees will be paid by Purchaser, there is no investment banker, broker, finder or other intermediary that has been retained by or is authorized to act on behalf of Purchaser or any of its Affiliates who might be entitled to any fee or commission from Purchaser or any of its Affiliates in connection with the transactions contemplated hereby.

Section 6.8 Financing . On the Closing Date, Purchaser will have sufficient cash, available lines of credit or other sources of immediately available funds to enable it to make the Closing Payment and to promptly pay any other amounts to be paid by it under this Agreement on the Closing Date.

Section 6.9 Eligibility . As of the date hereof, Purchaser satisfies, and as of the Closing Date will satisfy, all clearing standards and requirements under Applicable Law to (1) acquire and continue the operations of and services provided by the Banking Centers and (2) employ the financial advisors who are Banking Center Employees.

## ARTICLE VII

## GENERAL COVENANTS

Section 7.1 Access to Properties and Records Relating to the Banking Centers . (a) To the extent permitted by Applicable Law, from the date hereof until the earlier of the Closing Date and the termination of this Agreement, Seller will provide to Purchaser and to its officers, accountants, counsel, and other representatives reasonable access during Seller's normal business hours to the properties, books, contracts and records of Seller and its Subsidiaries relating primarily to the Banking Centers for purposes related to the consummation of the transactions contemplated by this Agreement, including for the purposes of conducting Phase I environmental site assessments at the Banking Center Premises (the " Phase I ESAs ") and other environmental investigations at the Banking Center Premises that the parties may agree upon pursuant to Section 8.10; provided , however , that such access shall be at reasonable times and upon reasonable prior notice and shall not disrupt the personnel and operations of Seller and its Subsidiaries; and provided further that Purchaser's access to Tax Returns filed by or otherwise relating to Seller or any of its Subsidiaries shall be governed by Article X . All requests for access to such offices, properties, books, and records shall be made to such representatives of Seller as Seller shall designate, who shall be solely responsible for coordinating all such requests and all access permitted hereunder.

(b) Following the Closing, to the extent permitted by Applicable Law, Purchaser will grant Seller and its representatives reasonable access during Purchaser's normal business hours to all books, records and other data related to the Purchased Assets and to the Transferred Banking Center Employees (including making such persons reasonably available to Seller for depositions, witness preparation, trial preparation and fact-gathering, but excluding any proceedings, or threatened proceedings, between Seller and Purchaser or an Affiliate of Purchaser or of Seller) at reasonable times and upon reasonable prior notice and provided such

access shall not disrupt the personnel and operations of Seller and its Subsidiaries, if such access is reasonably deemed necessary or desirable by Seller or any of its Subsidiaries in connection with its tax, regulatory, litigation, contractual or other legitimate, non-competitive matters, including for purposes of handling claims related to Section 2.2 for which Transferred Banking Center Employees may have relevant information. Nothing in the foregoing shall prevent Seller or any of its Subsidiaries from seeking to make such persons available via subpoena or other legal or similar process.

(c) If Seller does not deliver books, records and other data pursuant to Section 2.1(b)(7) that are otherwise required to be delivered pursuant to Section 2.1(a)(11) , and as otherwise provided for in the Transition Services Agreement, Seller will hold such books, records and other data as custodian for Purchaser. Seller, in its capacity as custodian, will provide to Purchaser access to such books, records and other data in the manner to be provided for in the Transition Services Agreement.

(d) Purchaser will review with Seller Purchaser's information security controls of the system or systems used by Purchaser to maintain the security of customer data, including providing reasonable access to Purchaser's owned facilities and data centers and, to the extent permitted under the relevant contract, to third-party facilities and data centers.

Section 7.2 Efforts; Regulatory Filings and Other Actions . (a) Each of the parties hereto agrees to use its reasonable best efforts to take, or cause to be taken, all actions and to do, or cause to be done, all things necessary, proper or advisable to consummate and make effective as promptly as practicable the transactions contemplated hereby and to cooperate with the other parties in connection with the foregoing. Without limiting the generality of the foregoing, each of the parties shall use its reasonable best efforts to: (i) obtain all Regulatory Approvals as promptly as practicable, (ii) to lift or rescind as promptly as practicable any injunction or restraining order or other order adversely affecting the ability of the parties hereto to consummate the transactions contemplated hereby, (iii) to effect all necessary registrations and filings, if any, and (iv) to fulfill all of the conditions to the obligations of the parties to consummate the transactions contemplated by this Agreement set forth in Article XI .

(b) Notwithstanding anything in this Agreement to the contrary, Purchaser agrees, and shall cause its Subsidiaries, to take all actions, including, but not limited to those relating to a Remedial Action or a Capital Action necessary: (i) to obtain any Purchaser Regulatory Approvals and (ii) to avoid or eliminate each and every impediment to obtaining any Purchaser Regulatory Approvals; in each case of (i) and (ii) to cause the transactions contemplated by this Agreement to occur prior to the Outside Date. For purposes of this Section 7.2(b) , " Remedial Action " shall mean (x) promptly complying with or modifying any request for information by any Governmental Entity; (y) offering, negotiating, committing to and effecting, by agreement, consent decree, hold separate order or otherwise, the sale, divestiture, license or other disposition of any Purchased Assets, Assumed Deposits or Banking Centers or any existing deposits, loans, branches or operations of Purchaser or its Affiliates and any other restrictions on the activities of Purchaser and its Affiliates and (z) contesting, defending and appealing any threatened or pending preliminary or permanent injunction or other order, decree or ruling, that would adversely affect the ability of Purchaser to consummate the transactions contemplated hereby and taking any and all actions to prevent the entry, enactment or

promulgation thereof. For purposes of this Section 7.2(b) , " Capital Action " shall mean (x) committing to any Governmental Entity with regulatory or supervision authority over Purchaser to maintain capital levels and capital ratios at a level specified by such Governmental Entity, either formally or informally, and either currently or as a result of the transactions contemplated by this Agreement, (y) creating a capital plan that is acceptable to any Governmental Entity with regulatory or supervision authority over Purchaser, either by entering into a new capital plan or modifying an existing capital plan and (z) taking all actions reasonably necessary, including by raising capital through a public or private equity or debt offering, to fully satisfy and achieve the regulatory capital expectations of any Governmental Entity with regulatory or supervision authority over Purchaser.

(c) In furtherance, and not in limitation, of the covenants set forth in Section 7.2(a) and Section 7.2(b) , but subject to Section 7.2(f) , each of the parties hereto agrees to use its reasonable best efforts to take, or cause to be taken, all actions and to do, or cause to be done, all things necessary, proper or advisable to obtain the Required Government Approvals as promptly as practicable, including promptly agreeing to take and taking any other actions required by any Governmental Entity with respect to any Required Government Approval (i) to the extent necessary to consummate the transactions contemplated hereby as promptly as practicable and, where applicable, or (ii) to avoid a decision by a Governmental Entity to open an in-depth investigation or to cause a Governmental Entity to close its investigation as promptly as reasonably practicable. The parties agree to cooperate in preparing, submitting, filing, updating and publishing (as applicable), as promptly as reasonably practicable, all applications, notifications and report forms as may be required by Applicable Law with respect to the transactions contemplated by this Agreement, including those of any applicable state, federal or foreign regulatory agency, and the parties hereto will use their reasonable best efforts to obtain such approvals and accomplish such actions as expeditiously as possible; provided that, within forty-five (45) days after the date hereof, each party will file any application, notice or report required to be filed by such party with any Governmental Entity with respect to any Regulatory Approval or otherwise required in connection with the transactions contemplated hereby and will use its reasonable best efforts to obtain a waiver from any applicable waiting period, and will make any further filings pursuant thereto that may be necessary in connection therewith.

(d) Each party shall, subject to Applicable Law, (i) permit counsel for the other party to review in advance, and consider in good faith the views of the other party in connection with, any proposed written communication to any Governmental Entity in connection with the transactions contemplated hereby, and (ii) provide counsel for the other party with copies of all filings made by such party, and all material correspondence between such party (and its advisors) with any Governmental Entity and any other information supplied by such party and such party's Affiliates to a Governmental Entity or received from such a Governmental Entity in connection with the transactions contemplated hereby; provided , however , that materials may be redacted (x) to remove references concerning the valuation of the Banking Centers or Purchased Assets (or any aspect thereof), (y) as necessary to comply with contractual arrangements, and (z) as necessary to address reasonable privilege or confidentiality concerns. Each party agrees that it will use reasonable best efforts to keep the other party fully informed with respect to all applications and developments related thereto and, where reasonably practicable under the circumstances, give the other party reasonable advance notice of, and whenever appropriate, invite the other party (and give due consideration in good faith to any reasonable request of the

other party) to participate in, any meetings or discussions held with any Governmental Entity; provided that such participation is not objected to by such Governmental Entity. The parties further covenant and agree to mutually identify the most expedient method of effecting, as promptly as practicable, the legal transfer of all of the Purchased Assets and the Assumed Liabilities to Purchaser, and each party further covenants and agrees to use its reasonable best efforts to so effectuate such transfer. The parties further covenant and agree not to extend any waiting period associated with any Regulatory Approval or enter into any agreement with any Governmental Entity not to consummate the transactions contemplated by this Agreement, except with the prior written consent of the other party hereto.

(e) The parties further covenant and agree that (i) with respect to any threatened or pending preliminary or permanent injunction or other order, decree or ruling or statute, rule, regulation or executive order that would adversely affect the ability of the parties hereto to consummate the transactions contemplated hereby, to use their respective best efforts to prevent the entry, enactment or promulgation thereof, as the case may be, and (ii) in the event that any action, suit, proceeding or investigation is commenced after the date hereof challenging any of the parties' rights to consummate the transactions contemplated by this Agreement, the parties shall use their best efforts, and take all actions necessary and appropriate, to contest such action, suit, proceeding or investigation.

(f) Promptly upon the execution of this Agreement and subject to Applicable Law, Purchaser and Seller will reasonably coordinate in good faith in respect of any communications by Seller with the parties whose consent is required. Seller and Purchaser, in consultation with each other, shall as promptly as practicable following the date hereof develop a communications and action plan (which plan shall be designed to communicate promptly and follow up with all such parties with respect to, and to obtain, all such required consents), and shall keep each other reasonably informed regarding the progress and status of such efforts.

(g) Each party represents, warrants and agrees that any information furnished by it for inclusion in any regulatory application will to its Knowledge be true and complete in all material respects as of the date so furnished.

Section 7.3 Further Assurances . The parties agree that, from time to time, whether before, on or after the Closing Date, each of them will execute and deliver such further instruments of conveyance and transfer and take such other action as may be reasonably necessary to carry out the purposes and intents of this Agreement. To the extent any Purchased Assets are currently held by an Affiliate of Seller, Seller shall enter into such agreements as are necessary in order to transfer the Purchased Assets to Seller on or before the Closing Date, or otherwise ensure such Purchased Assets will be sold, transferred and assigned to Purchaser at the Closing, subject to the satisfaction of all conditions precedent to the Closing.

Section 7.4 Notice of Changes . (a) Purchaser shall promptly advise Seller, and Seller shall promptly advise Purchaser of (i) any change or event that would or would be reasonably likely to cause or constitute a material breach of any of Purchaser's or Seller', as applicable, representations, warranties or covenants contained herein, or (ii) to the extent permitted by Applicable Law and to the Knowledge of Purchaser or Seller, as applicable, any governmental complaints, any change or event, including investigations or hearings (or communications indicating that the same may be contemplated) or the institution or the threat of significant litigation, that would reasonably be expected to prevent or materially delay the consummation of the transactions contemplated hereby.

(b) Notwithstanding anything to the contrary herein, a party's good-faith failure to comply with its obligations under this Section 7.4 shall not provide the other party hereto or any of such other party's Affiliates with a right not to effect the transactions contemplated by this Agreement, except, in each case, to the extent that the underlying material breach of a representation, warranty or covenant would independently provide such right.

Section 7.5 Confidentiality . Each party to this Agreement shall hold, and shall cause its respective directors, officers, employees, agents, consultants and advisors to hold, in strict confidence, except to the extent necessary to discharge obligations pursuant to Section 7.2 or unless compelled to disclose by judicial or administrative process or, based on the advice of its counsel, by other requirements of Applicable Law or the applicable requirements of any regulatory agency or relevant stock exchange, all non-public records, books, contracts, instruments, computer data and other data and information (collectively, " Information ") concerning the other party (or, if required under a contract with a third party, such third party) furnished to it by such other party or its representatives pursuant to the Confidentiality Agreement or otherwise in connection with the transactions contemplated by this Agreement (except to the extent that such information can be shown to have been (i) previously known by such party on a non-confidential basis, (ii) in the public domain through no fault of such party or (iii) later lawfully acquired from other sources by the party to which it was furnished), and neither Seller nor Purchaser shall release or disclose such Information to any other person, except its auditors, attorneys, financial advisors, bankers, other consultants and advisors with a duty of confidentiality and, to the extent permitted above, any Governmental Entity. To the extent permitted by Applicable Law, each party will notify the other party promptly upon becoming aware that any of the Confidential Information has been disclosed to or obtained by a third party (otherwise than as permitted by this Section 7.5 ). The Confidentiality Agreement is hereby terminated.

Section 7.6 Publicity; Notices . Until the Closing Date, the parties hereto shall coordinate with each other as soon as practicable in advance as to (i) the form and content of any external communication, including any communication intended for dissemination or to reach, or reasonably expected to be disseminated or to reach, members of the public or Banking Center Customers regarding the transactions contemplated by this Agreement and (ii) the form and content of any communication from Purchaser to the Banking Center Employees. Neither party shall disseminate any such communication without adequate advance notice and the prior review of the other, which review shall not be unreasonably delayed, except that nothing contained in this Agreement shall prevent the parties hereto from publishing any press release or from making any and all public disclosures which it reasonably determines to be legally required to comply with any applicable securities laws or regulations or requests of governmental agencies or authorities; provided that, to the extent possible under the circumstances, the party making such disclosure consults with the other party, and considers in good faith the views of the other party, before doing so.

Section 7.7 Restricted Assignments . Notwithstanding anything in this Agreement to the contrary, this Agreement shall not constitute an agreement to assign any Purchased Asset, Assumed Agreement, Assumed Deposits or other Assumed Liability, or any claim or right or any benefit arising thereunder or resulting therefrom if an attempted assignment thereof, without the consent of a third party thereto, would constitute a breach thereof or in any way affect the rights of Seller or its Subsidiaries thereunder or be contrary to Applicable Law. If any such consent or approval is not obtained, Seller will use its reasonable best efforts (which shall not require Seller to pay any money or other consideration to any Person or to initiate any claim or proceeding against any Person) to secure an arrangement reasonably satisfactory to Purchaser ensuring that Purchaser will receive the benefits under the agreement for which such consent is being sought following the Closing; provided , however , that Seller shall have no obligation to obtain such consent or approval or to provide such an alternative arrangement other than the undertaking to use reasonable best efforts to obtain or provide the same as set forth in this Section 7.7 and, Purchaser shall remain obligated to close the transactions contemplated, subject to the other provisions hereof, and shall have no remedy for failure of Seller to obtain any such consent or approval or to provide any such alternative arrangement.

Section 7.8 Transition Coordinators; Cooperation with Transition . Subject to Applicable Law, from the date hereof until the earlier of the Closing Date and the termination of this Agreement, Seller will cooperate with Purchaser to provide current information regarding material activities of the Banking Centers, and Purchaser and Seller shall cooperate with and assist each other in planning and implementing necessary and appropriate policies and procedures in connection with the transition of the ownership of the Banking Centers from Seller to Purchaser. In connection therewith, Seller and Purchaser shall each as promptly as practicable after the execution of this Agreement designate certain of their respective employees as "transition coordinators."

Section 7.9 Non-Competition and Non-Solicitation. (a) During the period beginning on the Closing Date and ending on the first (1st) anniversary of the Closing Date (the " Non-Competition Period "), neither Seller nor any of its Subsidiaries (collectively, for purposes of this Section 7.9(a) , the " Restricted Entities ") shall establish new banking branches in the Designated Footprint ( it being understood that expansion at any existing banking branch in the Designated Footprint shall not be limited); provided , however , that the foregoing shall not restrict any of the Restricted Entities from (i) making any acquisitions of or investments in any then existing banking branch in the Designated Footprint or (ii) acquiring branches under the Purchase and Assumption Agreement dated as of July 30, 2011, as amended from time to time, with HSBC Bank USA, National Association and Affiliates thereof.

(b) From the date hereof until the Closing Date, Purchaser and its Affiliates shall not, directly or indirectly, solicit for employment (other than as expressly permitted by this Agreement) or hire (i) any Banking Center Employees who are not hourly wage (non-exempt) employees or (ii) any employees of Seller or its Affiliates who are or will be engaged in the preparation for or implementation of any Conversion or the transfer of any of the Purchased Assets or Assumed Liabilities, or who are or will be otherwise involved in providing services under the Transition Services Agreement. For purposes of monitoring Section 7.9(b)(i) and (ii) , all individuals described in (i) and (ii) shall be identified on a Schedule 7.9(b) to be delivered to Purchaser within thirty (30) calendar days of the date hereof and which may be updated from time to time by Seller.

(c) During the period beginning on the Closing Date and ending on the first anniversary of the Closing Date:

(1) Purchaser and its Affiliates shall not, directly or indirectly, solicit for employment or hire any Retained Employee; provided that this Section 7.9(c)(1) shall not prohibit Purchaser or any of its Affiliates from (i) engaging in solicitation by means of a general purpose advertisement not specifically targeted at the Retained Employees or hiring any Retained Employee as a result of such general purpose advertisement or (ii) hiring any Retained Employee who was terminated by Seller after the Closing Date; and

(2) Seller shall not, directly or indirectly, solicit for employment or hire any Transferred Banking Center Employee; provided that this Section 7.9(c)(2) shall not prohibit Seller from (i) engaging in solicitation by means of a general purpose advertisement not specifically targeted at the Transferred Banking Center Employees or hiring any Transferred Banking Center Employee as a result of such general purpose advertisement or (ii) hiring any Transferred Banking Center Employee who was terminated by Purchaser or any of its Affiliates after the Closing Date.

(d) During the period beginning on the date hereof and ending on the first (1st) anniversary of the Closing Date, Seller and its Affiliates shall not, directly or indirectly (i) solicit or engage in other efforts directed to or targeted at any Banking Center Customer that is a retail customer or "business banking" customer with respect to providing Banking Related Services to such retail customer or business banking customer; or (ii) advertise or market Banking Related Services through advertisements or marketing efforts primarily directed to or primarily targeting retail or business banking Banking Center Customers; provided that nothing in this Section 7.9(d) shall be construed as limiting the ability of Seller to (x) respond to unsolicited requests by retail or business banking Banking Center Customers; (y) advertise or solicit directly to the public generally; or (z) service retail or business banking Banking Center Customers who, as of the date hereof, are also customers of Seller or its Affiliates. For the avoidance of doubt this Section 7.9(d) shall not restrict Seller and its Affiliates with respect to Excluded Business Activities. As used in this Section 7.9(d), "business banking" customer shall be determined by reference to Section 2.1(c) .

(e) Each of Purchaser and Seller understands and acknowledges that (i) it would be difficult to calculate damages to Seller or Purchaser, as applicable, from any breach of the obligations of Purchaser or Seller, as applicable, under this Section 7.9 , (ii) injury to Purchaser or Seller, as applicable, from any such breach would be irreparable and impossible to measure and (iii) the remedy at law for any breach or threatened breach of this Section 7.9 would therefore be an inadequate remedy and, accordingly, Purchaser and Seller shall, in addition to all other available remedies (including, without limitation, seeking such damages as either can show it has sustained by reason of such breach and/or the exercise of all other rights either has under this Agreement), be entitled to seek injunctive relief, specific performance and other equitable remedies without the necessity of showing actual damages or posting bond.

(f) Purchaser and Seller understand and acknowledge that the restrictive covenants and other agreements contained in this Section 7.9 are an essential part of this Agreement and the transactions contemplated hereby and thereby. It is the intention of the parties that, if any of the restrictions or covenants contained herein are held to cover a geographic area or to be for a length of time that is not permitted by Applicable Law, or is in any way construed to be too broad or to any extent invalid, such provision shall not be construed to be null, void and of no effect, but to the extent that such provision would then be valid or enforceable under Applicable Law, such provision shall be construed and interpreted or reformed to provide for a restriction or covenant having the maximum enforceable geographic area, time period and other provisions as shall be valid and enforceable under Applicable Law.

(g) For the avoidance of doubt, none of the restrictions imposed by applicable subsections of this Section 7.9 shall apply to any Person that is an Affiliate of a party to this Agreement if such Person ceases to be an Affiliate of such party.

(h) Purchaser shall take any commercially reasonable actions to cooperate and facilitate Seller's ability to retain and/or continue to service Banking Center Customers with regard to the Credit Card Accounts and Receivables.

Section 7.10 Arrangements with Respect to Employee Pension Plans, IRAs and Keogh Plans . On or before the Closing Date, Seller shall cause notice (such notice to be approved in advance by Purchaser) to be sent to each depositor of an Assumed Deposit held by Seller or any of its Subsidiaries in an IRA and each "employer" who established an Assumed Deposit pursuant to a Keogh plan and each depositor that is an Employee Pension Plan, regarding the resignation of Seller as IRA custodian or Keogh plan or Employee Pension Plan trustee, as applicable. Such resignation shall be effective as of the date that is thirty (30) days following the date of the notice or, if later, the Closing Date. If a depositor of an Assumed Deposit held by Seller in an IRA or an employer who established an Assumed Deposit pursuant to a Keogh plan, Employee Pension Plan or other retirement plan fails to appoint another trustee or custodian for such account within this period, such depositor or employer will be deemed to have appointed Purchaser as successor trustee or custodian for the deposit account. Upon its appointment as successor trustee or custodian for such accounts, as applicable, Purchaser shall perform the services and carry out the duties and obligations required of it under the applicable plans, the Code and Applicable Law. If, notwithstanding the foregoing, as of the Closing Date, Purchaser shall be unable to retain deposit liabilities in respect of an Employee Pension Plan, IRA, Keogh Plan or other retirement plan, such deposit liabilities shall be considered "Excluded Deposits."

Section 7.11 Updated Schedules . (a) On the fifth (5th) day prior to the Closing Date anticipated by the parties, Seller shall deliver to Purchaser updated versions of the following schedules so that they are as of a date no earlier than last day of the month preceding the Closing Date (such date, the " Update Date "): Schedule 1.1(a) (Assumed Deposits), Schedule 1.1(c)(i) (Banking Center Employees), Schedule 1.1(h) (Purchased Overdrafts), Schedule 2.1(a)(1) (Purchased Real Property), Schedule 2.1(a)(2) (Real Property Leases), Schedule 2.1(a)(4) (Personal Property Leases), Schedule 2.1(a)(5)(i) (Purchased ATMs), Schedule 2.1(a)(5)(ii) (ATM Real Property Leases), Schedule 2.1(a)(6) (Purchased Loans), Schedule 2.1(a)(8) (CRA Assets), Schedule 2.1(a)(9) (Assumed Letters of Credit), and Schedule 2.1(a)(10) (Assumed Contracts). Seller and Purchaser agree that the updated versions of the foregoing Schedules shall be prepared using the same methodology and criteria used in preparing the Schedules attached to this Agreement.

(b) In connection with delivery of the Final Closing Statement Seller shall deliver to Purchaser updated versions of the following schedules, so that they are as of the Closing Date (such schedules, collectively, the " Final Schedules "): Schedule 1.1(a) (Assumed Deposits), Schedule 1.1(c)(i) (Banking Center Employees), Schedule 1.1(h) (Purchased Overdrafts), Schedule 2.1(a)(1) (Purchased Real Property), Schedule 2.1(a)(2) (Real Property Leases), Schedule 2.1(a)(4) (Personal Property Leases), Schedule 2.1(a)(5)(i) (Purchased ATMs), Schedule 2.1(a)(5)(ii) (ATM Real Property Leases), Schedule 2.1(a)(6) (Purchased Loans), Schedule 2.1(a)(8) (CRA Assets), S chedule 2.1(a)(9) (Assumed Letters of Credit), and Schedule 2.1(a)(10) (Assumed Contracts). Seller and Purchaser agree that the updated versions of the foregoing Schedules shall be prepared using the same methodology and criteria used in preparing the Schedules attached to this Agreement.

## ARTICLE VIII

## FURTHER AGREEMENTS

Section 8.1 Conduct of the Banking Centers Prior to the Closing . (a) From the date hereof until the earlier of the Closing Date and the termination of this Agreement, Seller shall, consistent with the other provisions of this Agreement: (i) use reasonable best efforts to, and cause its Subsidiaries to use their respective reasonable best efforts to, conduct the business of the Banking Centers in the ordinary course consistent with past practice and maintain, generally, their existing relations and goodwill with Banking Center Customers and vendors and suppliers to the Banking Centers; and (ii) use its ordinary course efforts to, and cause its applicable Subsidiaries to use their respective ordinary course efforts to, consistent with historical and customary past practices, preserve in all material respects, the mix, type and aggregate amount of the Purchased Assets and Assumed Liabilities, including the Assumed Deposits, provided that the agreement by Seller to use its ordinary course efforts shall not be construed as any promise, representation or guarantee by Seller that such mix, type and amount will in fact be maintained and may in fact be materially different as of the Closing Date, and the occurrence of such event shall not, in and of itself, be considered a breach of Seller's obligations under this Section 8.1(a) .

(b) From the date hereof until the earlier of the Closing Date or the termination of this Agreement, except as (i) otherwise expressly contemplated by this Agreement, (ii) consented to in writing in advance by Purchaser (which consent shall not be unreasonably withheld or delayed), or (iii) required by Applicable Law, Seller shall not, and shall cause its applicable Subsidiaries not to:

(1)(i) materially increase or reduce the number of persons employed in the Banking Centers, (ii) increase the compensation or benefits payable to any Banking Center Employees by an aggregate amount that is greater than 4% of base salary or base wage (in connection with Seller's ordinary annual performance evaluation cycle) or by any amount (in any other case), (iii) promote any Banking Center Employee to

the position of vice president or any more senior position, or (iv) enter into any Employee Plan or any collective bargaining agreement with respect to the Transferred Banking Center Employees; provided , however , that nothing in this Section 8.1(b)(1) shall limit the ability of Seller and any of its Subsidiaries to adopt, modify, amend or terminate any employee benefit plan, program, policy, arrangement or practice that is or may become applicable to the employees of Seller generally; provided , further , that Seller shall promptly notify Purchaser of any such adoption, modification, amendment or termination that affects any Banking Center Employee;

(2) terminate or materially modify in any manner materially adverse to Seller any Real Property Lease; or place or permit to be placed, any Lien (other than a Permitted Lien) upon any of the Purchased Assets;

(3) fail to maintain the Banking Center Premises in a condition substantially the same as of the date of this Agreement, ordinary wear and use excepted;

(4) fail to maintain in effect all property, liability, fire and casualty insurance in effect as of the date hereof, on substantially the same terms as currently in effect, with regard to the Banking Center Premises or Purchased Assets;

(5) terminate or materially modify any Assumed Agreement, except as required by its existing terms, including as a result of action by the other party to such Assumed Agreement or in the ordinary course of business;

(6) close, sell, consolidate or relocate or materially alter any of the Banking Centers;

(7) amend or modify, including by entering into any forbearance agreement with respect to, any Purchased Loan in any manner materially adverse to Seller or its Subsidiaries or in any manner other than in the ordinary course of business and consistent with the written loan policies of Seller and its Subsidiaries as of the date hereof;

(8) sell, transfer or convey any material property that is part of the Purchased Assets, other than in the ordinary course of business;

(9) release, compromise, or waive any material claim or right that is part of the Purchased Assets, other than in the ordinary course of business;

(10) settle or compromise any litigation or investigation if such settlement or litigation would reasonably be expected to impose any material obligation or liability on the Purchased Assets, the Assumed Liabilities or Purchaser or any of its Subsidiaries (other than any settlement or compromise providing solely for the payment of money damages that is included as a liability on the Closing Statement or Final Closing Statement);

(11) other than in the ordinary course of business consistent with past practice or as determined to be necessary or advisable by Seller in the reasonable bona fide exercise of its discretion based on changes in market conditions applicable to the Banking Centers, materially alter its interest rate, credit policies or fee pricing policies or practices with respect to the Assumed Deposits and the Purchased Loans provided , however , that Seller shall be permitted to take such actions with respect to the Assumed Deposits to the extent reasonably deemed necessary to preserve the mix, type and aggregate amount of the Assumed Deposits; or

(12) agree to take any of the actions listed in the foregoing clauses (1) through (11).

Section 8.2 Real Property Leases and ATM Leases . (a) Seller shall use its reasonable best efforts (which shall not require Seller to pay any money or other consideration to any Person or to initiate any claim or proceeding against any Person) to cause every landlord of a Real Property Lease or ATM Real Property Lease, the consent of which is required under the terms of the applicable Real Property Lease or ATM Real Property Lease to the assignment of such Real Property Lease or ATM Real Property Lease to Purchaser, to execute in favor of Purchaser a Landlord Consent.

(b) If, despite Seller's reasonable best efforts, a Landlord Consent to assignment of a Real Property Lease or ATM Real Property Lease cannot be obtained, or cannot be obtained without the payment of an assignment fee or similar lump sum or rent increase, Seller shall, if permitted without the consent of the landlord under the Real Property Lease or ATM Real Property Lease, sublease the Banking Center Premises or ATM location to Purchaser pursuant to a sublease agreement which shall be, to the extent permitted, for the remainder of the existing term of the Real Property Lease or ATM Real Property Lease, as applicable, and which shall provide for Purchaser to perform all of the obligations of Seller under such Real Property Lease or ATM Real Property Lease and which otherwise shall contain mutually agreeable terms (a " Sublease Agreement ").

(c) Purchaser shall use its reasonable best efforts to cooperate with Seller's attempts to obtain each Landlord Consent or its approval of a Sublease Agreement, but shall not be obligated to pay any consideration or grant any concession in connection therewith.

(d) Notwithstanding anything to the contrary contained in this Agreement, if Seller is unable to obtain for Purchaser the right to occupy a Banking Center Premises, whether pursuant to a Landlord Consent or a Sublease Agreement or otherwise, Purchaser shall not be entitled to terminate this Agreement and Purchaser shall remain obligated to perform all of its obligations hereunder, including, without limitation, the assumption of the Assumed Deposits without any reduction or adjustment to the consideration to be paid by Purchaser as provided in this Agreement.

Section 8.3 UCC-1 Assignment and Other Documents . (a) Seller shall use its reasonable best efforts to deliver to Purchaser at the Closing all signed UCC-1 financing statements and UCC-3 assignments of financing statements, endorsed notes, participations, assignments of mortgages in recordable form and all other documentation necessary to effect the assignment of the Purchased Loans (including all related collateral) and the Assumed Letters of Credit to Purchaser. The out-of-pocket costs and expenses of preparing and filing any such documentation shall be split equally between Seller and Purchaser.

(b) In accordance with Article 9 of the UCC, from the date hereof until the Closing Date, Seller shall make all filings of continuation statements necessary to maintain perfection of security interests related to the Purchased Loans and Assumed Letters of Credit.

Section 8.4 Letters of Credit . In the event that any Assumed Letter of Credit cannot be assigned to Purchaser, on the applicable Closing Date, Purchaser and Seller shall enter into a participation agreement in customary form reasonably satisfactory to Purchaser and Seller pursuant to which Purchaser shall acquire and assume all of Seller's rights and obligations under such Assumed Letters of Credit and become entitled to all reimbursements thereunder.

Section 8.5 Form of Transfer . Seller and Purchaser may by mutual written agreement at any time change the method of transferring the Banking Centers from Seller to Purchaser in order to achieve, in a more efficient manner, the business, financial accounting, regulatory and tax objectives of Seller and Purchaser in connection with the transactions contemplated by this Agreement; provided , however , no such change shall alter or change the amount of consideration to be paid by Purchaser as provided in this Agreement.

Section 8.6 Conversion Plan, Data Processing and Related Matters (a) The parties hereto agree to cooperate to employ their reasonable best efforts to plan, execute and complete the Conversion in an orderly and efficient manner pursuant to the Conversion Plan. As promptly as practicable after the date hereof, Purchaser and Seller shall each appoint qualified staff members to act as project managers for the Conversion (each, a " Conversion Project Manager "). Such Conversion Project Managers shall act as the principal contacts between the parties on matters relating to the Conversion, and shall coordinate the assignment of personnel as required and generally facilitate the planning, execution and completion of the Conversion pursuant to the Conversion Plan. In addition to any conversion of the data and systems files as part of the Conversion pursuant to the Conversion Plan, the parties shall reasonably cooperate in performing such tasks as may be outlined in the Conversion Plan (as defined below), including the collection and input of relevant data, development of new operating procedures and design of forms, in each case, as mutually agreed by the parties.

(b) Purchaser and Seller shall each bear all out-of-pocket costs and expenses associated with their respective area of responsibility as defined in the Conversion Plan, including costs and expenses (including the costs and expenses incurred by Seller or its Affiliates) incurred in converting, moving, storing, archiving, adapting or otherwise transferring or facilitating the transfer of any data, information, securities, records, files and systems from the systems and facilities of Seller and its Affiliates to the systems and facilities of Purchaser and its Affiliates (including costs with respect to computer programs, data processing, deconversion, data extraction, third-party charges and filing fees) provided, however, that, notwithstanding anything to the contrary in this Section 8.6 or otherwise in this Agreement, Purchaser shall not be liable hereunder for any termination fees, penalties or other break costs incurred by Seller or any of its Subsidiaries as a result of the Conversion. Purchaser and Seller each agrees to promptly reimburse the other in accordance with the Conversion Plan.

(c) In connection with the conversion activities described in subsections (a) and (b) immediately above, and subject to Applicable Law and the Transition Services Agreement, it is further agreed that:

(1) Purchaser will review, subject to Section 7.1 , current operations of the Banking Centers and Purchaser and Seller shall cooperate and use their reasonable best efforts to develop a mutually agreeable written plan within forty-five (45) days of the date hereof (as it may be amended from time to time, the " Conversion Plan "), which Conversion Plan shall (i) set forth the plan, procedures, scheduling methodology, resources and expenditures required to fully effect the Conversion by the end of the weekend immediately after the Closing Date (or such other date as may be agreed by the parties), (ii) include interim target dates for the completion of integral items to the Conversion; and (iii) provide that conversion items integral to the operation of the Banking Centers, as identified by Purchaser, shall have the earliest target completion dates in the Conversion Plan; and

(2) as of the Closing Date, Seller will provide Purchaser with existing customer, account and transaction data feeds related to the Banking Centers in order to allow Purchaser to comply with applicable legal and contractual anti-money laundering and privacy requirements on and after the Closing Date.

(d) The parties agree to cooperate to schedule arrangements for change in displays and advertisements at the Banking Centers such that on the next Business Day following a Closing Date, no Signage shall be displayed at the Banking Centers, either internally or externally. To the extent that any Signage shall remain at a Banking Center, Purchaser shall use its reasonable best efforts to remove such Signage prior to the next Business Day following the Closing Date and to retain such Signage for later collection by Seller.

(e) The parties agree to address certain transitional matters in the Transition Services Agreement to be prepared jointly by them reasonably and in good faith.

Section 8.7 Seller Intellectual Property . (a) Except as specifically provided in this Section 8.7 , Purchaser acknowledges and agrees that none of Purchaser or its Affiliates is purchasing, acquiring, receiving a license to or otherwise obtaining any right, title or interest in, to or under any Intellectual Property owned or licensed by Seller or any of its Affiliates, including the Seller Names.

(b) Except as provided in this Section 8.7 , as of and following the Closing, Purchaser shall, and shall cause its Affiliates to, cease and discontinue promptly after the Closing any and all uses of any and all Intellectual Property owned or licensed by Seller or any of its Affiliates, including Seller Names. Except as provided in this Section 8.7 , Purchaser agrees that, as of and following the Closing, none of Purchaser not any of its Affiliates shall have any right, title or interest in, or any authority or license to use or allow others to use in any manner whatsoever, any Intellectual Property owned or licensed by Seller or its Affiliates, and any such right, title, interest, authority, license or sublicense or other arrangement relating thereto (whether written or oral) existing prior to the Closing, shall automatically terminate simultaneously with and effective as of the Closing. Notwithstanding the foregoing and only to the extent that use of

labeling, stationery, business forms, supplies, ATM cards, debit cards, gift cards, checks, deposit slips and envelopes (but excluding any advertising, marketing or other promotional materials) existing on the Banking Center Premises or in the possession of a Banking Center Customer, in each case, that bear a Seller Name as of the Closing (the " Business Material ") cannot be commercially reasonably avoided after the Closing by Purchaser and its Affiliates, Purchaser and such Affiliates shall have, subject to the execution by Purchaser and such Affiliates of the License Agreement, a limited, non-transferable, non-sublicensable, royalty-free, non-exclusive right to use and deplete the Business Materials for a thirty- (30) day period following the Closing Date (such right, the " Seller Name License " and such period, the " Transitional Period "); provided , however , that (i) none of Purchaser or any of its Affiliates shall take any action that could reasonably be expected to impair the value of or goodwill associated with the Seller Names, (ii) Purchaser and its Affiliates shall use the Business Materials and make any use of the Seller Names pursuant to this Section 8.7 in substantially the same forms, and for substantially the same purposes, as Seller is using such Seller Names in connection with the operation and conduct of the Banking Centers immediately prior to the Closing, but not including any advertising, marketing or other promotional activities and (iii) Purchaser and its Affiliates shall use their reasonable best efforts to minimize their respective use of the Seller Names and shall cease using the Seller Names on such Business Materials as set forth in the License Agreement and in any event within the Transitional Period. For clarity, the foregoing activities during the Transitional Period will be for wind-down purposes only, and none of Purchaser or any of its Affiliates shall actively use the Seller Names in any advertising, marketing or other promotional activities during the Transitional Period.

(c) Purchaser, for itself and its Affiliates, acknowledges and agrees that, (i) as between the parties hereto, Seller and its Affiliates own or have the exclusive right to use any and all of the Seller Names and, except as otherwise expressly provided in this Section 8.7 , none of Purchaser or any of its Affiliates shall, as of the Closing, have any rights in or to the Seller Names, (ii) none of Purchaser or any of its Affiliates shall contest the ownership or validity of any rights of Seller or any of its Affiliates in or to the Seller Names, and (iii) none of Purchaser or any of its Affiliates shall adopt, use, register or attempt to register any of the Seller Names or instruct others to do so. Purchaser, for itself and its Affiliates, agrees and shall ensure that any use of the Seller Names as permitted in this Section 8.7 shall be only with respect to goods and services of a level of quality equal to or greater than the quality of goods and services with respect to which Seller and its Affiliates used such Seller Names prior to the Closing. Purchaser, for itself and its Affiliates, agrees that, after the Closing, none of Purchaser or any of its Affiliates, will expressly, or willingly by implication, do business as or represent themselves as Seller or any Affiliate of Seller and the personnel of Purchaser or any of its Affiliates shall not, and shall have no authority to, as of the Closing, hold themselves out as officers, employees or agents of Seller or any of its Affiliates.

(d) Purchaser, on behalf of itself and its Affiliates, agrees that Purchaser and its Affiliates shall indemnify and hold harmless Seller and its Affiliates from and against all Damages that arise out of, relate to or result from use of the Seller Names by Purchaser during the Transitional Period.

Section 8.8 Wrong Pocket Assets . Unless otherwise specifically provided in the Transition Services Agreement, if at any time or from time to time after the Closing Date, Seller, on the one hand, or Purchaser, on the other, shall receive or otherwise possess any asset (including cash) that should belong to another Person pursuant to this Agreement, Seller or Purchaser agrees to promptly transfer, or cause to be transferred, such asset to the Person so entitled thereto.

Section 8.9 Title Objections . Within fifteen (15) days of the date of this Agreement, Seller shall provide Purchaser with copies of all deeds, title policies, title commitments, surveys, tax searches or other title documentation in its possession for all Purchased Real Property. Purchaser shall be entitled, at its own expense, to update title and survey with respect to any or all parcels of Purchased Real Property. No later than thirty (30) days after the date of this Agreement, Purchaser may deliver to Seller in writing Purchaser's objections to title to the Purchased Real Property (with each objection stated with reasonable specificity) (such delivery, the " Title Objections Report ") if Purchaser in good faith believes that the objectionable matters would materially detract from the value of the Purchased Real Property or interfere with the continued operations at the Purchased Real Property in the manner in which operations are currently being conducted at the Purchased Real Property (any such matter, a " Title Objection "). Seller shall have fifteen (15) days after its receipt of the Title Objections Report to determine, in its sole discretion, if Seller is willing to remove or cure the Title Objection(s) or bond over the Title Objections. If Seller is unwilling to remove or cure or bond over such Title Objections, then Purchaser, at its sole discretion, shall have the right (exercisable upon irrevocable written notice to Seller delivered within fifteen (15) days after expiration of the forgoing 15-day period, to exclude the Banking Center situated on such Purchased Real Property from the Purchased Assets (and to exclude such Purchased Real Property from the Purchased Assets). Seller shall not list any such Purchased Real Property so excluded by Purchaser on Schedule 2.1(a)(1) , and the excluded Banking Center shall be excluded from the Designated Footprint.

Section 8.10 Environmental Objections . Within forth-five (45) days of the date of this Agreement, Purchaser shall give Seller written notice of environmental matters and conditions to which Purchaser objects based upon the results of its Phase I ESAs, the results of its other environmental due diligence, and Seller's Disclosure Schedules (the " Environmental Objections "). Upon Seller's receipt of Purchaser's notice of Environmental Objections, the parties shall, in good faith, use reasonable efforts to negotiate mutually satisfactory resolution of the Environmental Objections prior to the Closing Date. The parties agree that matters or conditions shall only qualify as Environmental Objections if Purchaser believes the matters or conditions constitute actual or potential violations of, or liabilities under, Environmental Laws. If, despite such good faith negotiations, all of the Environmental Objections are not resolved within ten (10) days prior to the Closing Date, then Purchaser, at its sole discretion, shall have the right to exclude the Banking Center Premises to which the unresolved Environmental Objections pertain (and, if applicable, any corresponding Real Estate Lease) from the Purchased Assets (and to exclude such Real Estate leases from the Assumed Liabilities). Seller shall not list any such Banking Center Premises or Real Estate Leases so excluded by Purchaser on Schedule 2.1(a)(1) or Schedule 2.1(a)(2) , as applicable. For the avoidance of doubt, Purchaser shall have the right to exclude from the Purchased Assets any Banking Center Premises (and corresponding Real Estate Leases) for which Purchaser is unable to conduct full and complete Phase I ESAs which meet the requirements in 40 CFR Part 312 because Seller has not provided reasonable access pursuant to Section 7.1(a). Seller shall not list any such Banking Center Premises (or Real Estate Leases) so excluded by Purchaser on Schedule 2.1(a)(1) or Schedule 2.1(a)(2 ), as applicable, and the excluded Banking Center shall be excluded from the Designated Footprint.

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## ARTICLE IX

## EMPLOYMENT AND BENEFIT MATTERS

Section 9.1 Transferred Banking Center Employees . (a) *Offers of Employment* . Subject to Applicable Law, at least thirty (30) days (unless an earlier date is required by Applicable Law) prior to the Closing Date and effective as of the Closing Date, Purchaser shall make, and Purchaser and Seller shall use reasonable best efforts to cause to be accepted, a Comparable Job Offer to all Banking Center Employees. Purchaser's employment of the Transferred Banking Center Employees shall be deemed to commence at 11:59 p.m. on the Closing Date, without regard to whether the Transferred Banking Center Employee is actively at work on the Closing Date in the case of an employee who on the Closing Date is absent from work due to a vacation, jury duty, funeral leave or personal day. Notwithstanding the foregoing, to the extent that a Banking Center Employee who has accepted Purchaser's offer is not available to perform services on the Closing Date because on the Closing Date such employee is on sick leave, short-term disability, workers compensation leave, military leave, leave of absence under the Family Medical Leave Act or other leave of absence approved by Seller or one of its Affiliates (other than a vacation, jury duty, funeral leave or personal day), he or she shall remain an employee of Seller or one of its Affiliates (except as otherwise required by Applicable Law); provided that Purchaser make, and shall use reasonable best efforts to cause to be accepted, a Comparable Job Offer to such Banking Center Employee if such Banking Center Employee returns to work no later than the date that is the earlier of the scheduled return date (including any approved extensions thereto) and six (6) months from the date of commencement of such leave, unless such Employee is entitled to reemployment under the Uniformed Services Employment and Reemployment Act, in which case Purchaser shall not be obligated hire such Employee unless the return date is no later than twelve (12) months following the Closing Date, and, for purposes of this Agreement, such Employee shall become a Transferred Banking Center Employee as of the date active employment with Purchaser commences and, to the extent applicable, references in this Section 9.1 to the "Closing Date" shall relate to the date on which active employment commences. Those Banking Center Employees who do not accept a Comparable Job Offer from Purchaser shall not be considered Transferred Banking Center Employees for any purpose of this Agreement. Each of the Transferred Banking Center Employees shall be provided by the Purchaser with an aggregate annual amount of paid time-off under the plans of the Purchaser equal to such Transferred Banking Center Employee's current aggregate annual amount of paid time-off, which, for clarity, takes into account and grandfathers all service with Seller and its Affiliates (including vacation time, personal time and sick time); provided that the Purchaser may allocate such aggregate annual amount of paid time-off in a manner consistent with the policies of the Purchaser. Notwithstanding the foregoing provisions of this Section 9.1(a) , and subject to the provisions of Section 9.1(d) , Transferred Banking Center Employees who accept an offer of employment (including any Comparable Job Offer) with Purchaser or an Affiliate of Purchaser will be considered at-will employees and may be terminated by Purchaser for any reason or for no reason at any time.

(b) *Termination of Employment with Seller* . As of the Closing Date, the Transferred Banking Center Employees shall cease active participation in each Employee Plan and shall have a "separation from service" as that term is defined by Section 409A of the Code and the regulations promulgated thereunder. Seller and its Affiliates shall retain all assets and Liabilities for the Banking Center Employees under the Employee Plans. Seller and its Affiliates shall be liable for all eligible claims for benefits under the Employee Plans. For purposes of this Agreement, the following claims shall be deemed to be incurred as follows: (i) life, accidental death and dismemberment, business travel accident, disability and workers compensation insurance benefits, upon the event giving rise to such benefits; and (ii) health, vision, dental and/or prescription drug benefits, on the date such services, materials or supplies were provided.

(c) *Benefits Following the Closing Date* . Effective as of the Closing Date, Purchaser shall provide the Transferred Banking Center Employees with the same employee benefit plans and programs as those that are provided to similarly situated employees of Purchaser (both by job classification or status and by geographic location). For purposes of determining (i) eligibility to participate in and vesting under applicable employee benefit plans of Purchaser or its Affiliates (other than under any employee stock ownership or option plan), (ii) the banking privileges and perquisites applicable to the Transferred Banking Center Employees, (iii) retirement eligibility under any Purchaser plan providing for the grant of equity awards, (iv) for benefit accrual purposes for paid time-off (including vacation time, personal time and sick time) and, if applicable, severance benefits, (v) the level of pay credits under a cash balance plan, in each case, as applicable, each Transferred Banking Center Employee shall be credited with the years of service he or she has been credited with under any comparable Employee Plans; provided that such service shall not be recognized for purposes of (x) grandfathering and/or benefit accruals under any Purchaser defined benefit retirement plan, (y) retiree medical benefits (but it shall be recognized for access-only retiree medical, if applicable) or (z) any employee stock ownership or option plan. Purchaser shall (i) deem satisfied any preexisting conditions and waiting periods under the welfare benefit plans of Purchaser that provide healthcare benefits in which the Transferred Banking Center Employees are eligible to participate to the same extent that such conditions and waiting periods were satisfied under a comparable Employee Plan and (y) subject to Seller providing Purchaser with the applicable information with respect to each Transferred Banking Center Employee in a form that Purchaser determines is administratively feasible to take into account under its plans, cause such plans to honor any expenses incurred by such Transferred Banking Center Employees and their eligible dependents under comparable Employee Plans that are healthcare benefit plans during the portion of the calendar year in which they become Transferred Banking Center Employees for purposes of satisfying applicable deductible, co-insurance, maximum out-of-pocket, and similar expenses, to the same extent that such expenses were recognized under the comparable Employee Plan. Purchaser shall not provide any payment or incentive to any Transferred Banking Center Employee to induce such employee to elect continued participation in any healthcare benefit plan of Seller

(d) *Severance* . (i) Termination of Transferred Banking Center Employees Following the Closing Date . Purchaser shall pay, or cause to be paid, severance and provide benefits in accordance with the severance schedule set forth on Schedule 9.1(d)(i)(A) , to each

Transferred Banking Center Employee whose employment is terminated by Purchaser or any Affiliate of Purchaser without "cause" (within the meaning set forth on Schedule 9.1(d)(i)(B )) within twelve (12) months after the Closing Date, subject to the execution, delivery and non-revocation of a release of claims in favor of Purchaser, Seller and the respective Affiliates of Purchaser and Seller.

(ii) Termination of Banking Center Employees who do not become Transferred Banking Center Employees . With respect to Banking Center Employees who do not become Transferred Banking Center Employees for any reason (other than due to having rejected a Comparable Job Offer), (A) Purchaser shall be responsible for reimbursing Seller or its Affiliates, as applicable, for any severance benefits but not greater than those described on Schedule 9.1(d)(i)(A) to the extent a Banking Center Employee rejects an offer of employment from Purchaser that was not a Comparable Job Offer and (B) Seller and its Affiliates shall retain and shall satisfy all severance benefits payable to any other Banking Center Employees. Except as may otherwise be required by Applicable Law, none of Seller, Purchaser or any of its Affiliates shall pay or provide severance benefits to any Banking Center Employee who receives a Comparable Job Offer from Purchaser and does not accept such offer. Nothing in this Section 9.1(d)(ii) is intended to conflict with the provisions of Section 9.1(g) , but in the event of an inconsistency, Section 9.1(d)(ii) shall govern. Subject to Applicable Law, Seller, its Affiliates and Purchaser shall cooperate to take commercially reasonable steps to reduce, to the extent possible, the likelihood that severance benefits will be required to be paid to any Banking Center Employees who do not become Transferred Banking Center Employees; provided , however , that, in no event, shall Purchaser or Seller be required to find alternative employment for such employees at Purchaser or Seller or one of their respective Affiliates.

(e) *Retirement Plans* . Purchaser shall take commercially reasonable action to permit Purchaser's tax-qualified employee savings plan (s) maintained in the United States and in which Transferred Banking Center Employees participate to accept rollover contributions of "eligible rollover distributions" (within the meaning of Section 402(c)(4) of the Code) for the benefit of participating Transferred Banking Center Employees, including direct rollovers of outstanding plan loans of Transferred Banking Center Employees, provided that such loans are not in default. Without limiting the generality of the foregoing, the parties will cooperate to facilitate the above-described rollover of plan loans by causing their respective savings plan trustees to promptly accomplish the transfer of the relevant plan loan notes and related loan agreements, and by taking commercially reasonable action to forestall loan default.

(f) *Annual Incentives* . (i) Seller shall be liable for the payment of all formulaic incentive bonuses and annual discretionary bonuses to the Transferred Banking Center Employees with respect to the calendar year commencing on January 1, 2011 and ending on December 31, 2011. In addition, Seller shall be liable for the payment of any formulaic incentive bonuses, including monthly, quarterly and semi-annual incentive bonuses, to the Transferred Banking Center Employees with respect to the period commencing on January 1, 2012 and ending on the Closing Date. Such payments shall be made consistent with past practice of Seller, notwithstanding that Transferred Banking Center Employees may not be employed by Seller or any of its Affiliates at the time of payment.

(ii) The Purchaser shall provide Transferred Banking Center Employees an annual discretionary bonus opportunity prorated for calendar year 2012, based upon the number of days elapsed between the Closing Date and December 31, 2012 (with the amount, if any, determined consistent with Purchaser's internal methodology for awarding annual discretionary bonuses). The Seller shall be responsible for and shall pay to the Transferred Banking Center Employees a prorated portion of the annual discretionary bonuses accrued for the Transferred Banking Center Employees prior to the Closing Date, calculated using accruals for performance year 2011, based upon the number of days elapsed between January 1, 2012 and the Closing Date. For purposes of clarity, Seller and its Affiliates shall retain all liabilities for, and shall be responsible for the payment of, any formulaic incentive bonus amounts payable to the Transferred Banking Center Employees for performance periods occurring prior to the Closing Date under any formulaic incentive plans maintained by Seller or its Affiliates (for example, under any monthly, quarterly or commissions-based plans), and such formulaic incentive plans shall not be taken into consideration when determining the obligations of the Purchaser and Seller under this Section 9.1(f)(ii) .

(g) *WARN Act* . The parties hereto agree to cooperate in good faith, including by sharing information about terminations of employment in a timely manner, to determine whether any notification may be required under the WARN Act as a result of the transactions contemplated by this Agreement. Purchaser shall be responsible for providing any notice (or pay in lieu of notice) required pursuant to the WARN Act with respect to a layoff or plant closing involving Transferred Banking Center Employees that occurs on or after the Closing Date. Subject to Section 9.1(d)(ii) , Seller and its Affiliates shall be responsible for providing any such notice (or pay in lieu of notice) with respect to a layoff or plant closing occurring prior to, on or after the Closing Date and involving Banking Center Employees who do not become Transferred Banking Center Employees.

(h) *Employee Communications* . Any communications by Purchaser with the Banking Center Employees prior to the Closing Date shall be subject to and in compliance with the terms of this Agreement. Written communications from Purchaser to Banking Center Employees shall be subject to prior review, comment and approval by Seller and its Affiliates. Seller shall not make any promises or commitments to the Banking Center Employees with respect to employment by Purchaser, or the terms and conditions thereof.

(i) *Banking Privileges* . Purchaser agrees to provide the Transferred Banking Center Employees with the same banking privileges, if any, that Purchaser generally provides to similarly situated employees of Purchaser (both by job classification or status and by geographic location).

(j) *No Third-Party Rights* . No provision of this Article IX shall create any third-party beneficiary rights in any Person, nor is it intended to amend or alter any benefit plan of Purchaser, Seller or any of their respective Affiliates, or limit the ability of the Purchaser or its Affiliates to amend their benefits plans in any respect at any time nor guarantee any Transferred Banking Center Employee the right to continued employment for any period.

(k) *Transition Services* . Purchaser and Seller shall work together and reasonably cooperate to delay the separation from Seller and the start date with Purchaser for any Transferred Banking Center Employees who are necessary to assist Seller in fulfilling their obligations under the Transition Services Agreement.

(l) *Wage Reporting* . Purchaser and Seller agree to utilize the standard procedure set forth in Revenue Procedure 2004-53 with respect to wage reporting.

## ARTICLE X

## TAX MATTERS

Section 10.1 Tax Indemnification . (a) Except to the extent reflected as a liability in the Final Closing Statement, (i) Seller shall pay or cause to be paid, shall be liable for, and shall indemnify, defend and hold Purchaser and its Affiliates harmless from and against any and all Excluded Taxes, other than any liability for Taxes resulting from transactions or actions taken by Purchaser on the Closing Date that are properly attributable to the portion of the Closing Date after the Closing, and (ii) Purchaser shall pay or cause to be paid, shall be liable for, and shall indemnify, defend and hold Seller and its Affiliates harmless from and against any and all Taxes relating to the Banking Centers, the Purchased Assets or Assumed Liabilities other than Excluded Taxes that are the responsibility of Seller under the immediately preceding sentence.

(b) Payment in full of any amount due from Purchaser or Seller under this Section 10.1 shall be made to the affected party in immediately available funds at least two (2) Business Days before the date payment of the Taxes to which such payment relates is due, or, if no Tax is payable, within fifteen (15) days after written demand is made for such payment.

Section 10.2 Refunds, Credits and Carrybacks . (a) Seller shall be entitled to any refunds or credits of or against any Excluded Taxes that are the responsibility of Seller under Section 10.1(a) . Purchaser shall be entitled to any refunds or credits of or against any Taxes relating to the Purchased Assets, other than refunds or credits of or against Excluded Taxes that are the responsibility of Seller under Section 10.1(a) .

(b) Purchaser shall promptly forward to Seller or reimburse Seller for any refunds or credits due to Seller (pursuant to the terms of this Article X ) after receipt thereof, and Seller shall promptly forward to Purchaser or reimburse Purchaser for any refunds or credits due Purchaser (pursuant to the terms of this Article X ) after receipt thereof.

Section 10.3 Cooperation . Each party hereto shall, and shall cause its Affiliates to, provide to the other party hereto such cooperation, documentation and information relating to the Purchased Assets as either of them reasonably may request in: (i) filing any Tax Return, amended Tax Return or claim for refund, (ii) determining a liability for Taxes or an indemnity obligation under this Article X or a right to refund of Taxes, (iii) conducting any audit, examination, contest, litigation or other proceeding by or against any Taxing Authority or (iv) determining an allocation of Taxes between a Pre-Closing Period and Post-Closing Period. Each party will retain all Tax Returns, schedules and work papers, and all material records and other documents relating to Taxes relating to the Purchased Assets for Tax periods ending on or prior to the Closing Date until the later of (x) the expiration of the statute of limitations for the Tax periods to which the Tax Returns or other documents relate or (y) eight (8) years following the

due date (without extension) for such Tax Returns. Thereafter, the party holding such Tax Returns or other documents may dispose of them after offering the other party reasonable notice and opportunity to take possession of such Tax Returns and other documents at such other party's own expense. Each party shall make its employees reasonably available on a mutually convenient basis at its cost to provide explanation of any documents or information so provided.

Section 10.4 Contest Provisions . Each of Purchaser and Seller shall promptly notify the other in writing upon receipt of notice of any pending or threatened audits or assessments with respect to Taxes for which such other party (or such other party's Affiliates) may be liable hereunder. Seller shall be entitled to participate at their expense in the defense of and, at its option, take control of the complete defense of, any Tax audit or administrative or court proceeding relating to Taxes for which it may be liable, and to employ counsel and other advisors of its choice at its expense. Neither party may agree to settle any claim for Taxes for which the other may be liable without the prior written consent of such other party, which consent shall not be unreasonably withheld.

Section 10.5 Transfer Taxes . (a) All Transfer Taxes that are payable or that arise as a result of the consummation of the purchase and sale of the Purchased Assets contemplated by this Agreement shall be paid by Seller. Any Tax Returns that must be filed in connection with Transfer Taxes shall be prepared and filed by the party primarily or customarily responsible under Applicable Law for filing such Tax Returns, and such party will use its reasonable best efforts to provide such Tax Returns to the other party at least ten (10) Business Days prior to the date such Tax Returns are due to be filed. Such Tax Returns shall be prepared consistent with the Allocation Statement pursuant to Section 3.4(a) . Purchaser and Seller shall cooperate in the timely completion and filing of all such Tax Returns. Seller shall promptly pay all Transfer Taxes due with respect to Tax Returns to be filed by Seller under this Section 10.5 and Seller shall pay to Purchaser any Transfer Taxes due with respect to Tax Returns to be filed by Purchaser under this Section 10.5 at least two (2) Business Days prior to the due date for the filing of such Tax Returns. Any Transfer Taxes resulting from any subsequent increase in consideration shall be borne in accordance with the provisions of this Section 10.5 and any Tax Returns required to be filed in connection therewith shall be prepared and filed in accordance with the provisions of this Section 10.5 . For the avoidance of doubt, any Transfer Taxes resulting from any transfer after the Closing Date of any Purchased Asset or Assumed Liability, or any other property owned after the Closing Date by Purchaser or any of its Affiliates shall be borne by Purchaser and any Tax Returns relating thereto shall be prepared and filed by Purchaser. Purchaser agrees to timely sign and deliver any certificates or forms as may be necessary or appropriate to establish an exemption from (or otherwise reduce), and file Tax Returns with respect to, such Transfer Taxes.

(b) The parties shall attempt in good faith to agree, on or prior to the Closing Date, on the fair market value of the Banking Center Premises and shall prepare and file any Tax Returns required to be filed by them with respect to Transfer Taxes on a basis consistent with any such agreed valuation.

(c) Any party shall have the right to seek a refund of any and all Transfer Taxes paid by it for which it is responsible pursuant to this Section 10.5 at its own expense (subject to the last sentence of this Section 10.5(c) ). If so requested, the other party shall

cooperate in good faith with the party seeking such refund. Any refund of Transfer Taxes (and any reasonable out-of-pocket expenses incurred by the parties in obtaining such refund, provided, in the case of fees and disbursements paid to any accounting firm, such expenses were incurred after providing reasonable advance notice to and consulting in good faith with the other party) shall be shared between the parties in accordance with the portion of such Tax paid by each such party.

Section 10.6 Coordination . Notwithstanding anything in this Agreement to the contrary, in the event there is a conflict between Article X and any provision contained in any other article of this Agreement, Article X shall control.

Section 10.7 Tax Treatment of Payments . Purchaser, Seller and its Affiliates shall treat any and all payments under this Article X or Article XIII as an adjustment to the consideration, for Tax purposes unless they are required to treat such payments otherwise by applicable Tax laws.

Section 10.8 Limitations and Survival . Notwithstanding anything in this Agreement to the contrary, the indemnification provisions of Section 10.1 are not subject to the limitations of Article XIII and shall survive the Closing until the expiration of the applicable statutes of limitation.

Section 10.9 No Double Recovery . For the avoidance of doubt, neither Purchaser nor Seller shall be entitled to receive indemnification from the other in respect of all or any portion of any Loss more than once, in each case, whether proceeding under this Article X or Article XIII .

## ARTICLE XI

## CLOSING CONDITIONS

Section 11.1 Conditions to Obligations of Each Party to Close . The respective obligations of each party to effect the transactions contemplated by this Agreement are subject to the satisfaction or, where legally permitted, waiver by such party, prior to or at the Closing, of each of the following conditions:

(a) No statute, rule, regulation, executive order, decree, ruling, permanent injunction or other permanent order shall have become effective (and final and nonappealable) permanently restraining, enjoining or otherwise prohibiting or making illegal the consummation of the transactions contemplated hereby.

(b) All Regulatory Approvals set forth on Schedule 11.1(b) (the " Required Government Approvals ") shall have been obtained, and any applicable waiting periods relating thereto shall have expired or been terminated early.

(c) the HSBC Assignment Agreement shall be in force and effect and shall not have been terminated.

Section 11.2 Conditions to Obligation of Seller to Effect the Closing . The obligation of Seller to effect the transactions contemplated by this Agreement is subject to the satisfaction or waiver (in the sole discretion of Seller), prior to or at the Closing, of each of the following conditions:

(a) All of the covenants and other agreements required by this Agreement to be complied with and performed by Purchaser on or before the Closing Date shall have been duly complied with and performed in all material respects.

(b) Each of the representations and warranties of Purchaser contained in Article VI shall be true and correct as of the Closing Date as though made on and as of the Closing Date, except (i) that those representations and warranties which address matters only as of a particular date shall be true and correct as of such particular date; and (ii) where the failure of such representations and warranties in the aggregate to be so true and correct has not had, and would not reasonably be expected to result in, a material adverse effect on Purchaser's ability to consummate the transactions contemplated by this Agreement (disregarding for purposes of this clause (ii) any qualification in the text of the relevant representation or warranty as to materiality, material adverse effect or Knowledge).

(c) Seller shall have received at the Closing a certificate dated the Closing Date and validly executed on behalf of Purchaser by an appropriate officer certifying that the conditions specified in Section 11.2(a) and Section 11.2(b) have been satisfied.

Section 11.3 Conditions to Obligation of Purchaser to Effect the Closing . Purchaser's obligation to effect the transactions contemplated by this Agreement is subject to the satisfaction or waiver (in Purchaser's sole discretion), prior to or at the Closing, of each of the following conditions:

(a) All of the covenants and agreements required by this Agreement to be complied with and performed by Seller on or before the Closing Date shall have been duly complied with and performed in all material respects.

(b) Each of the representations and warranties of Seller contained in Article V shall be true and correct as of the Closing Date as though made on and as of the Closing Date, except (i) that those representations and warranties which address matters only as of a particular date shall be true and correct as of such particular date; and (ii) where the failure of such representations and warranties in the aggregate to be so true and correct has not had, and would not reasonably be expected to result in, a Material Adverse Effect (disregarding for purposes of this clause (ii) any qualification in the text of the relevant representation or warranty as to materiality, Material Adverse Effect or Knowledge).

(c) Purchaser shall have received at the Closing a certificate dated the Closing Date and validly executed on behalf of Seller by an appropriate officer of Seller certifying that the conditions specified in Section 11.3(a) and Section 11.3(b) have been satisfied.

(d) No event shall have occurred and no facts or conditions shall exist that, individually or in the aggregate, have had, or would reasonably be expected to have, a Material Adverse Effect.

## ARTICLE XII

## TERMINATION

Section 12.1 Termination . This Agreement may be terminated at any time prior to the Closing Date:

(a) by mutual written consent of Purchaser and Seller;

(b) by Purchaser or Seller if (i) any Governmental Entity that must grant a Required Government Approval has denied such Required Government Approval, and such denial has become final and nonappealable or (ii) any Governmental Entity of competent jurisdiction shall have issued a final nonappealable order enjoining or otherwise prohibiting the consummation of the transactions contemplated by this Agreement, unless, in either case, such denial of approval or issuance of such order arises out of, or results from, a material breach by the party seeking to terminate this Agreement of any representation, warranty, covenant or agreement of such party in this Agreement;

(c) by Purchaser or by Seller, if the Closing shall not have occurred on or before the Outside Date; unless the failure of the Closing to occur by such date arises out of, or results from, a material breach by the parties seeking to terminate this Agreement of any representation, warranty, covenant or agreement of such parties in this Agreement;

(d)(i) by Purchaser, if Seller has breached any of its covenants or agreements or any of its representations or warranties contained in this Agreement, which breach, individually or in the aggregate, would cause the conditions set forth in Section 11.3(a) or Section 11.3(b) to be not satisfied, and such breach is not cured within forty-five (45) days following written notice to Seller or cannot, by its nature, be cured prior to the Outside Date; provided that Purchaser is not then in material breach of any representation, warranty, covenant or other agreement contained in this Agreement, or (ii) by Seller, if Purchaser has breached any of its covenants or agreements or any of its representations or warranties contained in this Agreement, which breach, individually or in the aggregate, would cause the conditions set forth in Section 11.2(a) or Section 11.2(b) to not be satisfied, and such breach is not cured within forty-five (45) days following written notice to Purchaser, or cannot, by its nature, be cured prior to the Outside Date; provided that Seller is not then in material breach of any representation, warranty, covenant or other agreement contained in this Agreement; and

(e) By Purchaser or Seller if the HSBC Assignment Agreement has been terminated.

Section 12.2 Effect of Termination . In the event of termination of this Agreement as provided in Section 12.1 , this Agreement shall forthwith become void and have no effect, and none of Seller, Purchaser, any of its Affiliates or any of the officers, directors or stockholders of any of them shall have any liability of any nature whatsoever hereunder, or in connection with the transactions contemplated hereby, except (i) the confidentiality provisions of Section 7.5 shall survive any termination of this Agreement, and (ii) notwithstanding anything to the contrary contained in this Agreement, neither Purchaser nor Seller shall be relieved or released from any liabilities or damages arising out of its willful breach of any provision of this Agreement.

## ARTICLE XIII

## SURVIVAL; INDEMNIFICATION

Section 13.1 Survival of Representations and Warranties . The representations and warranties contained in this Agreement shall survive the Closing for the period set forth in this Section 13.1 . All representations and warranties contained in this Agreement and all claims with respect thereto shall terminate eighteen (18) months after the Closing Date, except that (i) the representations and warranties contained in Sections 5.1 , 5.2 , 5.7 , 6.1 , 6.2 and 6.7 shall survive until the expiration of the applicable statute of limitations; it being understood that in the event notice of any claim for indemnification under this Article XIII has been given (within the meaning of Section 13.4 ) within the applicable survival period, the representations and warranties that are the subject of such indemnification claim shall survive with respect to such claim until such time as such claim is finally resolved. The agreements and covenants contained in this Agreement that by their terms contemplate performance after the Closing Date shall survive the Closing in accordance with their terms.

Section 13.2 Indemnification by Seller . (a) Seller hereby agrees that from and after the Closing it shall indemnify, defend and hold harmless Purchaser and its respective Affiliates, and its directors, officers, employees (other than the Transferred Banking Center Employees), agents and their heirs, successors and permitted assigns, each in their capacity as such (the " Purchaser Indemnified Parties " from, against and in respect of any damages, losses, charges, Liabilities, claims, demands, actions, suits, proceedings, payments, judgments, settlements, assessments, deficiencies, interest, penalties, and costs and expenses (including removal costs, remediation costs, closure costs, fines, penalties and expenses of investigation and ongoing monitoring, reasonable attorneys' fees, and reasonable out of pocket disbursements) (collectively, " Losses ") imposed on, sustained, incurred or suffered by, or asserted against, any of the Purchaser Indemnified Parties, whether in respect of third-party claims, claims between the parties hereto, or otherwise, directly or indirectly relating to, or arising out of:

(1) any breach of any representation or warranty made by Seller under Article V for the period such representation or warranty survives, it being understood that for purposes of this Section 13.2 any qualifications in the text of any such representation or warranty relating to materiality, Material Adverse Effect, or Knowledge shall be disregarded for purposes of determining whether such representation or warranty was breached or the amount of Losses;

(2) any breach of any covenant or agreement of Seller contained in this Agreement; and

(3) any of (i) the Excluded Liabilities, (ii) Liens that are not Permitted Liens, or (iii) the conduct of the Retained Business after the Closing Date.

(b) Seller shall not be liable to the Purchaser Indemnified Parties for (i) any Losses in respect of Section 13.2(a)(1) for any individual claim (or group of directly related claims) less than twenty thousand dollars ($20,000) (each a " de minimis loss ") or (ii) any Losses in respect of Section 13.2(a)(1) unless the Losses therefrom exceed an aggregate amount (including all Losses attributable to Seller) equal to two hundred fifty thousand dollars ($250,000), and then only for Losses in excess of that amount and up to an aggregate amount equal to twenty-five percent (25%) of the Premium.

Section 13.3 Indemnification by Purchaser . (a) Purchaser hereby agrees that from and after the Closing it shall indemnify, defend and hold harmless Seller, any of its Affiliates, and each of their respective directors, officers, agents and their heirs, successors and permitted assigns, each in their capacity as such (the " Seller Indemnified Parties " and collectively, with the Purchaser Indemnified Parties, the " Indemnified Parties ") from, against and in respect of any Losses imposed on, sustained, incurred or suffered by, or asserted against, any of the Seller Indemnified Parties, whether in respect of third-party claims, claims between the parties hereto, or otherwise, directly or indirectly, relating to, arising out of or resulting from:

(1) any breach of any representation or warranty made by Purchaser under Article VI for the period such representation or warranty survives, it being understood that for purposes of this Section 13.3 any qualifications in the text of any such representation or warranty relating to materiality, material adverse effect, or Knowledge shall be disregarded for purposes of determining whether such representation or warranty was breached;

(2) any breach of a covenant or agreement of Purchaser contained in this Agreement; and

(3) any of the Assumed Liabilities or the conduct of the Banking Centers after the Closing Date.

(b) Purchaser shall not be liable to the Seller Indemnified Parties for (i) a de minimis loss in respect of Section 13.3(a)(1) or (ii) any Losses with respect to the matters contained in Section 13.3(a)(1) unless the Losses therefrom exceed an aggregate amount (including all Losses attributable to Seller) equal to two hundred fifty thousand dollars ($250,000), and then only for Losses in excess of that amount and up to an aggregate amount equal to twenty-five percent (25%) of the Premium.

Section 13.4 Third-Party Claim Indemnification Procedures . (a) In the event that any written claim or demand for which an indemnifying party (an " Indemnifying Party ") may have liability to any Indemnified Party hereunder, other than those relating to Taxes (which are the exclusive subject of Article X ), is asserted against or sought to be collected from any Indemnified Party by a third party (a " Third-Party Claim "), such Indemnified Party shall promptly, but in no event more than ten (10) days following such Indemnified Party's receipt of a Third-Party Claim, notify the Indemnifying Party in writing of such Third-Party Claim, the amount or the estimated amount of damages sought thereunder to the extent then ascertainable (which estimate shall not be conclusive of the final amount of such Third-Party Claim), any other remedy sought thereunder, any relevant time constraints relating thereto and, to the extent

practicable, any other material details pertaining thereto (a " Claim Notice "); provided , however , that the failure timely to give a Claim Notice shall affect the rights of an Indemnified Party hereunder only to the extent that such failure has a material prejudicial effect on the defenses or other rights available to the Indemnifying Party with respect to such Third-Party Claim. The Indemnifying Party shall have thirty (30) days (or such lesser number of days set forth in the Claim Notice as may be required by court proceeding in the event of a litigated matter) after receipt of the Claim Notice (the " Notice Period ") to notify the Indemnified Party that it desires to assume the defense of the Indemnified Party against such Third-Party Claim.

(b) In the event that the Indemnifying Party notifies the Indemnified Party within the Notice Period that it desires to defend the Indemnified Party against a Third-Party Claim, the Indemnifying Party shall have the right to defend the Indemnified Party by appropriate proceedings and shall have the sole power to direct and control such defense at its expense. Once the Indemnifying Party has duly assumed the defense of a Third-Party Claim, the Indemnified Party shall have the right, but not the obligation, to participate in any such defense and to employ separate counsel of its choosing. The Indemnified Party shall participate in any such defense at its expense unless the Indemnifying Party and the Indemnified Party are both named parties to the proceedings and the Indemnified Party shall have reasonably concluded, based on the written advice of counsel, that representation of both parties by the same counsel would be inappropriate due to actual or potential differing material interests between them. The Indemnifying Party shall not, without the prior written consent of the Indemnified Party, settle, compromise or offer to settle or compromise any Third-Party Claim; provided , however , that no such prior written consent of the Indemnified Party shall be required to any proposed settlement that involves only the payment of money by the Indemnifying Party, includes as an unconditional term thereof the granting by the person asserting such claim or bringing such action of an unconditional release from liability to all Indemnified Parties with respect to such claim and does not include any admission of culpability.

(c) If the Indemnifying Party elects not to defend the Indemnified Party against a Third-Party Claim, whether by not giving the Indemnified Party timely notice of its desire to so defend or otherwise, the Indemnified Party shall have the right but not the obligation to assume its own defense; it being understood that the Indemnified Party's right to indemnification for a Third-Party Claim shall not be adversely affected by assuming the defense of such Third-Party Claim. The Indemnified Party shall not settle a Third-Party Claim without the consent of the Indemnifying Party and/or its respective insurer.

(d) The Indemnified Party and the Indemnifying Party shall cooperate in order to ensure the proper and adequate defense of a Third-Party Claim, including by providing access to each other's relevant business records and other documents, and employees.

(e) The Indemnified Party and the Indemnifying Party shall use reasonable best efforts to avoid production of confidential information (consistent with Applicable Law), and to cause all communications among employees, counsel and others representing any party to a Third-Party Claim to be made so as to preserve any applicable attorney-client or work-product privileges.

Section 13.5 Consequential Damages . Notwithstanding anything to the contrary contained in this Agreement, no Person shall be liable under this Article XIII for any consequential, punitive, special, incidental or indirect damages, including lost profits, except to the extent awarded by a court of competent jurisdiction in connection with a Third-Party Claim.

Section 13.6 Adjustments to Losses . (a) In calculating the amount of any Loss, the proceeds actually received by the Indemnified Party or any of its Affiliates under any insurance policy or pursuant to any claim, recovery, settlement or payment by or against any other Person in each case relating to the Third-Party Claim, net of any actual costs, expenses or premiums incurred in connection with securing or obtaining such proceeds, shall be deducted. Without limiting the generality or effect of any other provision hereof, each Indemnified Party and Indemnifying Party shall duly execute upon request all instruments reasonably necessary to evidence and perfect the subrogation and subordination rights detailed herein, and otherwise cooperate in the prosecution of such claims.

(b) In calculating the amount of any Loss, there shall be deducted an amount equal to any net Tax benefit actually realized (including the utilization of a Tax loss or Tax credit carried forward) as a result of such Loss by the party claiming such Loss, and there shall be added an amount equal to any actual net Tax detriment resulting from such Loss.

(c) Reimbursement . If an Indemnified Party recovers an amount from a third-party in respect of a Loss that is the subject of indemnification hereunder after all or a portion of such Loss has been paid by an Indemnifying Party pursuant to this Article XIII , the Indemnified Party shall promptly remit to the Indemnifying Party the excess (if any) of (i) the amount paid by the Indemnifying Party in respect of such Loss, plus the amount received from the third party in respect thereof, less (ii) the full amount of Loss.

Section 13.7 Payments . The Indemnifying Party shall pay all amounts payable pursuant to this Article XIII , by wire transfer of immediately available funds, promptly following receipt from an Indemnified Party of a bill, together with all accompanying reasonably detailed back-up documentation, for a Loss that is the subject of indemnification hereunder, unless the Indemnifying Party in good faith disputes the Loss, in which event it shall so notify the Indemnified Party. In any event, the Indemnifying Party shall pay to the Indemnified Party, by wire transfer of immediately available funds, the amount of any Loss for which it is liable hereunder no later than three (3) days following any final determination of such Loss and the Indemnifying Party's liability therefor. A "final determination" shall exist when (i) the parties to the dispute have reached an agreement in writing, (ii) a court of competent jurisdiction shall have entered a final and non-appealable order or judgment, or (iii) an arbitration or like panel shall have rendered a final non-appealable determination with respect to disputes the parties have agreed to submit thereto.

Section 13.8 Mitigation . Each Indemnified Party shall use its reasonable best efforts to mitigate any indemnifiable Loss. In the event an Indemnified Party fails to so mitigate an indemnifiable Loss, the Indemnifying Party shall have no liability for any portion of such Loss that reasonably could have been avoided had the Indemnified Person made such efforts.

Section 13.9 Survival of Indemnity . The obligation of Purchaser and Seller to indemnify under this Article XIII as to claims covered by Section 13.2(a)(1) and Section 13.3(a)(1) , as applicable, shall expire on the applicable expiration date of the applicable representation or warranty, as provided in Section 13.1 , and shall not apply to any claims made after such date, except that the obligation of Purchaser and Seller to indemnify with respect to bona fide claims for indemnity made in writing by Seller Indemnified Parties and Purchaser Indemnified Parties, as applicable, prior to such expiration shall continue until final resolution of such claims.

Section 13.10 Remedies Exclusive . Except as otherwise specifically provided herein or in the case of fraud or willful misconduct, the remedies provided in this Article XIII shall be the exclusive remedies of the parties hereto from and after the Closing in connection with any breach of a representation or warranty, or non-performance, partial or total, of any covenant or agreement contained herein except as to Taxes, as to which the provisions of Article X shall control exclusively.

## ARTICLE XIV

## MISCELLANEOUS

Section 14.1 Entire Agreement; Amendment . All Exhibits (attached hereto and as executed) and Schedules hereto shall be deemed to be incorporated into and made part of this Agreement. This Agreement, together with the Exhibits and Schedules hereto, and the Transition Services Agreement, contain the entire agreement and understanding among the parties with respect to the subject matter hereof (and supersede any prior agreements, arrangements or understandings among the parties with respect to the subject matter hereof) and there are no agreements, representations, or warranties which are not set forth herein. This Agreement may not be amended or revised except by a writing signed by Seller and Purchaser.

Section 14.2 Binding Effect; Assignment; No Third-Party Beneficiaries . Except as otherwise provided in this Agreement, this Agreement shall be binding upon and inure to the benefit of the parties hereto and its successors and assigns. Except as expressly provided herein, this Agreement and all rights hereunder may not be assigned by any party hereto except by prior written consent of the other party hereto; provided that Purchaser may assign its right to acquire any asset and/or the obligation to pay all or part of the consideration and to assume any liability to any wholly owned Subsidiary without the prior written consent of the other party hereto; provided , further, that Purchaser agrees to guarantee the performance of any such wholly owned Subsidiary. The parties intend that this Agreement shall not benefit or create any right or cause of action in or on behalf of any Person other than the parties hereto; provided that the provisions of Article XIII will inure to the benefit of the Indemnified Parties.

Section 14.3 Specific Performance . The parties hereto acknowledge and agree that (i) monetary damages could not adequately compensate any party hereto in the event of a breach of this Agreement by any other party which results in the failure of the transactions contemplated by this Agreement to be consummated by the Outside Date; (ii) the non-breaching party would suffer irreparable harm in the event of such a breach with such an effect; and (iii) the non-breaching party shall have, in addition to any other rights or remedies it may have at law or

in equity, specific performance and injunctive relief as a remedy for the enforcement hereof. The parties agree to not seek, and agree to waive, any requirement for the securing or posting of a bond in connection with a party seeking or obtaining any relief pursuant to this Section 14.3 .

Section 14.4 Counterparts . This Agreement may be executed in any number of counterparts, each of which shall be deemed to be an original as against any party whose signature appears thereon, and all of which shall together constitute one and the same instrument. This Agreement shall become binding when two or more counterparts hereof, individually or taken together, shall bear the signatures of all of the parties reflected hereon as the signatories. The execution and delivery of this Agreement may be effected by facsimile or any other electronic means such as ".pdf" or ".tiff" files.

Section 14.5 Notices . All notices, request, demands and other communications required hereunder shall be in writing and shall be deemed to have been duly given or made if delivered personally, sent by facsimile transmission or telex confirmed in writing within two (2) Business Days, or sent by registered or certified mail, postage prepaid, as follows:

If to Purchaser addressed to:

Peter G. Humphrey
President and Chief Executive Officer
Five Star Bank
220 Liberty Street
Warsaw, NY 14569
Facsimile: (585) 786-1108

with a copy to:

John L. Rizzo
General Counsel
Five Star Bank
220 Liberty Street
Warsaw, NY 14569
Facsimile: (585) 786-1108

with an additional copy to:

James M. Jenkins, Esq.
Harter Secrest & Emery LLP
1600 Bausch & Lomb Place
Rochester, NY 14604
Facsimile: (585) 232-6500

and if to Seller addressed to:

Oliver H. Sommer
Executive Vice President, Corporate Development
First Niagara Financial Group, Inc.
726 Exchange Street, Suite 618
Buffalo, NY 14210
Facsimile: (716) 819-5157

with a copy to:

John Mineo
SVP, General Counsel & Corporate Secretary
First Niagara Financial Group, Inc.
726 Exchange Street, Suite 618
Buffalo, NY 14210
Facsimile: (716) 819-5158

with an additional copy to:

Michael Friedman, Esq.
Pepper Hamilton LLP
3000 Two Logan Square
Eighteenth and Arch Streets
Philadelphia, PA 19103-2799
Facsimile: (215) 981-4750

Any party may change the address or fax number to which such communications are to be sent to it by giving written notice of change of address to the other party in the manner provided above for giving notice.

Section 14.6 Provisions Separable . The provisions of this Agreement are independent of and separable from each other, and no provision shall be affected or rendered invalid or unenforceable by virtue of the fact that for any reason any other or others of them may be invalid or unenforceable in whole or in part.

Section 14.7 Expenses . Except as otherwise expressly set forth herein, all fees and expenses payable in connection with the consummation of the transactions contemplated by this Agreement shall be the sole liability of the party incurring such expense.

Section 14.8 Deadlines . If the last day of the time period for the giving of any notice or the taking of any action required under this Agreement falls on a Saturday, Sunday or legal holiday or a date on which banks in the State of New York are authorized by law to close, the time period for giving such notice or taking such action shall be extended through the next Business Day following the original expiration date of such.

Section 14.9 Scope of Agreements . This Agreement shall not create any partnership, joint venture or other similar arrangement between Seller or any of its Affiliates, on the one hand, and Purchaser or any of its Affiliates, on the other hand.

Section 14.10 Delays or Omissions . Any waiver, permit, consent or approval of any kind or character of any breach or default under this Agreement, or any waiver of any provision or condition of this Agreement shall be effective only to the extent specifically set forth in writing. Notwithstanding any provision set forth herein, no party hereto shall be required to take any action or refrain from taking any action that would cause it to violate any Applicable Law, statute, legal restriction, regulation, rule or order or any Governmental Entity.

Section 14.11 Waiver of Jury Trial . EACH PARTY HERETO HEREBY WAIVES TRIAL BY JURY IN ANY ACTION, PROCEEDING OR COUNTERCLAIM BROUGHT BY ANY OF THEM AGAINST THE OTHER ARISING OUT OF OR IN ANY WAY CONNECTED WITH THIS AGREEMENT, OR ANY OTHER AGREEMENTS EXECUTED IN CONNECTION HEREWITH, OR THE ADMINISTRATION THEREOF OR ANY OF THE TRANSACTIONS CONTEMPLATED HEREIN OR THEREIN. NO PARTY TO THIS AGREEMENT SHALL SEEK A JURY TRIAL IN ANY LAWSUIT, PROCEEDING, COUNTERCLAIM, OR ANY OTHER LITIGATION PROCEDURE BASED UPON, OR ARISING OUT OF, THIS AGREEMENT OR ANY RELATED INSTRUMENTS OR THE RELATIONSHIP BETWEEN THE PARTIES. NO PARTY WILL SEEK TO CONSOLIDATE ANY SUCH ACTION, IN WHICH A JURY TRIAL HAS BEEN WAIVED, WITH ANY OTHER ACTION IN WHICH A JURY TRIAL CANNOT BE OR HAS NOT BEEN WAIVED. THE PROVISIONS OF THIS SECTION HAVE BEEN FULLY DISCUSSED BY THE PARTIES HERETO, AND THESE PROVISIONS SHALL BE SUBJECT TO NO EXCEPTIONS. NO PARTY HAS IN ANY WAY AGREED WITH OR REPRESENTED TO ANY OTHER PARTY THAT THE PROVISIONS OF THIS SECTION WILL NOT BE FULLY ENFORCED IN ALL INSTANCES.

Section 14.12 Governing Law; Consent to Jurisdiction . The execution, interpretation, and performance of this Agreement shall be governed by the laws of the State of New York without giving effect to any conflict of laws provision or rule (whether of the State of New York or any other jurisdiction) that would cause the application of the law of any other jurisdiction other than the State of New York. EACH PARTY HERETO, TO THE EXTENT IT MAY LAWFULLY DO SO, HEREBY SUBMITS TO THE JURISDICTION OF ANY COURT OF THE STATE OF NEW YORK LOCATED IN THE BOROUGH OF MANHATTAN IN NEW YORK CITY AND THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK, AS WELL AS TO THE JURISDICTION OF ALL COURTS FROM WHICH AN APPEAL MAY BE TAKEN OR OTHER REVIEW SOUGHT FROM THE AFORESAID COURTS, FOR THE PURPOSE OF ANY SUIT, ACTION OR OTHER PROCEEDING ARISING OUT OF SUCH PARTY'S OBLIGATIONS UNDER OR WITH RESPECT TO THIS AGREEMENT OR ANY OF THE AGREEMENTS, INSTRUMENTS OR DOCUMENTS CONTEMPLATED HEREBY AND EXPRESSLY WAIVES ANY AND ALL OBJECTIONS IT MAY HAVE AS TO VENUE IN ANY OF SUCH COURTS.

[ *Remainder of page left intentionally blank* ]

IN WITNESS WHEREOF, each of the parties hereto has caused this Purchase and Assumption Agreement to be duly executed as an instrument under seal by its officer thereunto duly authorized as of the date first above written.

FIRST NIAGARA BANK, NATIONAL ASSOCIATION

By: _____
Name:
Title:

FIVE STAR BANK

By: _____
Name:
Title:

*[Signature Page to Purchase and Assumption Agreement]*

**Exhibit 21**

## SUBSIDIARIES OF REGISTRANT

| Name | State or Jurisdiction of Incorporation or Organization |
|---|---|
| Five Star Bank | New York |
| Five Star Investment Services, Inc. | New York |

**Exhibit 23**

**Consent of Independent Registered Public Accounting Firm**

The Board of Directors and Shareholders
Financial Institutions, Inc.:

We consent to incorporation by reference in the Registration Statements No. 333-40544, 333-87338, 333-172651 and 333-176522 on Form S-8 and Registration Statements No. 333-156855 and 333-160843 on Form S-3 of Financial Institutions, Inc. of our reports, dated March 9, 2012, relating to the consolidated statements of financial condition of Financial Institutions, Inc. and subsidiaries (the Company) as of December 31, 2011 and 2010, and the related consolidated statements of income, changes in shareholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2011 , and the effectiveness of internal control over financial reporting as of December 31, 2011, which reports appear in the December 31, 2011 annual report on Form 10-K of Financial Institutions, Inc.

***/s/ KPMG LLP***

Rochester, New York
March 9, 2012

**Exhibit 31.1**

**Certification of Principal Executive Officer**
**Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Peter G. Humphrey, certify that:

1. I have reviewed this annual report on Form 10-K of Financial Institutions, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 9, 2012

***/s/ Peter G. Humphrey***
Peter G. Humphrey
President and Chief Executive Officer

**Exhibit 31.2**

**Certification of Principal Financial Officer**
**Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Karl F. Krebs, certify that:

1. I have reviewed this annual report on Form 10-K of Financial Institutions, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 9, 2012

***/s/ Karl F. Krebs***
Karl F. Krebs
Chief Financial Officer

**Exhibit 32**

**Certification pursuant to**
**18 U.S.C. Section 1350,**
**as adopted pursuant to**
**Section 906 of the Sarbanes-Oxley Act of 2002**

Peter G. Humphrey, President and Chief Executive Officer, and Karl F. Krebs, Chief Financial Officer of Financial Institutions, Inc. (the "Company"), each certify in his capacity as an officer of the Company that he has reviewed the Annual Report of the Company on Form 10-K for the period ended December 31, 2011 and that to the best of his knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 9, 2012

***/s/ Peter G. Humphrey***
Peter G. Humphrey
President and Chief Executive Officer
(Principal Executive Officer)

Date: March 9, 2012

***/s/ Karl F. Krebs***
Karl F. Krebs
Chief Financial Officer
(Principal Financial Officer)

The purpose of this statement is solely to comply with Title 18, Chapter 63, Section 1350 of the United States Code, as amended by Section 906 of the Sarbanes-Oxley Act of 2002. A signed original of this written statement required by Section 906 has been provided to Financial Institutions, Inc. and will be retained by Financial Institutions, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.

**Exhibit 99.1**

**Certification pursuant to 31 C.F.R. § 30.15**

I, Peter G. Humphrey, certify, based on my knowledge, that:

(i) The compensation committee of Financial Institutions, Inc. has discussed, reviewed and evaluated with senior risk officers at least every six months during any part of the most recently completed fiscal year that was a TARP period, senior executive officer (SEO) compensation plans and employee compensation plans and the risks these plans pose to Financial Institutions, Inc.;

(ii) The compensation committee of Financial Institutions, Inc. has identified and limited during any part of the most recently completed fiscal year that was a TARP period any features of the SEO compensation plans that could lead SEOs to take unnecessary and excessive risks that could threaten the value of Financial Institutions, Inc. and has identified any features of the employee compensation plans that pose risks to Financial Institutions, Inc. and has limited those features to ensure that Financial Institutions, Inc. is not unnecessarily exposed to risks;

(iii) The compensation committee has reviewed, at least every six months during any part of the most recently completed fiscal year that was a TARP period, the terms of each employee compensation plan and identified any features of the plan that could encourage the manipulation of reported earnings of Financial Institutions, Inc. to enhance the compensation of an employee, and has limited any such features;

(iv) The compensation committee of Financial Institutions, Inc. will certify to the reviews of the SEO compensation plans and employee compensation plans required under (i) and (iii) above;

(v) The compensation committee of Financial Institutions, Inc. will provide a narrative description of how it limited during any part of the most recently completed fiscal year that included a TARP period the features in

(A) SEO compensation plans that could lead SEOs to take unnecessary and excessive risks that could threaten the value of Financial Institutions, Inc.;

(B) Employee compensation plans that unnecessarily expose Financial Institutions, Inc. to risks; and

(C) Employee compensation plans that could encourage the manipulation of reported earnings of Financial Institutions, Inc. to enhance the compensation of an employee;

(vi) Financial Institutions, Inc. has required that bonus payments, as defined in the regulations and guidance established under section 111 of EESA (bonus payments), of SEOs and twenty next most highly compensated employees be subject to a recovery or “clawback” provision during any part of the most recently completed fiscal year that was a TARP period if the bonus payments were based on materially inaccurate financial statements or any other materially inaccurate performance metric criteria;

(vii) Financial Institutions, Inc. has prohibited any golden parachute payment, as defined in the regulations and guidance established under section 111 of EESA, to a SEO or any of the next five most highly compensated employees during any part of the most recently completed fiscal year that was a TARP period;

(viii) Financial Institutions, Inc. has limited bonus payments to its applicable employees in accordance with Section 111 of EESA and the regulations and guidance established thereunder during any part of the most recently completed fiscal year that was a TARP period;

(ix) Financial Institutions, Inc. and its employees have complied with the excessive or luxury expenditures policy, as defined in the regulations and guidance established under section 111 of EESA, during any part of the most recently completed fiscal year that was a TARP period; and any expenses that, pursuant to this policy, required approval of the board of directors, a committee of the board of directors, an SEO, or an executive officer with a similar level of responsibility were properly approved;

(x) Financial Institutions, Inc. will permit a non-binding shareholder resolution in compliance with any applicable Federal securities rules and regulations on the disclosures provided under the Federal securities laws related to SEO compensation paid or accrued during any part of the most recently completed fiscal year that was a TARP period;

(xi) Financial Institutions, Inc. will disclose the amount, nature, and justification for the offering, during any part of the most recently completed fiscal year that was a TARP period, of any perquisites, as defined in the regulations and guidance established under section 111 of EESA, whose total value exceeds $25,000 for any employee who is subject to the bonus payment limitations identified in paragraph (viii);

(xii) Financial Institutions, Inc. will disclose whether Financial Institutions, Inc., the board of directors of Financial Institutions, Inc., or the compensation committee of Financial Institutions, Inc. has engaged during any part of the most recently completed fiscal year that was a TARP period a compensation consultant; and the services the compensation consultant or any affiliate of the compensation consultant provided during this period;

(xiii) Financial Institutions, Inc. has prohibited the payment of any gross-ups, as defined in the regulations and guidance established under section 111 of EESA, to the SEOs and the next twenty most highly compensated employees during any part of the most recently completed fiscal year that was a TARP period;

(xiv) Financial Institutions, Inc. has substantially complied with all other requirements related to employee compensation that are provided in the agreement between Financial Institutions, Inc. and Treasury, including any amendments;

(xv) Financial Institutions, Inc. has submitted to Treasury a complete and accurate list of the SEOs and the twenty next most highly compensated employees for the current fiscal year, with the non-SEOs ranked in descending order of level of annual compensation, and with the name, title, and employer of each SEO and the most highly compensated employee identified; and

(xvi) I understand that a knowing and willful false or fraudulent statement made in connection with this certification may be punished by fine, imprisonment, or both.

Date: March 9, 2012

***/s/ Peter G. Humphrey***
Peter G. Humphrey
President and Chief Executive Officer

**Exhibit 99.2**

**Certification pursuant to 31 C.F.R. § 30.15**

I, Karl F. Krebs, certify, based on my knowledge, that:

(i) The compensation committee of Financial Institutions, Inc. has discussed, reviewed and evaluated with senior risk officers at least every six months during any part of the most recently completed fiscal year that was a TARP period, senior executive officer (SEO) compensation plans and employee compensation plans and the risks these plans pose to Financial Institutions, Inc.;

(ii) The compensation committee of Financial Institutions, Inc. has identified and limited during any part of the most recently completed fiscal year that was a TARP period any features of the SEO compensation plans that could lead SEOs to take unnecessary and excessive risks that could threaten the value of Financial Institutions, Inc. and has identified any features of the employee compensation plans that pose risks to Financial Institutions, Inc. and has limited those features to ensure that Financial Institutions, Inc. is not unnecessarily exposed to risks;

(iii) The compensation committee has reviewed, at least every six months during any part of the most recently completed fiscal year that was a TARP period, the terms of each employee compensation plan and identified any features of the plan that could encourage the manipulation of reported earnings of Financial Institutions, Inc. to enhance the compensation of an employee, and has limited any such features;

(iv) The compensation committee of Financial Institutions, Inc. will certify to the reviews of the SEO compensation plans and employee compensation plans required under (i) and (iii) above;

(v) The compensation committee of Financial Institutions, Inc. will provide a narrative description of how it limited during any part of the most recently completed fiscal year that included a TARP period the features in

(A) SEO compensation plans that could lead SEOs to take unnecessary and excessive risks that could threaten the value of Financial Institutions, Inc.;

(B) Employee compensation plans that unnecessarily expose Financial Institutions, Inc. to risks; and

(C) Employee compensation plans that could encourage the manipulation of reported earnings of Financial Institutions, Inc. to enhance the compensation of an employee;

(vi) Financial Institutions, Inc. has required that bonus payments, as defined in the regulations and guidance established under section 111 of EESA (bonus payments), of SEOs and twenty next most highly compensated employees be subject to a recovery or “clawback” provision during any part of the most recently completed fiscal year that was a TARP period if the bonus payments were based on materially inaccurate financial statements or any other materially inaccurate performance metric criteria;

(vii) Financial Institutions, Inc. has prohibited any golden parachute payment, as defined in the regulations and guidance established under section 111 of EESA, to a SEO or any of the next five most highly compensated employees during any part of the most recently completed fiscal year that was a TARP period;

(viii) Financial Institutions, Inc. has limited bonus payments to its applicable employees in accordance with Section 111 of EESA and the regulations and guidance established thereunder during any part of the most recently completed fiscal year that was a TARP period;

(ix) Financial Institutions, Inc. and its employees have complied with the excessive or luxury expenditures policy, as defined in the regulations and guidance established under section 111 of EESA, during any part of the most recently completed fiscal year that was a TARP period; and any expenses that, pursuant to this policy, required approval of the board of directors, a committee of the board of directors, an SEO, or an executive officer with a similar level of responsibility were properly approved;

(x) Financial Institutions, Inc. will permit a non-binding shareholder resolution in compliance with any applicable Federal securities rules and regulations on the disclosures provided under the Federal securities laws related to SEO compensation paid or accrued during any part of the most recently completed fiscal year that was a TARP period;

(xi) Financial Institutions, Inc. will disclose the amount, nature, and justification for the offering, during any part of the most recently completed fiscal year that was a TARP period, of any perquisites, as defined in the regulations and guidance established under section 111 of EESA, whose total value exceeds $25,000 for any employee who is subject to the bonus payment limitations identified in paragraph (viii);

(xii) Financial Institutions, Inc. will disclose whether Financial Institutions, Inc., the board of directors of Financial Institutions, Inc., or the compensation committee of Financial Institutions, Inc. has engaged during any part of the most recently completed fiscal year that was a TARP period a compensation consultant; and the services the compensation consultant or any affiliate of the compensation consultant provided during this period;

(xiii) Financial Institutions, Inc. has prohibited the payment of any gross-ups, as defined in the regulations and guidance established under section 111 of EESA, to the SEOs and the next twenty most highly compensated employees during any part of the most recently completed fiscal year that was a TARP period;

(xiv) Financial Institutions, Inc. has substantially complied with all other requirements related to employee compensation that are provided in the agreement between Financial Institutions, Inc. and Treasury, including any amendments;

(xv) Financial Institutions, Inc. has submitted to Treasury a complete and accurate list of the SEOs and the twenty next most highly compensated employees for the current fiscal year, with the non-SEOs ranked in descending order of level of annual compensation, and with the name, title, and employer of each SEO and the most highly compensated employee identified; and

(xvi) I understand that a knowing and willful false or fraudulent statement made in connection with this certification may be punished by fine, imprisonment, or both.

Date: March 9, 2012

***/s/ Karl F. Krebs***
Karl F. Krebs
Chief Financial Officer