OFG BANCORP
Form 10-Q
November 04, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2016

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 001-12647

OFG Bancorp

Incorporated in the Commonwealth of Puerto Rico, IRS Employer Identification No. 66-0538893

Principal Executive Offices:

254 Muñoz Rivera Avenue

San Juan, Puerto Rico 00918

Telephone Number: (787) 771-6800

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes 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 whether the registrant 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 ý Non-Accelerated Filer Smaller Reporting Company
(Do not check if a 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

Number of shares outstanding of the registrant’s common stock, as of the latest practicable date:

43,913,719 common shares ($1.00 par value per share) outstanding as of October 31, 2016

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FORWARD-LOOKING STATEMENTS

The information included in this quarterly report on Form 10-Q contains certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements may relate to the financial condition, results of operations, plans, objectives, future performance and business of OFG Bancorp ("we," "our," "us" or the "Company"), including, but not limited to, statements with respect to the adequacy of the allowance for loan losses, delinquency trends, market risk and the impact of interest rate changes, capital markets conditions, capital adequacy and liquidity, and the effect of legal proceedings and new accounting standards on the Company's financial condition and results of operations. All statements contained herein that are not clearly historical in nature are forward-looking, and the words "anticipate," "believe," "continues," "expect," "estimate," "intend," "project" and similar expr and future or conditional verbs such as "will," "would," "should," "could," "might," "can," "may," or similar expressions are generally intended to identify forward-looking statements.

These statements are not guarantees of future performance and involve certain risks, uncertainties, estimates and assumptions by management that are difficult to predict. Various factors, some of which by their nature are beyond the Company's control, could cause actual results to differ materially from those expressed in, or implied by, such forward-looking statements. Factors that might cause such a difference include, but are not limited to:

- additional credit defaults or a restructuring by the Commonwealth of Puerto Rico or any of its agencies, municipalities or instrumentalities;
- possible legislative, tax or regulatory changes;
- the rate of growth in the economy and employment levels, as well as general business and economic conditions;
- the relative strength or weakness of the consumer and commercial credit sectors and of the real estate market in

Puerto Rico;

- competition in the financial services industry;
- the fiscal and monetary policies of the federal government and its agencies;
- changes in interest rates, as well as the magnitude of such changes;
- changes in federal bank regulatory and supervisory policies, including required levels of capital;
- the impact of the industry regulations on the Company's businesses, business practices and cost of operations;
- the performance of the securities markets; and
- additional Federal Deposit Insurance Corporation ("FDIC") assessments.

Other possible events or factors that could cause results or performance to differ materially from those expressed in these forward-looking statements include the following: negative economic conditions that adversely affect the general economy, housing prices, the job market, consumer confidence and spending habits which may affect, among other things, the level of non-performing assets, charge-offs and provision expense; changes in interest rates and market liquidity which may reduce interest margins, impact funding sources and affect the ability to originate and distribute financial products in the primary and secondary markets; adverse movements and volatility in debt and equity capital markets; changes in market rates and prices which may adversely impact the value of financial assets and liabilities; liabilities resulting from litigation and regulatory investigations; changes in accounting standards, rules and interpretations; increased competition; the Company's ability to grow its core businesses; decisions to downsize, sell or close units or otherwise change the Company's business mix; and management's ability to identify and manage these and other risks.

All forward-looking statements included in this quarterly report on Form 10-Q are based upon information available to the Company as of the date of this report, and other than as required by law, including the requirements of applicable securities laws, the Company assumes no obligation to update or revise any such forward-looking statements to reflect occurrences or unanticipated events or circumstances after the date of such statements.

ITEM 1. *FINANCIAL STATEMENTS*

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

AS OF SEPTEMBER 30, 2016 AND DECEMBER 31, 2015

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ASSETS	
Cash and cash equivalents:	
Cash and due from banks	$
Money market investments	
Total cash and cash equivalents	
Restricted cash	
Investments:	
Trading securities, at fair value, with amortized cost of $667 (December 31, 2015 - $667)	
Investment securities available-for-sale, at fair value, with amortized cost of $623,994 (December 31, 2015 - $955,646)	
Investment securities held-to-maturity, at amortized cost, with fair value of $650,023 (December 31, 2015 - $614,679)	
Federal Home Loan Bank (FHLB) stock, at cost	
Other investments	
Total investments	
Loans:	
Mortgage loans held-for-sale, at lower of cost or fair value	
Other loans held-for-sale, at lower of cost or fair value	
Loans, net of allowance for loan and lease losses of $119,012 (December 31, 2015 - $234,132)	
Total loans	
Other assets:	
FDIC indemnification asset	
Foreclosed real estate	
Accrued interest receivable	
Deferred tax asset, net	
Premises and equipment, net	
Customers' liability on acceptances	
Servicing assets	
Derivative assets	
Goodwill	
Other assets	
Total assets	$
LIABILITIES AND STOCKHOLDERS' EQUITY	
Deposits:	
Demand deposits	$
Savings accounts	
Time deposits	
Total deposits	
Borrowings:	
Securities sold under agreements to repurchase	
Advances from FHLB	
Subordinated capital notes	
Other borrowings	

Total borrowings	
Other liabilities:	
Derivative liabilities	
Acceptances executed and outstanding	
Accrued expenses and other liabilities	
Total liabilities	
Commitments and contingencies (See Note 19)	
Stockholders' equity:	
Preferred stock; 10,000,000 shares authorized;	
1,340,000 shares of Series A, 1,380,000 shares of Series B, and 960,000 shares of Series D issued and outstanding, (December 31, 2015 - 1,340,000 shares; 1,380,000 shares; and 960,000 shares) $25 liquidation value	
84,000 shares of Series C issued and outstanding (December 31, 2015 - 84,000 shares); $1,000 liquidation value	
Common stock, $1 par value; 100,000,000 shares authorized; 52,625,869 shares issued; 43,913,719 shares outstanding (December 31, 2015 - 52,625,869; 43,867,909)	
Additional paid-in capital	
Legal surplus	
Retained earnings	
Treasury stock, at cost, 8,712,150 shares (December 31, 2015 - 8,757,960 shares)	
Accumulated other comprehensive income, net of tax of $43 (December 31, 2015 - $1,182)	
Total stockholders' equity	
Total liabilities and stockholders' equity	$

See notes to unaudited consolidated financial statements

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS

FOR THE QUARTERS AND NINE-MONTH PERIODS ENDED SEPTEMBER 30, 2016 AND 2015

	Quarter Ended September 30,		Nine-Month Period Ended September 30,	
	2016	2015	2016	2015
	(In thousands, except per share data)			
Interest income:				
Loans	$ 82,604	$ 97,264	$ 243,431	$ 285,251
Mortgage-backed securities	6,997	9,137	23,215	25,724
Investment securities and other	983	846	3,152	2,686
Total interest income	**90,584**	**107,247**	**269,798**	**313,661**
Interest expense:				
Deposits	7,331	6,651	21,822	20,359
Securities sold under agreements to repurchase	4,272	7,605	14,629	22,163
Advances from FHLB and other borrowings	1,237	2,283	5,574	6,766
Subordinated capital notes	817	885	2,559	2,623
Total interest expense	**13,657**	**17,424**	**44,584**	**51,911**
Net interest income	**76,927**	**89,823**	**225,214**	**261,750**
Provision for loan and lease losses, net	23,469	51,579	51,703	109,311
Net interest income after provision for loan and lease losses	**53,458**	**38,244**	**173,511**	**152,439**
Non-interest income:				
Banking service revenue	10,330	10,826	30,667	31,243
Wealth management revenue	6,526	6,885	19,719	21,325
Mortgage banking activities	1,421	992	3,300	4,717
Total banking and financial service revenues	**18,277**	**18,703**	**53,686**	**57,285**
Net impairment losses recognized in earnings	-	(246)	-	(246)
FDIC shared-loss expense, net	(3,296)	(2,079)	(10,745)	(38,408)
Reimbursement from FDIC shared-loss coverage in sale of loans	-	20,000	-	20,000
Net gain (loss) on:				
Sale of securities	-	-	12,207	2,572
Derivatives	17	(208)	4	(223)
Early extinguishment of debt	-	-	(12,000)	-
Other non-interest income (loss)	5,217	(193)	5,721	(2,778)
Total non-interest income, net	**20,215**	**35,977**	**48,873**	**38,202**
Non-interest expense:				
Compensation and employee benefits	19,191	21,015	58,006	60,455
Professional and service fees	3,744	4,000	10,881	12,324
Occupancy and equipment	7,484	8,556	23,413	26,075
Insurance	1,242	2,263	7,547	6,467
Electronic banking charges	5,077	5,496	15,613	16,714
Information technology expenses	1,862	1,364	5,124	4,360
Advertising, business promotion, and strategic initiatives	1,347	1,577	4,133	4,763
Foreclosure, repossession and other real estate expenses	5,279	16,601	13,250	32,384
Loan servicing and clearing expenses	2,804	1,976	6,811	6,923

Taxes, other than payroll and income taxes	2,385	2,649	7,386	6,831
Communication	617	774	2,017	2,234
Printing, postage, stationary and supplies	602	624	1,927	1,842
Director and investor relations	233	246	812	829
Other	3,059	1,949	6,688	7,658
Total non-interest expense	**54,926**	**69,090**	**163,608**	**189,859**
Income before income taxes	**18,747**	**5,131**	**58,776**	**782**
Income tax expense	3,627	562	15,146	2,310
Net income (loss)	**15,120**	**4,569**	**43,630**	**(1,528)**
Less: dividends on preferred stock	(3,465)	(3,465)	(10,396)	(10,396)
Net income (loss) available to common shareholders	**$ 11,655**	**$ 1,104**	**$ 33,234**	**$ (11,924)**
Earnings (loss) per common share:				
Basic	**$ 0.27**	**$ 0.03**	**$ 0.76**	**(0.27)**
Diluted	**$ 0.26**	**$ 0.03**	**$ 0.76**	**(0.27)**
Average common shares outstanding and equivalents	**51,111**	**51,146**	**51,091**	**51,609**
Cash dividends per share of common stock	**$ 0.06**	**$ 0.10**	**$ 0.18**	**0.30**

See notes to unaudited consolidated financial statements

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OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

FOR THE QUARTERS AND NINE-MONTH PERIODS ENDED SEPTEMBER 30, 2016 AND 2015

	Quarter Ended September 30,		Nine-Month Period Ended September 30,	
	2016	2015	2016	2015
	(In thousands)		(In thousands)	
Net income (loss)	**$ 15,120**	**$ 4,569**	**$ 43,630**	**$ (1,528)**
Other comprehensive income (loss) before tax:				
Unrealized gain (loss) on securities available-for-sale	(315)	3,958	12,049	(1,582)
Realized gain on investment securities included in net loss	-	-	(12,207)	(2,572)
Other-than-temporary impairment included in net income	-	246	-	246
Unrealized gain on cash flow hedges	853	119	1,504	2,190
Other comprehensive income (loss) before taxes	**538**	**4,323**	**1,346**	**(1,718)**
Income tax effect	(499)	(468)	501	163
Other comprehensive income (loss) after taxes	**39**	**3,855**	**1,847**	**(1,555)**
Comprehensive income (loss)	**$ 15,159**	**$ 8,424**	**$ 45,477**	**$ (3,083)**

See notes to unaudited consolidated financial statements

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

FOR THE NINE-MONTH PERIODS ENDED SEPTEMBER 30, 2016 AND 2015

	Nine-Month Period Ended September 30,	
	2016	2015
	(In thousands)	
Preferred stock:		
Balance at beginning of period	$ 176,000	$ 176,000
Balance at end of period	**176,000**	**176,000**
Common stock:		
Balance at beginning of period	52,626	52,626
Balance at end of period	**52,626**	**52,626**
Additional paid-in capital:		
Balance at beginning of period	540,512	539,311
Stock-based compensation expense	1,014	1,213
Lapsed restricted stock units	(834)	(436)
Balance at end of period	**540,692**	**540,088**
Legal surplus:		
Balance at beginning of period	70,435	70,467
Transfer from (to) retained earnings	4,353	(44)
Balance at end of period	**74,788**	**70,423**
Retained earnings:		
Balance at beginning of period	148,886	181,152
Net income (loss)	43,630	(1,528)
Cash dividends declared on common stock	(7,909)	(13,298)
Cash dividends declared on preferred stock	(10,396)	(10,396)
Transfer (to) from legal surplus	(4,353)	44
Balance at end of period	**169,858**	**155,974**
Treasury stock:		
Balance at beginning of period	(105,379)	(97,070)
Stock repurchased	-	(8,950)
Lapsed restricted stock units	505	641
Balance at end of period	**(104,874)**	**(105,379)**
Accumulated other comprehensive income, net of tax:		
Balance at beginning of period	13,997	19,711
Other comprehensive income (loss), net of tax	1,847	(1,555)
Balance at end of period	**15,844**	**18,156**
Total stockholders' equity	**$ 924,934**	**$ 907,888**

See notes to unaudited consolidated financial statements

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE NINE-MONTH PERIODS ENDED SEPTEMBER 30, 2016 AND 2015

	Nine-Month Period Ended September 30,	
	2016	**2015**
	(In thousands)	
Cash flows from operating activities:		
Net income (loss)	$ **43,630**	$ **(1,528)**
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Amortization of deferred loan origination fees, net of costs	2,849	2,515
Amortization of fair value premiums, net of discounts, on acquired loans	39	2,972
Amortization of investment securities premiums, net of accretion of discounts	6,541	9,312
Amortization of core deposit and customer relationship intangibles	1,258	1,429
Amortization of fair value premiums on acquired deposits	268	569
FDIC shared-loss expense, net	10,745	38,408
Other-than-temporary impairment on securities	-	246
Reimbursement from the FDIC shared-loss coverage in sale of loans	-	(20,000)
Depreciation and amortization of premises and equipment	7,229	8,538
Deferred income tax expense (benefit), net	15,176	(1,329)
Provision for loan and lease losses, net	51,703	109,311
Stock-based compensation	1,014	1,213
(Gain) loss on:		
Sale of securities	(12,207)	(2,572)
Sale of mortgage loans held-for-sale	(1,294)	(2,595)
Derivatives	78	(26)
Early extinguishment of debt	12,000	-
Foreclosed real estate	10,580	30,608
Sale of other repossessed assets	(1,498)	4,585
Sale of premises and equipment	12	193
Originations of loans held-for-sale	(134,189)	(165,333)
Proceeds from sale of mortgage loans held-for-sale	51,238	76,953
Net (increase) decrease in:		
Trading securities	(92)	1,011
Accrued interest receivable	2,671	2,720
Servicing assets	(938)	544
Other assets	(13,394)	(18,263)
Net increase (decrease) in:		
Accrued interest on deposits and borrowings	(1,013)	(745)
Accrued expenses and other liabilities	(5,594)	(11,923)
Net cash provided by operating activities	**46,812**	**66,813**
Cash flows from investing activities:		
Purchases of:		
Investment securities available-for-sale	(676)	(3,747)
Investment securities held-to-maturity	(81,261)	(458,229)

FHLB stock	(20,398)	-
Maturities and redemptions of:		
Investment securities available-for-sale	112,444	187,052
Investment securities held-to-maturity	56,058	24,753
FHLB stock	28,469	365
Proceeds from sales of:		
Investment securities available-for-sale	300,483	103,831
Foreclosed real estate and other repossessed assets, including write-offs	36,983	63,959
Proceeds from sale of loans held-for-investment	1,149	30,669
Premises and equipment	48	(76)
Mortgage servicing rights	-	5,927
Origination and purchase of loans, excluding loans held-for-sale	(555,658)	(611,815)
Principal repayment of loans, including covered loans	616,518	722,579
Reimbursements from the FDIC on shared-loss agreements	824	46,356
Additions to premises and equipment	(3,804)	(3,402)
Net change in restricted cash	319	4,058
Net cash provided by investing activities	**491,498**	**112,280**

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE NINE-MONTHS PERIODS ENDED SEPTEMBER 30, 2016 AND 2015 – (CONTINUED)

	Nine-Month Period Ended September 30,			
	2016		2015	
	(In thousands)			
Cash flows from financing activities:				
Net increase (decrease) in:				
Deposits		35,449		(211,637)
Securities sold under agreements to repurchase		(287,865)		20,717
FHLB advances, federal funds purchased, and other borrowings		(228,157)		(3,676)
Subordinated capital notes		(66,550)		787
Exercise of stock options and restricted units lapsed, net		(329)		204
Purchase of treasury stock		-		(8,950)
Dividends paid on preferred stock		(10,396)		(10,396)
Dividends paid on common stock		(7,906)		(13,373)
Net cash used in financing activities	**$**	**(565,754)**	**$**	**(226,324)**
Net change in cash and cash equivalents		**(27,444)**		**(47,231)**
Cash and cash equivalents at beginning of period		536,709		573,427
Cash and cash equivalents at end of period	**$**	**509,265**	**$**	**526,196**
Supplemental Cash Flow Disclosure and Schedule of Non-cash Activities:				
Interest paid	$	44,316	$	51,471
Income taxes paid	$	7,389	$	10,598
Mortgage loans securitized into mortgage-backed securities	$	71,315	$	87,609
Transfer from loans to foreclosed real estate and other repossessed assets	$	32,535	$	56,510
Reclassification of loans held-for-investment to loans held-for-sale	$	123,137	$	1,453
Reclassification of loans held-for-sale to loans held-for-investment	$	182	$	156

See notes to unaudited consolidated financial statements

OFG BANCORP

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 – ORGANIZATION, CONSOLIDATION AND BASIS OF PRESENTATION

Nature of Operations

OFG Bancorp (the "Company") is a publicly-owned financial holding company incorporated under the laws of the Commonwealth of Puerto Rico. The Company operates through various subsidiaries including, a commercial bank, Oriental Bank (the "Bank"), a securities broker-dealer, Oriental Financial Services Corp. ("Oriental Financial Services"), an insurance agency, Oriental Insurance, LLC ("Oriental Insurance") and a retirement plan administrator, Oriental Pension Consultants, Inc. ("OPC"). Through these subsidiaries and their respective divisions, the Company provides a wide range of banking and financial services such as commercial, consumer and mortgage lending, auto loans, financial planning, insurance sales, money management and investment banking and brokerage services, as well as corporate and individual trust services.

On April 30, 2010, the Bank acquired certain assets and assumed certain deposits and other liabilities of Eurobank, a Puerto Rico commercial bank, in an FDIC-assisted acquisition. On December 18, 2012, the Company acquired a group of Puerto Rico-based entities that included Banco Bilbao Vizcaya Argentaria Puerto Rico ("BBVAPR"), a Puerto Rico commercial bank, as well as a securities broker-dealer and an insurance agency, which is referred to herein as the "BBVAPR Acquisition." The businesses acquired in these acquisitions have been integrated with the Company's existing business.

Recent Accounting Developments

In August 2016, the Financial Accounting Standards Board (FASB) issued new accounting guidance that addresses eight specific cash flow issues with the objective of reducing the existing diversity in practice. The amendments in this update apply to all entities, including both business entities and not-for-profit entities that are required to present a statement of cash flows under Topic 230. The amendments in this update clarifies whether the following items should be categorized as operating, investing or financing in the statement of cash flows: (i) debt prepayments and extinguishment costs, (ii) settlement of zero-coupon debt, (iii) settlement of contingent consideration, (iv) insurance proceeds, (v) settlement of corporate-owned life insurance (COLI) and bank-owned life insurance (BOLI) policies, (vi) distributions from equity method investees, (vii) beneficial interests in securitization transactions, and (viii) receipts and payments with aspects of more than one class of cash flows. The new guidance is effective on January 1, 2018. The Company does not expect the new accounting guidance to have a material impact on its statement of cash flows.

In June 2016, the FASB issued new accounting guidance that will require the earlier recognition of credit losses on loans and other financial instruments based on an expected loss model, replacing the incurred loss model that is currently in use. Under the new guidance, an entity will measure all expected credit losses for financial instruments held at the reporting date based on historical experience, current conditions and reasonable and supportable forecasts. The expected loss model will apply to loans and leases, unfunded lending commitments, held-to-maturity (HTM) debt securities and other debt instruments measured at amortized cost. The impairment model for available-for-sale (AFS) debt securities will require the recognition of credit losses through a valuation allowance when fair value is less than amortized cost, regardless of whether the impairment is considered to be other-than-temporary. The new guidance is effective on January 1, 2020, with early adoption permitted on January 1, 2019. The Company is in the process of evaluating the impact of the provisions of this new accounting guidance.

In March 2016, the FASB issued new accounting guidance that simplifies certain aspects of the accounting for share-based payment transactions, including income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The new guidance is effective on January 1, 2017, with early adoption permitted. The Company does not expect the provisions of this new accounting guidance to have a material impact on its consolidated financial position or results of operations.

In February 2016, the FASB issued new accounting guidance that requires substantially all leases to be recorded as assets and liabilities on the balance sheet. This new accounting guidance is effective on January 1, 2019, with early adoption permitted. Upon adoption, the Company will record a right of use asset and a lease payment obligation associated with arrangements previously accounted for as operating leases. The Company is in the process of evaluating the impact of the provisions of this new accounting guidance on its consolidated financial position.

In January 2016, the FASB issued new accounting guidance on recognition and measurement of financial instruments. The new guidance makes targeted changes to existing Generally Accepted Accounting Principles (GAAP) including, among other provisions, requiring certain equity investments to be measured at fair value with changes in fair value reported in earnings and requiring changes

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

in instrument-specific credit risk. The new guidance is effective on January 1, 2018. The Company does not expect the provisions of this new accounting guidance to have a material impact on its consolidated financial position or results of operations.

In May 2014, the FASB issued new accounting guidance to clarify the principles for recognizing revenue from contracts with customers. This new accounting guidance is effective on January 1, 2018. The Company does not expect the provisions of this new accounting guidance to have a material impact on its consolidated financial position or results of operations.

NOTE 2 – RESTRICTED CASH

The following table includes the composition of the Company's restricted cash:

	September 30, 2016	December 31, 2015
	(In thousands)	
Cash pledged as collateral to other financial institutions to secure:		
Derivatives	$ 1,980	$ 1,980
Obligations under agreement of loans sold with recourse	1,050	1,369
	$ 3,030	**$ 3,349**

At September 30, 2016 and December 31, 2015, the Bank's international banking entities, Oriental International Bank Inc. ("OIB") and Oriental Overseas, a division of the Bank, each held unencumbered certificates of deposit in the amount of $300 thousand as the legal reserve required for international banking entities under Puerto Rico law. Each certificate of deposit cannot be withdrawn by OIB or Oriental Overseas without prior written approval of the Office of the Commissioner of Financial Institutions of Puerto Rico.

As part of its derivative activities, the Company has entered into collateral agreements with certain financial counterparties. At September 30, 2016 and December 31, 2015, the Company had delivered $2.0 million of cash as collateral for such derivatives activities.

As part of the BBVA Acquisition, the Company assumed a contract with FNMA which required collateral to guarantee the repurchase, if necessary, of loans sold with recourse. At September 30, 2016 and December 31, 2015, the Company delivered as collateral cash amounting to $1.1 million and $1.4 million, respectively.

The Bank is required by Puerto Rico law to maintain average weekly reserve balances to cover demand deposits. The amount of those minimum average reserve balances for the week that covered September 30, 2016 was $157.5 million (December 31, 2015 - $148.3 million). At September 30, 2016 and December 31, 2015, the Bank complied with such requirement. Cash and due from bank as well as other short-term, highly liquid securities are used to cover the required average reserve balances.

NOTE 3 – INVESTMENT SECURITIES

Money Market Investments

The Company considers as cash equivalents all money market instruments that are not pledged and that have maturities of three months or less at the date of acquisition. At September 30, 2016 and December 31, 2015, money market instruments included as part of cash and cash equivalents amounted to $5.5 million and $4.7 million, respectively.

OFG BANCORP

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Investment Securities

The amortized cost, gross unrealized gains and losses, fair value, and weighted average yield of the securities owned by the Company at September 30, 2016 and December 31, 2015 were as follows:

	September 30, 2016				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Weighted Average Yield
	(In thousands)				
Available-for-sale					
Mortgage-backed securities					
FNMA and FHLMC certificates	$ 376,242	$ 13,365	$ -	$ 389,607	2.60%
GNMA certificates	125,188	5,797	-	130,985	3.02%
CMOs issued by US government-sponsored agencies	111,808	398	370	111,836	1.88%
Total mortgage-backed securities	**613,238**	**19,560**	**370**	**632,428**	**2.56%**
Investment securities					
Obligations of US government-sponsored agencies	4,170	-	5	4,165	1.37%
Obligations of Puerto Rico government and public instrumentalities	4,680	-	607	4,073	5.55%
Other debt securities	1,906	111	-	2,017	2.94%
Total investment securities	**10,756**	**111**	**612**	**10,255**	**3.47%**
Total securities available for sale	**$ 623,994**	**$ 19,671**	**$ 982**	**$ 642,683**	**2.57%**
Held-to-maturity					
Mortgage-backed securities					
FNMA and FHLMC certificates	$ 616,883	8,141	18	625,006	2.17%
Investment securities					
US Treasury securities	25,007	10	-	25,017	0.49%
Total securities held to maturity	**641,890**	**8,151**	**18**	**650,023**	**2.11%**
Total	**$ 1,265,884**	**$ 27,822**	**$ 1,000**	**$ 1,292,706**	**2.34%**

	December 31, 2015				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Weighted Average Yield
	(In thousands)				
Available-for-sale					
Mortgage-backed securities					
FNMA and FHLMC certificates	$ 735,363	$ 25,791	$ 1,509	$ 759,645	2.97%
GNMA certificates	57,129	1,366	-	58,495	3.19%
CMOs issued by US government-sponsored agencies	137,787	27	2,741	135,073	1.85%
Total mortgage-backed securities	**930,279**	**27,184**	**4,250**	**953,213**	**2.82%**
Investment securities					

Obligations of US government-sponsored agencies	5,122	-	29	5,093	1.36%
Obligations of Puerto Rico government and political subdivisions	17,801	-	4,070	13,731	6.24%
Other debt securities	2,444	128	-	2,572	2.98%
Total investment securities	**25,367**	**128**	**4,099**	**21,396**	**4.94%**
Total securities available-for-sale	**$ 955,646**	**$ 27,312**	**$ 8,349**	**$ 974,609**	**2.87%**
Held-to-maturity					
Mortgage-backed securities					
FNMA and FHLMC certificates	595,157	426	5,865	589,718	2.24%
Investment securities					
US Treasury securities	25,032	-	71	24,961	0.49%
Total securities held to maturity	**620,189**	**426**	**5,936**	**614,679**	**2.17%**
Total	**$ 1,575,835**	**$ 27,738**	**$ 14,285**	**$ 1,589,288**	**2.60%**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The amortized cost and fair value of the Company's investment securities at September 30, 2016, by contractual maturity, are shown in the next table. Securities not due on a single contractual maturity date, such as collateralized mortgage obligations, are classified in the period of final contractual maturity. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

	September 30, 2016			
	Available-for-sale		Held-to-maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(In thousands)		(In thousands)	
Mortgage-backed securities				
Due from 1 to 5 years				
FNMA and FHLMC certificates	$ 11,294	$ 11,629	$ -	$ -
Total due from 1 to 5 years	**11,294**	**11,629**	**-**	**-**
Due from 5 to 10 years				
CMOs issued by US Government-sponsored agencies	2,244	2,245	-	-
FNMA and FHLMC certificates	27,173	27,837	-	-
Total due from 5 to 10 years	**29,417**	**30,082**	**-**	**-**
Due after 10 years				
FNMA and FHLMC certificates	337,775	350,141	616,883	625,006
GNMA certificates	125,188	130,985	-	-
CMOs issued by US government-sponsored agencies	109,564	109,591	-	-
Total due after 10 years	**572,527**	**590,717**	**616,883**	**625,006**
Total mortgage-backed securities	**613,238**	**632,428**	**616,883**	**625,006**
Investment securities				
US Treasury securities	-	-	25,007	25,017
Total due in less than one year	**-**	**-**	**25,007**	**25,017**
Due from 1 to 5 years				
Obligations of Puerto Rico government and public instrumentalities	4,680	4,073	-	-
Total due from 1 to 5 years	**4,680**	**4,073**	**-**	**-**
Due from 5 to 10 years				
Obligations of US government and sponsored agencies	4,170	4,165	-	-
Other debt securities	1,906	2,017	-	-
Total due from 5 to 10 years	**6,076**	**6,182**	**-**	**-**
Total investment securities	**10,756**	**10,255**	**25,007**	**25,017**
Total securities available-for-sale and held-to-maturity	**$ 623,994**	**$ 642,683**	**$ 641,890**	**$ 650,023**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The Company, as part of its asset/liability management, may purchase U.S. Treasury securities and U.S. government-sponsored agency discount notes close to their maturities as alternatives to cash deposits at correspondent banks or as a short term vehicle to reinvest the proceeds of sale transactions until investment securities with attractive yields can be purchased. During the nine-month period ended September 30, 2016, the Company retained securitized Government National Mortgage Association ("GNMA") pools totaling $71.8 million amortized cost, at a yield of 2.99% from its own originations. Previously, the Company was selling all securitized GNMA pools. The GNMA pools were sold until June 2015. During the first half of 2015, the Company sold $63.5 million of available-for-sale GNMA certificates as part of its recurring mortgage loan origination and securitization activities. These sales did not realize any gains or losses during such period.

During the nine-month period ended September 30, 2016, the Company sold $277.2 million of mortgage-backed securities and $11.1 million of Puerto Rico government bonds, and recorded a net gain on sale of securities of $12.2 million. Among the 2016 sales, the Company sold all but one of the Puerto Rico government bonds it held. The Company had other-than-temporary impairment charges on such securities sold totaling $1.5 million during the second half of 2015. During the nine-month period ended September 30, 2015, the Company sold $101.3 million of mortgage-backed securities and recorded a net gain on sale of securities of $2.6 million. The table below presents the gross realized gains and gross realized losses by category for such periods.

	Nine-Month Period Ended September 30, 2016			
Description	**Sale Price**	**Book Value at Sale**	**Gross Gains**	**Gross Losses**
	(In thousands)			
Sale of securities available-for-sale				
Mortgage-backed securities				
FNMA and FHLMC certificates	$ 293,505	$ 277,181	$ 16,324	$ -
Investment securities				
Obligations of Puerto Rico government and public instrumentalities	6,978	11,095	-	4,117
Total	**$ 300,483**	**$ 288,276**	**$ 16,324**	**$ 4,117**

	Nine-Month Period Ended September 30, 2015			
Description	**Sale Price**	**Book Value at Sale**	**Gross Gains**	**Gross Losses**
	(In thousands)			
Sale of securities available-for-sale				
Mortgage-backed securities				
FNMA and FHLMC certificates	$ 40,307	$ 37,736	$ 2,571	$ -
GNMA certificates	63,524	63,523	1	-

Total	**$**	**103,831**	**$**	**101,259**	**$**	**2,572**	**$**	**-**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following tables show the Company's gross unrealized losses and fair value of investment securities available-for-sale and held-to-maturity, aggregated by investment category and the length of time that individual securities have been in a continuous unrealized loss position at September 30, 2016 and December 31, 2015:

	September 30, 2016 12 months or more		
	Amortized Cost	Unrealized Loss	Fair Value
		(In thousands)	
Securities available-for-sale			
CMOs issued by US government-sponsored agencies	$ 37,579	$ 320	$ 37,259
Obligations of Puerto Rico government and public instrumentalities	4,680	607	4,073
	$ **42,259**	$ **927**	$ **41,332**

	Less than 12 months		
	Amortized Cost	Unrealized Loss	Fair Value
		(In thousands)	
Securities available-for-sale			
CMOs issued by US Government-sponsored agencies	13,181	50	13,131
Obligations of US government and sponsored agencies	4,170	5	4,165
Securities held to maturity			
FNMA and FHLMC certificates	21,240	18	21,222
	$ **38,591**	$ **73**	$ **38,518**

	Total		
	Amortized Cost	Unrealized Loss	Fair Value
		(In thousands)	
Securities available-for-sale			
CMOs issued by US government-sponsored agencies	$ 50,760	$ 370	$ 50,390
Obligations of Puerto Rico Government and political subdivisions	4,680	607	4,073
Obligations of US government and sponsored agencies	4,170	5	4,165
Securities held to maturity			
FNMA and FHLMC certificates	21,240	18	21,222
	$ 80,850	**$ 1,000**	**$ 79,850**

At September 30, 2016 there were no securities held-to-maturity in a continuous unrealized loss position for twelve months or more.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	December 31, 2015		
		12 months or more	
	Amortized Cost	Unrealized Loss	Fair Value
		(In thousands)	
Securities available-for-sale			
Obligations of Puerto Rico Government and public instrumentalities	$ 17,801	$ 4,070	$ 13,731
CMOs issued by US government-sponsored agencies	103,340	2,410	100,930
	$ 121,141	**$ 6,480**	**$ 114,661**

	Less than 12 months		
	Amortized Cost	Unrealized Loss	Fair Value
		(In thousands)	
Securities available-for-sale			
CMOs issued by US government-sponsored agencies	25,736	331	25,405
FNMA and FHLMC certificates	149,480	1,509	147,971
Obligations of US government and sponsored agencies	5,122	29	5,093
Securities held to maturity			
FNMA and FHLMC certificates	468,487	5,865	462,622
US Treausury Securities	25,032	71	24,961
	$ 673,857	**$ 7,805**	**$ 666,052**

	Total		
	Amortized Cost	Unrealized Loss	Fair Value
		(In thousands)	
Securities available-for-sale			
CMOs issued by US government-sponsored agencies	129,076	2,741	126,335
FNMA and FHLMC certificates	149,480	1,509	147,971
Obligations of Puerto Rico Government and public instrumentalities	17,801	4,070	13,731
Obligations of US government and sponsored agencies	5,122	29	5,093
	$ 301,479	**$ 8,349**	**$ 293,130**
Securities held to maturity			
FNMA and FHLMC certificates	468,487	5,865	462,622
US Treasury Securities	25,032	71	24,961
	$ 794,998	**$ 14,285**	**$ 780,713**

The Company performs valuations of the investment securities on a monthly basis. Moreover, the Company conducts quarterly reviews to identify and evaluate each investment in an unrealized loss position for other-than-temporary impairment. Any portion of a decline in value associated with credit loss is recognized in the statements of operations with the remaining noncredit-related component recognized in other comprehensive income (loss). A credit loss is determined by assessing whether the amortized cost basis of the security will be recovered by comparing the present value of cash flows expected to be collected from the security, discounted at the rate equal to the yield used to accrete current and prospective beneficial interest for the security. The shortfall of the present value of the cash flows expected to be collected in relation to the amortized cost basis is considered to be the "credit loss."

Other-than-temporary impairment analysis is based on estimates that depend on market conditions and are subject to further change over time. In addition, while the Company believes that the methodology used to value these exposures is reasonable, the methodology is subject to continuing refinement, including those made as a result of market developments. Consequently, it is reasonably possible that changes in estimates or conditions could result in the need to recognize additional other-than-temporary impairment charges in the future.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Most of the investments ($76.2 million, amortized cost, or 94%) with an unrealized loss position at September 30, 2016 consist of securities issued or guaranteed by the U.S. Treasury or U.S. government-sponsored agencies, all of which are highly liquid securities that have a large and efficient secondary market. Their aggregate losses and their variability from period to period are the result of changes in market conditions, and not due to the repayment capacity or creditworthiness of the issuers or guarantors of such securities.

The remaining investments ($4.7 million, amortized cost, or 6%) with an unrealized loss position at September 30, 2016 consist of obligations issued or guaranteed by the government of Puerto Rico and its public instrumentalities. The decline in the market value of this security is mainly attributed to an increase in volatility as a result of changes in market conditions that reflect the significant economic and fiscal challenges that Puerto Rico is facing, including the government's credit default, a protracted economic recession, sizable government debt-service obligations and structural budget deficits, high unemployment and a shrinking population.

The only obligation issued or guaranteed by the government of Puerto Rico and its instrumentalities held at the end of the third quarter of 2016 by the Company was the Puerto Rico Highways and Transportation Authority (“PRHTA”) – Teodoro Moscoso Bridge revenue bond. The pledged income of this bond comes from gross revenues from Teodoro Moscoso Bridge operations. Although PRHTA is included in the Puerto Rico Governor's executive order of November 30, 2015 ordering the '"clawback" of certain government revenues, the toll bridge revenues for the repayment of such bonds were not subject to the “clawback." All other Puerto Rico government securities were sold during the first quarter of 2016. The PRHTA bond with a principal amount of $4.6 million had an aggregate fair value of $4.1 million at September 30, 2016 (87% of the bond's cost). The discounted cash flow analysis for the investments showed a cumulative default probability at maturity of 8.9%, thus reflecting that it is more likely than not that the bond will not default during its remaining term. Based on this analysis, the Company determined that it is more likely than not that it will recover all interest and principal invested in this Puerto Rico government bond and is, therefore, not required to recognize a credit loss as of September 30, 2016. Also, the Company’s conclusion is based on the assessment of the specific source of repayment of the outstanding bond, which continues to perform. PRHTA started principal repayments on July 1, 2014. All scheduled principal and interest payments to date have been collected. On July 1, 2016, the Company received the scheduled principal payment of $2.0 million. The next payment is due on July 1, 2017. As a result of the aforementioned analysis, no other-than-temporary losses were recorded during the quarter ended September 30, 2016.

As of September 30, 2016, the Company applied a discounted cash flow analysis to the bond guaranteed by the government of Puerto Rico to calculate the cash flows expected to be collected and determine if any portion of the decline in market value of these investments was considered an other-than-temporary impairment. The analysis derives an estimate of value based on the present value of risk-adjusted future cash flows of the underlying investments, and included the following components:

- The contractual future cash flows of the bonds are projected based on the key terms as set forth in the official statements for each investment. Such key terms include among others the interest rate, amortization schedule, if any, and maturity date.

- The risk-adjusted cash flows are calculated based on a monthly default probability and recovery rate assumptions based on the credit rating of each investment. Constant monthly default rates are assumed throughout the life of the bonds which are based on the respective security's credit rating as of the date of the analysis.

- The adjusted future cash flows are then discounted at the original effective yield of each investment based on the purchase price and expected risk-adjusted future cash flows as of the purchase date of each investment.

The following table presents a roll-forward of credit-related impairment losses recognized in earnings for the nine-month period ended September 30, 2016 and 2015 on available-for-sale securities:

	Nine-Mon Period End September	
	2016	**20**
Balance at beginning of period	$ 1,490	$
Reductions for securities sold during the period (realized)	(1,490)	
Additions from credit losses recognized on available-for-sale securities that had no previous impairment losses	-	2
Balance at end of period	$ **-**	$ 2

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 4 - LOANS

The Company’s loan portfolio held for investment is composed of two segments, loans initially accounted for under the amortized cost method (referred to as "originated and other" loans) and loans acquired (referred to as "acquired" loans). Acquired loans are further segregated between acquired BBVAPR loans and acquired Eurobank loans. Acquired Eurobank loans were purchased subject to loss-sharing agreements with the FDIC. The FDIC loss-share coverage related to commercial and other-non single family acquired Eurobank loans expired on June 30, 2015. Notwithstanding the expiration of loss share coverage of commercial loans, on July 2, 2015, the Company entered into an agreement with the FDIC pursuant to which the FDIC concurred with a potential sale of a pool of loss-share assets covered under the commercial loss-sharing agreement. Pursuant to such agreement, and as further discussed below, the FDIC agreed to and paid $20 million in loss share coverage with respect to the aggregate loss resulting from any portfolio sale within 120 days of the agreement. This sale was completed on September 28, 2015. Covered loans are no longer a material amount. Therefore, the Company changed its loan disclosures during 2015. Loans held for sale are presented separately.

The coverage for the single family residential loans will expire on June 30, 2020. At September 30, 2016, the remaining covered loans, amounting to $62.8 million, net carrying amount ($75.0 million gross amount), are included as part of acquired Eurobank loans under the name "loans secured by 1-4 family residential properties." At December 31, 2015, covered loans amounted to $67.2 million, net carrying amount ($92.3 million gross amount). Interest income recognized for covered loans during the nine-month periods ended September 30, 2016 and 2015 was $6.4 million and $31.4 million, respectively. The decrease in interest income recognized for covered loans is mainly due to the expiration of the FDIC loss-share coverage related to commercial and other-non single family residential loans on June 30, 2015.

Effective June 30, 2016, pursuant to supervisory direction, the Company changed the purchase credit impaired policy for all loans accounted for under ASC 310-30 (*Loans and Debt Securities Acquired with Deteriorated Credit Quality*). Under the revised policy, the Company writes-off the loan’s recorded investment and derecognizes the associated allowance for loan and lease losses for loans that exit the acquired pools. The revised policy was implemented prospectively due to the immaterial impact of retrospective adoption. Prior to June 30, 2016, the pool’s carrying value and allowance was determined by discounting expected cash flows at the pool’s effective yield. The allowance for loan and lease losses was maintained until all of the loans in the pool were paid off or charged-off. The transition to this revised policy during the second quarter of 2016 resulted in the de-recognition of $8.9 million and $73.1 million in the recorded investment balance and associated allowance for loans that had exited the pools, for acquired BBVAPR loans and acquired Eurobank loans, respectively, with no impact to the provision for loan and lease losses. Refer to Note 5 Allowances for Loan and Lease Losses.

During the third quarter of 2016, the Company entered into an agreement to sell its outstanding $200.0 million participation in the Puerto Rico Electric Power Authority ("PREPA") line of credit for $123.5 million, slightly lower than the adjusted book balance, net of reserves. As a result of this transaction, the Company recognized a $56.2

million charge-off and $2.9 million provision for loan and lease losses during the quarter ended September 30, 2016. At September 30, 2016, this line of credit was reported as other loans held for sale, at fair value of $123.1 million. The sale transaction settled on October 7, 2016.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The composition of the Company's loan portfolio at September 30, 2016 and December 31, 2015 was as follows:

	September 30, 2016	Decem 31 201
	(In thousands)	
Originated and other loans and leases held for investment:		
Mortgage	$ 735,367	$ 757
Commercial (c)	1,267,177	1,441
Consumer	278,666	242
Auto and leasing	730,589	669
	3,011,799	**3,111**
Allowance for loan and lease losses on originated and other loans and leases	(62,168)	(112
	2,949,631	**2,998**
Deferred loan costs, net	5,421	4
Total originated and other loans loans held for investment, net	**2,955,052**	**3,003**
Acquired loans:		
Acquired BBVAPR loans:		
Accounted for under ASC 310-20 (Loans with revolving feature and/or acquired at a premium)		
Commercial	5,755	7
Consumer	34,215	38
Auto	64,393	106
	104,363	**152**
Allowance for loan and lease losses on acquired BBVAPR loans accounted for under ASC 310-20 (b)	(4,213)	(5
	100,150	**147**
Accounted for under ASC 310-30 (Loans acquired with deteriorated credit quality, including those by analogy) (a)		
Mortgage	579,769	608
Commercial	230,163	287
Construction	71,436	88
Consumer	5,768	11
Auto	100,475	153
	987,611	**1,149**
Allowance for loan and lease losses on acquired BBVAPR loans accounted for under ASC 310-30	(29,819)	(25
	957,792	**1,123**
Total acquired BBVAPR loans, net	**1,057,942**	**1,270**
Acquired Eurobank loans: (a)		
Loans secured by 1-4 family residential properties	75,043	92
Commercial and construction	82,753	142
Consumer	1,488	2
Total Eurobank loans	**159,284**	**230**
Allowance for loan and lease losses on Eurobank loans (b)	(22,812)	(90

Total Eurobank loans, net	**136,472**	**14(**
Total acquired loans, net	**1,194,414**	**1,41'**
Total held for investment, net	**4,149,466**	**4,42(**
Mortgage loans held for sale	26,362	1:
Other loans held for sale (c)	123,137	
Total loans, net	**$ 4,298,965**	**$ 4,43**

(a) Current period amounts have been re-measured using the revised de-recognition policy for purchased credit impaired loans implemented in the second quarter of 2016.

(b) A portion of the allowance for loan and lease losses associated with purchased credit impaired loans was de-recognized due the revision in the de-recognition policy for these loans implemented during the second quarter of 2016.

(c) During the third quarter of 2016, the Company entered into an agreement to sell its outstanding participation in the PREPA of credit. At September 30, 2016 this line of credit was reported as other loans held for sale, at fair value of $123.1 million.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Originated and Other Loans and Leases Held for Investment

The Company’s originated and other loans held for investment are encompassed within four portfolio segments: mortgage, commercial, consumer, and auto and leasing.

The following tables present the aging of the recorded investment in gross originated and other loans held for investment as of September 30, 2016 and December 31, 2015 by class of loans. Mortgage loans past due include delinquent loans in the GNMA buy-back option program. Servicers of loans underlying GNMA mortgage-backed securities must report as their own assets the defaulted loans that they have the option (but not the obligation) to repurchase, even when they elect not to exercise that option.

	September 30, 2016							
	30-59 Days Past Due	60-89 Days Past Due	90+ Days Past Due	Total Past Due	Current in Non-Accrual	Current Accruing	Total Loans	Loans 90+ Days Past Due and Still Accruing
	(In thousands)							
Mortgage								
Traditional (by origination year):								
Up to the year 2002	$ 190	$ 1,607	$ 3,388	$ 5,185	$ 92	$ 47,169	$ 52,446	$ 114
Years 2003 and 2004	249	4,271	6,142	10,662	332	81,915	92,909	-
Year 2005	123	1,810	3,930	5,863	202	44,617	50,682	-
Year 2006	781	3,434	7,045	11,260	321	60,358	71,939	-
Years 2007, 2008 and 2009	929	2,182	11,283	14,394	46	66,407	80,847	569
Years 2010, 2011, 2012, 2013	452	2,777	10,497	13,726	-	129,710	143,436	571
Years 2014, 2015 and 2016	-	430	1,150	1,580	47	102,789	104,416	-
	2,724	16,511	43,435	62,670	1,040	532,965	596,675	1,254
Non-traditional	-	301	5,002	5,303	-	19,036	24,339	-
Loss mitigation program	10,908	6,571	18,315	35,794	2,704	65,918	104,416	2,120
	13,632	23,383	66,752	103,767	3,744	617,919	725,430	3,374
Home equity secured personal loans	-	-	-	-	-	339	339	-
GNMA's buy-back option program	-	-	9,598	9,598	-	-	9,598	-
Total mortgage	**13,632**	**23,383**	**76,350**	**113,365**	**3,744**	**618,258**	**735,367**	**3,374**

Commercial								
Commercial secured by real estate:								
Corporate	-	-	-	-	-	240,458	240,458	-
Institutional	-	-	-	-	1,495	27,265	28,760	-
Middle market	-	205	3,114	3,319	1,406	232,088	236,813	-
Retail	672	707	6,477	7,856	3,710	236,983	248,549	-
Floor plan	-	-	-	-	-	2,793	2,793	-
Real estate	-	-	-	-	-	15,783	15,783	-
	672	912	9,591	11,175	6,611	755,370	773,156	-
Other commercial and industrial:								
Corporate	-	-	-	-	-	126,325	126,325	-
Institutional	500	-	-	500	1,345	172,988	174,833	-
Middle market	-	-	-	-	1,350	85,349	86,699	-
Retail	1,112	311	1,060	2,483	210	71,252	73,945	-
Floor plan	670	-	119	789	-	31,430	32,219	-
	2,282	311	1,179	3,772	2,905	487,344	494,021	-
Total commercial	**2,954**	**1,223**	**10,770**	**14,947**	**9,516**	**1,242,714**	**1,267,177**	**-**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	September 30, 2016							
	30-59 Days Past Due	60-89 Days Past Due	90+ Days Past Due	Total Past Due	Current in Non-Accrual	Current Accruing	Total Loans	Loans 90+ Days Past Due and Still Accruing
	(In thousands)							
Consumer								
Credit cards	486	264	510	1,260	-	24,204	25,464	-
Overdrafts	12	3	3	18	-	178	196	-
Personal lines of credit	38	18	37	93	-	2,199	2,292	-
Personal loans	2,154	1,657	926	4,737	778	229,480	234,995	-
Cash collateral personal loans	162	2	30	194	-	15,525	15,719	-
Total consumer	**2,852**	**1,944**	**1,506**	**6,302**	**778**	**271,586**	**278,666**	**-**
Auto and leasing	**46,564**	**18,738**	**8,407**	**73,709**	**115**	**656,765**	**730,589**	**-**
Total	**$ 66,002**	**$ 45,288**	**$ 97,033**	**$ 208,323**	**$ 14,153**	**$ 2,789,323**	**$ 3,011,799**	**$ 3,374**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	December 31, 2015							
	30-59 Days Past Due	60-89 Days Past Due	90+ Days Past Due	Total Past Due	Current in Non-Accrual	Current Accruing	Total Loans	Loans 90+ Days Past Due and Still Accruing
	(In thousands)							
Mortgage								
Traditional (by origination year):								
Up to the year 2002	$ 80	$ 2,217	$ 3,889	$ 6,186	$ 41	$ 51,562	$ 57,789	$ 144
Years 2003 and 2004	251	5,036	5,536	10,823	-	88,623	99,446	-
Year 2005	79	2,553	3,549	6,181	-	48,040	54,221	-
Year 2006	551	2,878	7,934	11,363	176	66,864	78,403	-
Years 2007, 2008 and 2009	170	2,053	14,733	16,956	-	74,590	91,546	526
Years 2010, 2011, 2012, 2013	662	1,673	10,519	12,854	141	137,749	150,744	72
Years 2014 and 2015	-	65	663	728	-	85,128	85,856	-
	1,793	16,475	46,823	65,091	358	552,556	618,005	742
Non-traditional	-	977	5,079	6,056	13	23,483	29,552	-
Loss mitigation program	9,958	6,887	14,930	31,775	5,593	64,548	101,916	3,083
	11,751	24,339	66,832	102,922	5,964	640,587	749,473	3,825
Home equity secured personal loans	-	-	64	64	-	346	410	-
GNMA's buy-back option program	-	-	7,945	7,945	-	-	7,945	-
Total mortgage	**11,751**	**24,339**	**74,841**	**110,931**	**5,964**	**640,933**	**757,828**	**3,825**
Commercial								
Commercial secured by real estate:								
Corporate	-	-	-	-	-	227,557	227,557	-
Institutional	213	-	-	213	-	33,594	33,807	-
Middle market	1,174	712	9,113	10,999	1,730	194,219	206,948	-
Retail	686	466	6,921	8,073	1,177	231,840	241,090	-
Floor plan	-	-	-	-	-	2,892	2,892	-
Real estate	-	-	-	-	-	16,662	16,662	-
	2,073	1,178	16,034	19,285	2,907	706,764	728,956	-
Other commercial and industrial:								
Corporate	-	-	-	-	-	108,582	108,582	-
Institutional	-	-	-	-	190,290	190,695	380,985	-
Middle market	-	-	-	-	1,565	105,748	107,313	-
Retail	282	639	604	1,525	783	75,489	77,797	-
Floor plan	238	51	39	328	-	37,688	38,016	-
	520	690	643	1,853	192,638	518,202	712,693	-

Total commercial	**2,593**	**1,868**	**16,677**	**21,138**	**195,545**	**1,224,966**	**1,441,649**	**-**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	December 31, 2015							
	30-59 Days Past Due	60-89 Days Past Due	90+ Days Past Due	Total Past Due	Current in Non-Accrual	Current Accruing	Total Loans	Loans 90+ Days Past Due and Still Accruing
	(In thousands)							
Consumer								
Credit cards	449	182	369	1,000	-	21,766	22,766	-
Overdrafts	24	-	-	24	-	166	190	-
Personal lines of credit	74	-	45	119	19	2,106	2,244	-
Personal loans	2,078	1,179	627	3,884	414	196,858	201,156	-
Cash collateral personal loans	125	17	2	144	-	16,450	16,594	-
Total consumer	**2,750**	**1,378**	**1,043**	**5,171**	**433**	**237,346**	**242,950**	**-**
Auto and leasing	**53,566**	**16,898**	**8,293**	**78,757**	**49**	**590,357**	**669,163**	**-**
Total	**$ 70,660**	**$ 44,483**	**$ 100,854**	**$ 215,997**	**$ 201,991**	**$ 2,693,602**	**$ 3,111,590**	**$ 3,825**

During 2015, the Company changed its early delinquency reporting on mortgage loans from one scheduled payment due to two scheduled payments due to be comparable with local peers, except for troubled-debt restructured loans which continue using one scheduled payment due for delinquency reporting. During the quarter ended June 30, 2016, the Company changed its early delinquency reporting on consumer and auto loans from one scheduled payment due to two scheduled payments to report consistently its retail portfolio. The change resulted in a $19 thousand and $5.9 million reduction in early and total delinquency for consumer and auto loans, respectively.

At September 30, 2016 and December 31, 2015, the Company had carrying balances of $136.8 million and $334.6 million, respectively, in originated and other loans held for investment granted to the Puerto Rico government, including its instrumentalities, public corporations and municipalities as part of the institutional commercial loan segment. All loans granted to the Puerto Rico government were current at September 30, 2016 and December 31, 2015.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Acquired Loans

Acquired loans were initially measured at fair value and subsequently accounted for under either ASC 310-30 or ASC 310-20 (*Non-refundable fees and Other Costs*). We have acquired loans in two bank acquisitions, BBVAPR and Eurobank.

Acquired BBVAPR Loans

Accounted for under ASC 310-20 (Loans with revolving feature and/or acquired at a premium)

Credit cards, retail and commercial revolving lines of credits, floor plans and performing auto loans with FICO scores over 660 acquired at a premium, excluding the acquired Eurobank loan portfolio, are accounted for under the guidance of ASC 310-20, which requires that any contractually required loan payment receivable in excess of the Company's initial investment in the loans be accreted into interest income on a level-yield basis over the life of the loan. Loans accounted for under ASC 310-20 are placed on non-accrual status when past due in accordance with the Company's non-accrual policy, and any accretion of discount or amortization of premium is discontinued. Acquired BBVAPR loans that were accounted for under the provisions of ASC 310-20 are removed from the acquired loan category at the end of the reporting period upon refinancing, renewal or normal re-underwriting.

The following tables present the aging of the recorded investment in gross acquired BBVAPR loans accounted for under ASC 310-20 as of September 30, 2016 and December 31, 2015, by class of loans:

	September 30, 2016							
	30-59 Days Past Due	60-89 Days Past Due	90+ Days Past Due	Total Past Due	Current in Non-Accrual	Current Accruing	Total Loans	Loans 90+ Days Past Due and Still Accruing
	(In thousands)							
Commercial								

Commercial secured by real estate								
Retail	$ -	$ -	$ 150	$ 150	$ -	$ -	$ 150	$ -
Floor plan	969	-	227	1,196	-	1,286	2,482	-
	969	-	377	1,346	-	1,286	2,632	-
Other commercial and industrial								
Retail	67	56	78	201	-	2,919	3,120	-
Floor plan	-	-	3	3	-	-	3	-
	67	56	81	204	-	2,919	3,123	-
	1,036	**56**	**458**	**1,550**	**-**	**4,205**	**5,755**	**-**
Consumer								
Credit cards	827	443	641	1,911	-	29,452	31,363	-
Personal loans	95	15	62	172	-	2,680	2,852	-
	922	**458**	**703**	**2,083**	**-**	**32,132**	**34,215**	**-**
Auto	**4,321**	**1,608**	**739**	**6,668**	**4**	**57,721**	**64,393**	**-**
Total	**$ 6,279**	**$ 2,122**	**$ 1,900**	**$ 10,301**	**$ 4**	**$ 94,058**	**$ 104,363**	**$ -**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	December 31, 2015							
	30-59 Days Past Due	60-89 Days Past Due	90+ Days Past Due	Total Past Due	Current in Non-Accrual	Current Accruing	Total Loans	Loans 90+ Days Past Due and Still Accruing
	(In thousands)							
Commercial								
Commercial secured by real estate								
Retail	$ -	$ -	$ 228	$ 228	$ -	$ -	$ 228	$ -
Floor plan	-	-	467	467	-	2,422	2,889	-
	-	-	695	695	-	2,422	3,117	-
Other commercial and industrial								
Retail	186	29	178	393	-	3,331	3,724	-
Floor plan	-	-	7	7	-	609	616	-
	186	29	185	400	-	3,940	4,340	-
	186	**29**	**880**	**1,095**	**-**	**6,362**	**7,457**	**-**
Consumer								
Credit cards	930	384	489	1,803	-	33,414	35,217	-
Personal loans	14	29	46	89	-	3,079	3,168	-
	944	**413**	**535**	**1,892**	**-**	**36,493**	**38,385**	**-**
Auto	**7,553**	**2,279**	**831**	**10,663**	**-**	**96,248**	**106,911**	**-**
Total	**$ 8,683**	**$ 2,721**	**$ 2,246**	**$ 13,650**	**$ -**	**$ 139,103**	**$ 152,753**	**$ -**

Acquired BBVAPR Loans Accounted for under ASC 310-30 (including those accounted for under ASC 310-30 by analogy)

Acquired BBVAPR loans, except for credit cards, retail and commercial revolving lines of credits, floor plans and performing auto loans with FICO scores over 660 acquired at a premium, are accounted for by the Company in accordance with ASC 310-30.

The carrying amount corresponding to acquired BBVAPR loans with deteriorated credit quality, including those accounted under ASC 310-30 by analogy, in the statements of financial condition at September 30, 2016 and December 31, 2015 is as follows:

	September 30, 2016		December 31, 2015	
	(In thousands)			
Contractual required payments receivable (a)	$	1,716,721	$	1,945,098
Less: Non-accretable discount		367,754		434,190
Cash expected to be collected		1,348,967		1,510,908
Less: Accretable yield		361,356		361,688
Carrying amount, gross		987,611		1,149,220
Less: allowance for loan and lease losses (b)		29,819		25,785
Carrying amount, net	**$**	**957,792**	**$**	**1,123,435**

(a) Current period amounts have been re-measured using the revised de-recognition policy for purchased credit impaired loans implemented in the second quarter of 2016.
(b) A portion of the allowance for loan and lease losses associated with purchased credit impaired loans was de-recognized due to the revision in the de-recognition policy for these loans implemented during the second quarter of 2016.

At September 30, 2016 and December 31, 2015, the Company had $65.6 million and $80.9 million, respectively, in loans granted to the Puerto Rico government, including its instrumentalities, public corporations and municipalities as part of its acquired BBVAPR loans accounted for under ASC 310-30.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following tables describe the accretable yield and non-accretable discount activity of acquired BBVAPR loans accounted for under ASC 310-30 for the quarters and nine-month periods ended September 30, 2016 and 2015:

	Quarter Ended September 30, 2016					
	Mortgage	Commercial	Construction	Auto	Consumer	Total
	(In thousands)					
Accretable Yield Activity:						
Balance at beginning of period	$ 283,823	$ 37,059	$ 15,248	$ 14,103	$ 4,885	$ 355,118
Accretion	(8,197)	(5,201)	(1,485)	(3,107)	(662)	(18,652)
Change in expected cash flows	(1)	1,764	(1)	618	(241)	2,139
Transfer from (to) non-accretable discount	24,056	(1,296)	283	(525)	233	22,751
Balance at end of period	**$ 299,681**	**$ 32,326**	**$ 14,045**	**$ 11,089**	**$ 4,215**	**$ 361,356**
Non-Accretable Discount Activity:						
Balance at beginning of period	$ 336,153	$ 10,582	$ 7,419	$ 22,121	$ 18,225	$ 394,500
Change in actual and expected losses	(2,591)	(1,215)	(1)	(309)	121	(3,995)
Transfer (to) from accretable yield	(24,056)	1,296	(283)	525	(233)	(22,751)
Balance at end of period	**$ 309,506**	**$ 10,663**	**$ 7,135**	**$ 22,337**	**$ 18,113**	**$ 367,754**

	Nine-Month Period Ended September 30, 2016					
	Mortgage	Commercial	Construction	Auto	Consumer	Total
	(In thousands)					
Accretable Yield Activity:						
Balance at beginning of period	$ 268,794	$ 45,411	$ 19,615	$ 21,578	$ 6,290	$ 361,688
Accretion	(24,798)	(16,312)	(4,661)	(10,934)	(2,470)	(59,175)
Change in expected cash flows	(1)	4,954	(209)	1,249	(242)	5,751
Transfer from (to) non-accretable discount	55,686	(1,727)	(700)	(804)	637	53,092
Balance at end of period	**$ 299,681**	**$ 32,326**	**$ 14,045**	**$ 11,089**	**$ 4,215**	**$ 361,356**
Non-Accretable Discount Activity:						
Balance at beginning of period	$ 374,772	$ 11,781	$ 6,764	$ 22,039	$ 18,834	$ 434,190
Change in actual and expected losses	(9,580)	(2,845)	(329)	(506)	(84)	(13,344)
Transfer (to) from accretable yield	(55,686)	1,727	700	804	(637)	(53,092)
Balance at end of period	**$ 309,506**	**$ 10,663**	**$ 7,135**	**$ 22,337**	**$ 18,113**	**$ 367,754**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Quarter Ended September 30, 2015					
	Mortgage	Commercial	Construction	Auto	Consumer	Total
	(In thousands)					
Accretable Yield Activity:						
Balance at beginning of period	$ 275,880	$ 71,563	$ 24,613	$ 31,531	$ 8,461	$ 412,048
Accretion	(8,614)	(12,693)	(2,719)	(5,463)	(1,207)	(30,696)
Change in actual and expected losses	-	6,134	1,396	(1)	(1)	7,528
Transfer from (to) non-accretable discount	75	(6,450)	(4,075)	148	35	(10,267)
Balance at end of period	**$ 267,341**	**$ 58,554**	**$ 19,215**	**$ 26,215**	**$ 7,288**	**$ 378,613**
Non-Accretable Discount Activity:						
Balance at beginning of period	$ 389,107	$ 10,770	$ 6,994	$ 23,690	$ 19,356	$ 449,917
Change in actual and expected losses	(2,184)	(12,090)	(2,937)	(555)	(315)	(18,081)
Transfer (to) from accretable yield	(75)	6,450	4,075	(148)	(35)	10,267
Balance at end of period	**$ 386,848**	**$ 5,130**	**$ 8,132**	**$ 22,987**	**$ 19,006**	**$ 442,103**

	Nine-Month Period Ended September 30, 2015					
	Mortgage	Commercial	Construction	Auto	Consumer	Total
	(In thousands)					
Accretable Yield Activity:						
Balance at beginning of period	$ 298,364	$ 61,196	$ 25,829	$ 53,998	$ 6,559	$ 445,946
Accretion	(26,414)	(33,049)	(8,672)	(18,614)	(3,420)	(90,169)
Change in actual and expected losses	-	6,134	1,396	(1)	(1)	7,528
Transfer (to) from non-accretable discount	(4,609)	24,273	662	(9,168)	4,150	15,308
Balance at end of period	**$ 267,341**	**58,554**	**19,215**	**26,215**	**7,288**	**378,613**
Non-Accretable Discount Activity:						
Balance at beginning of period	$ 389,839	$ 23,069	$ 3,486	$ 16,215	$ 24,018	$ 456,627
Change in actual and expected losses	(7,600)	6,334	5,308	(2,396)	(862)	784
Transfer from (to) accretable yield	4,609	(24,273)	(662)	9,168	(4,150)	(15,308)
Balance at end of period	**$ 386,848**	**$ 5,130**	**$ 8,132**	**$ 22,987**	**$ 19,006**	**$ 442,103**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Acquired Eurobank Loans

The carrying amount of acquired Eurobank loans at September 30, 2016 and December 31, 2015 is as follows:

	September 30 2016	December 31 2015
	(In thousands)	
Contractual required payments receivable (a)	$ 243,873	$ 342,511
Less: Non-accretable discount	7,934	21,156
Cash expected to be collected	235,939	321,355
Less: Accretable yield	76,655	84,391
Carrying amount, gross	159,284	236,964
Less: Allowance for loan and lease losses (b)	22,812	90,178
Carrying amount, net	**$ 136,472**	**$ 146,786**

(a) Current period amounts have been re-measured using the revised de-recognition policy for purchased credit impaired loans implemented in the second quarter of 2016.
(b) A portion of the allowance for loan and lease losses associated with purchased credit impaired loans was de-recognized due to the revision in the de-recognition policy for these loans implemented during the second quarter of 2016.

The following tables describe the accretable yield and non-accretable discount activity of acquired Eurobank loans for the quarters and nine-month periods ended September 30, 2016 and 2015:

	Quarter Ended September 30, 2016					
	Loans Secured by 1-4 Family Residential Properties	Commercial and Other Construction	Construction & Development Secured by 1-4 Family Residential Properties	Leasing	Consumer	Total
	(In thousands)					
Accretable Yield Activity:						
Balance at beginning of period	$ 48,336	$ 29,142	$ 2,204	$ -	$ -	$ 79,682
Accretion	(2,217)	(6,570)	-	(62)	(490)	(9,339)
Change in expected cash flows	646	1,719	(8)	62	490	2,909
Transfer from (to) non-accretable discount	3,737	(188)	(146)	-	-	3,403
Balance at end of year	**$ 50,502**	**$ 24,103**	**$ 2,050**	**$ -**	**$ -**	**$ 76,655**

Non-Accretable Discount Activity:											
Balance at beginning of period	$	11,555	$	-	$	-	$	-	$	-	$	11,555
Change in actual and expected losses		(845)		617		10		-		-		(218)
Transfer from (to) accretable yield		(3,737)		188		146		-		-		(3,403)
Balance at end of period	**$**	**6,973**	**$**	**805**	**$**	**156**	**$**	**-**	**$**	**-**	**$**	**7,934**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Nine-Month Period Ended September 30, 2016					
	Loans Secured by 1-4 Family Residential Properties	Commercial and Other Construction	Construction & Development Secured by 1-4 Family Residential Properties	Leasing	Consumer	Total
	(In thousands)					
Accretable Yield Activity:						
Balance at beginning of period	$ 51,954	$ 26,970	$ 2,255	$ -	$ 3,212	$ 84,391
Accretion	(6,746)	(15,193)	(47)	(60)	(1,751)	(23,797)
Change in expected cash flows	1,432	14,431	(31)	(15)	(1,456)	14,361
Transfer from (to) non-accretable discount	3,862	(2,105)	(127)	75	(5)	1,700
Balance at end of period	**$ 50,502**	**$ 24,103**	**$ 2,050**	**$ -**	**$ -**	**$ 76,655**
Non-Accretable Discount Activity:						
Balance at beginning of period	$ 12,869	$ -	$ -	$ -	$ 8,287	$ 21,156
Change in actual and expected losses	(2,034)	(1,300)	29	75	(8,292)	(11,522)
Transfer (to) from accretable yield	(3,862)	2,105	127	(75)	5	(1,700)
Balance at end of period	**$ 6,973**	**$ 805**	**$ 156**	**$ -**	**$ -**	**$ 7,934**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Quarter Ended September 30, 2015					
	Loans Secured by 1-4 Family Residential Properties	Commercial and Other Construction	Construction & Development Secured by 1-4 Family Residential Properties	Leasing	Consumer	Total
	(In thousands)					
Accretable Yield Activity:						
Balance at beginning of period	$ 55,806	$ 27,473	$ 18,349	$ 1,103	$ 1,910	$ 104,641
Accretion	(3,543)	(10,100)	(1,446)	(711)	(214)	(16,014)
Change in expected cash flows	4,320	43,775	(10,749)	270	118	37,734
Transfer from non-accretable discount	(2,188)	(30,400)	175	307	1,603	(30,503)
Balance at end of period	**$ 54,395**	**$ 30,748**	**$ 6,329**	**$ 969**	**$ 3,417**	**$ 95,858**
Non-Accretable Discount Activity:						
Balance at beginning of period	$ 11,402	$ -	$ -	$ -	$ 9,730	$ 21,132
Change in actual and expected losses	(8)	(30,400)	175	307	(34)	(29,960)
Transfer to accretable yield	2,188	30,400	(175)	(307)	(1,603)	30,503
Balance at end of period	**$ 13,582**	**$ -**	**$ -**	**$ -**	**$ 8,093**	**$ 21,675**

	Nine-Month Period Ended September 30, 2015					
	Loans Secured by 1-4 Family Residential Properties	Commercial and Other Construction	Construction & Development Secured by 1-4 Family Residential Properties	Leasing	Consumer	Total
	(In thousands)					
Accretable Yield Activity:						
Balance at beginning of period	$ 47,636	$ 37,919	$ 20,753	$ 2,479	$ 1,072	$ 109,859
Accretion	(10,337)	(28,002)	(2,470)	(3,040)	(427)	(44,276)
Change in Expected Cash Flows	4,320	43,775	(10,749)	270	118	37,734
Transfer from (to) non-accretable discount	12,776	(22,944)	(1,205)	1,260	2,654	(7,459)
Balance at end of period	**$ 54,395**	**$ 30,748**	**$ 6,329**	**$ 969**	**$ 3,417**	**$ 95,858**
Non-Accretable Discount Activity:						
Balance at beginning of period	$ 27,348	$ 24,464	$ -	$ -	$ 10,598	$ 62,410
Change in actual and expected cash flows	(990)	(47,408)	(1,205)	1,260	149	(48,194)
Transfer (to) from accretable yield	(12,776)	22,944	1,205	(1,260)	(2,654)	7,459
Balance at end of period	**$ 13,582**	**$ -**	**$ -**	**$ -**	**$ 8,093**	**$ 21,675**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Non-accrual Loans

The following table presents the recorded investment in loans in non-accrual status by class of loans as of September 30, 2016 and December 31, 2015:

	September 30, 2016	December 31, 2015
	(In thousands)	
Originated and other loans and leases held for investment		
Mortgage		
Traditional (by origination year):		
Up to the year 2002	$ 3,436	$ 3,786
Years 2003 and 2004	6,474	5,737
Year 2005	4,367	3,627
Year 2006	7,412	8,189
Years 2007, 2008 and 2009	10,931	14,625
Years 2010, 2011, 2012, 2013	10,059	10,588
Years 2014, 2015 and 2016	1,197	663
	43,876	47,215
Non-traditional	5,002	5,092
Loss mitigation program	21,485	20,172
	70,363	**72,479**
Home equity loans, secured personal loans	-	64
	70,363	**72,543**
Commercial		
Commercial secured by real estate		
Middle market	4,726	12,729
Retail	11,040	8,726
	15,766	21,455
Other commercial and industrial		
Institutional	1,845	190,290
Middle market	1,350	1,565
Retail	2,101	1,932
Floor plan	790	39
	6,086	193,826
	21,852	**215,281**
Consumer		
Credit cards	510	369
Personal lines of credit	37	100
Personal loans	1,890	1,146
Cash collateral personal loans	30	16
	2,467	**1,631**
Auto and leasing	**9,477**	**8,418**

Total non-accrual originated loans	$	**104,159**	$	**297,873**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	September 30, 2016	December 31, 2015
	(In thousands)	
<u>**Acquired BBVAPR loans accounted for under ASC 310-20**</u>		
Commercial		
Commercial secured by real estate		
Retail	$ 150	$ 228
Floor plan	227	467
	377	695
Other commercial and industrial		
Retail	78	178
Floor plan	3	7
	81	185
	458	**880**
Consumer		
Credit cards	641	489
Personal loans	62	46
	703	**535**
Auto	**777**	**831**
Total non-accrual acquired BBVAPR loans accounted for under ASC 310-20	**1,938**	**2,246**
Total non-accrual loans	**$ 106,097**	**$ 300,119**

Loans accounted for under ASC 310-30 are excluded from the above table as they are considered to be performing due to the application of the accretion method, in which these loans will accrete interest income over the remaining life of the loans using estimated cash flow analyses or are accounted for under the cost recovery method.

Delinquent residential mortgage loans insured or guaranteed under applicable Federal Housing Administration ("FHA") and U.S. Department of Veterans Affairs ("VA") programs are classified as non-performing loans when they become 90 days or more past due, but are not placed in non-accrual status until they become 18 months or more past due, since they are insured loans. Therefore, these loans are included as non-performing loans but excluded from non-accrual loans. In addition, these loans are excluded from the impairment analysis.

During the first quarter of 2015, the participation in the PREPA line of credit was classified as non-accrual. At December 31, 2015, this participation had an unpaid principal balance of $190.3 million. During the third quarter of 2016, the Company agreed to sell its participation with a settlement on October 7, 2016. Therefore, at September 30, 2016 this line of credit was reported as other loans held for sale, at fair value of $123.1 million.

At September 30, 2016 and December 31, 2015, loans whose terms have been extended and which are classified as troubled-debt restructurings that are not included in non-accrual loans amounted to $100.3 million and $93.6 million, respectively, as they are performing under their new terms.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Impaired Loans

The Company evaluates all loans, some individually and others as homogeneous groups, for purposes of determining impairment. The total investment in impaired commercial loans was $36.6 million and $235.8 million at September 30, 2016 and December 31, 2015, respectively. Impaired commercial loans at December 31, 2015 included the PREPA line of credit with an unpaid principal balance of $190.3 million. The impaired commercial loans were measured based on the fair value of collateral or the present value of cash flows, including those identified as troubled-debt restructurings. The valuation allowance for impaired commercial loans amounted to $5.6 million at September 30, 2016 and $55.9 million at December 31, 2015. The valuation allowance for impaired commercial loans at December 31, 2015 included $53.3 million of specific allowance for PREPA. The total investment in impaired mortgage loans was $92.3 million and $90.0 million at September 30, 2016 and December 31, 2015, respectively. Impairment on mortgage loans assessed as troubled-debt restructurings was measured using the present value of cash flows. The valuation allowance for impaired mortgage loans amounted to $8.7 million at September 30, 2016 and $9.2 million at December 31, 2015.

Originated and Other Loans and Leases Held for Investment

The Company's recorded investment in commercial and mortgage loans categorized as originated and other loans and leases held for investment that were individually evaluated for impairment and the related allowance for loan and lease losses at September 30, 2016 and December 31, 2015 are as follows:

	September 30, 2016			
	Unpaid Principal	Recorded Investment	Related Allowance	Coverage
	(In thousands)			
Impaired loans with specific allowance:				
Commercial	$ 16,915	$ 14,949	$ 5,572	38%
Residential impaired and troubled-debt restructuring	100,390	92,343	8,725	9%
Impaired loans with no specific allowance:				
Commercial	27,908	21,420	-	0%
Total investment in impaired loans	**$ 145,213**	**$ 128,712**	**$ 14,297**	**11%**

	December 31, 2015			
	Unpaid Principal	Recorded Investment	Related Allowance	Coverage
	(In thousands)			

Impaired loans with specific allowance:				
Commercial	$ 210,718	$ 199,366	$ 55,947	28%
Residential impaired and troubled-debt restructuring	97,424	89,973	9,233	10%
Impaired loans with no specific allowance				
Commercial	42,110	35,928	-	0%
Total investment in impaired loans	**$ 350,252**	**$ 325,267**	**$ 65,180**	**20%**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Acquired BBVAPR Loans

Loans Accounted for under ASC 310-20 (Loans with revolving feature and/or acquired at a premium)

The Company's recorded investment in acquired BBVAPR commercial loans accounted for under ASC 310-20 that were individually evaluated for impairment and the related allowance for loan and lease losses at September 30, 2016 and December 31, 2015 are as follows:

	September 30, 2016			
	Unpaid Principal	Recorded Investment	Related Allowance	Coverage
		(In thousands)		
Impaired loans with no specific allowance				
Commercial	$ 251	$ 230	$ -	0%
Total investment in impaired loans	**$ 251**	**$ 230**	**$ -**	**0%**

	December 31, 2015			
	Unpaid Principal	Recorded Investment	Specific Allowance	Coverage
		(In thousands)		
Impaired loans with no specific allowance				
Commercial	$ 486	$ 474	$ -	0%
Total investment in impaired loans	**$ 486**	**$ 474**	**$ -**	**0%**

Loans Accounted for under ASC 310-30 (including those accounted for under ASC 310-30 by analogy)

The Company's recorded investment in acquired BBVAPR loan pools accounted for under ASC 310-30 that have recorded impairments and their related allowance for loan and lease losses at September 30, 2016 and December 31, 2015 are as follows:

	September 30, 2016			
	Unpaid Principal	Recorded Investment	Allowance	Coverage to Recorded Investment
		(In thousands)		
Impaired loan pools with specific allowance: (a)(b)				
Mortgage	$ 608,751	$ 579,770	$ 2,664	0%
Commercial	168,980	164,061	17,878	11%

Construction		52,775		51,271		4,120	8%
Auto		107,358		100,475		5,157	5%
Total investment in impaired loan pools	**$**	**937,864**	**$**	**895,577**	**$**	**29,819**	**3%**

(a) Current period amounts have been re-measured using the revised derecognition policy for purchased credit impaired loans implemented in the second quarter of 2016.

(b) A portion of the allowance for loan and lease losses associated with purchased credit impaired loans was derecognized due to the revision in the derecognition policy for these loans implemented during the second quarter of 2016.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	December 31 , 2015			
	Unpaid Principal	Recorded Investment	Allowance	Coverage to Recorded Investment
	(In thousands)			
Impaired loan pools with specific allowance:				
Mortgage	$ 608,294	$ 608,294	$ 1,761	0%
Commercial	287,311	168,107	15,455	9%
Construction	88,180	87,983	5,707	6%
Auto	153,592	153,592	2,862	2%
Total investment in impaired loan pools	**$ 1,137,377**	**$ 1,017,976**	**$ 25,785**	**3%**

The tables above only present information with respect to acquired BBVAPR loans and pools accounted for under ASC 310-30 if there is a recorded impairment to such loans or loan pools and a specific allowance for loan losses.

Acquired Eurobank Loans

The Company's recorded investment in acquired Eurobank loan pools that have recorded impairments and their related allowance for loan and lease losses as of September 30, 2016 and December 31, 2015 are as follows:

	September 30, 2016			
	Unpaid Principal	Recorded Investment	Allowance	Coverage to Recorded Investment
	(In thousands)			
Impaired loan pools with specific allowance: (a)(b)				
Loans secured by 1-4 family residential properties	$ 83,216	$ 70,337	$ 12,268	17%
Commercial and construction	57,889	53,445	10,544	20%
Consumer	-	1,488	-	0%
Total investment in impaired loan pools	**$ 141,105**	**$ 125,270**	**$ 22,812**	18%

(a) Current period amounts have been re-measured using the revised derecognition policy for purchased credit impaired loans implemented in the second quarter of 2016.
(b) A portion of the allowance for loan and lease losses associated with purchased credit impaired loans was derecognized due to the revision in the derecognition policy for these loans implemented during the second quarter of 2016.

	December 31, 2015						
		Unpaid Principal		Recorded Investment		Specific Allowance	Coverage to Recorded Investment
				(In thousands)			
Impaired loan pools with specific allowance							
Loans secured by 1-4 family residential properties	$	101,444	$	92,273	$	22,570	24%
Commercial and construction		133,148		142,377		67,365	47%
Consumer		6,713		2,314		243	11%
Total investment in impaired loan pools	**$**	**241,305**	**$**	**236,964**	**$**	**90,178**	38%

The tables above only present information with respect to acquired Eurobank loans and loan pools accounted for under ASC 310-30 if there is a recorded impairment to such loans or loan pools and a specific allowance for loan losses.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following table presents the interest recognized in commercial and mortgage loans that were individually evaluated for impairment, excluding loans accounted for under ASC 310-30 for the quarters and nine-month periods ended September 30, 2016 and 2015:

	Quarter Ended September 30,			
	2016		2015	
	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment
	(In thousands)			
Originated and other loans held for investment:				
Impaired loans with specific allowance				
Commercial	$ 162	$ 73,729	$ 37	$ 207,610
Residential troubled-debt restructuring	765	91,345	788	90,278
Impaired loans with no specific allowance				
Commercial	259	62,946	365	31,159
	1,186	**228,020**	**1,190**	**329,047**
Acquired loans accounted for under ASC 310-20:				
Impaired loans with specific allowance				
Commercial	$ 15	$ 323	$ -	$ -
Impaired loans with no specific allowance				
Commercial	-	952	-	1,077
Total interest income from impaired loans	**$ 1,201**	**$ 229,295**	**$ 1,190**	**$ 330,124**

	Nine-Month Period Ended September 30,			
	2016		2015	
	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment
	(In thousands)			
Originated and other loans held for investment:				
Impaired loans with specific allowance				
Commercial	$ 202	$ 155,094	$ 73	$ 166,633
Residential troubled-debt restructuring	2,321	90,881	2,381	90,903
Impaired loans with no specific allowance				
Commercial	749	42,050	727	74,247
Total interest income from impaired loans	**$ 3,272**	**$ 288,025**	**$ 3,181**	**$ 331,783**
Aquired loans accounted for under SC 310-20:				
Impaired loans with specific allowance				
Commercial	$ 45	$ 108	$ -	$ -
Impaired loans with no specific allowance				
Commercial	-	736	-	1,641

Total interest income from impaired loans	**$**	**3,317**	**$**	**288,869**	**$**	**3,181**	**$**	**333,424**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Modifications

The following tables present the troubled-debt restructurings during the quarters and nine-month periods ended September 30, 2016 and 2015.

Quarter Ended September 30, 2016 (Dollars in thousands)	Number of contracts	Pre-Modification Outstanding Recorded Investment	Pre-Modification Weighted Average Rate	Pre-Modification Weighted Average Term (in Months)	Post-Modification Outstanding Recorded Investment	Post-Modification Weighted Average Rate	Post-Modification Weighted Average Term (in Months)
Mortgage	20	$ 2,737	6.28%	297	$ 2,768	4.72%	387
Commercial	5	7,352	5.31%	65	7,352	5.89%	130
Consumer	20	183	14.73%	72	210	12.72%	54

Nine-Month Period Ended September 30, 2016 (Dollars in thousands)	Number of contracts	Pre-Modification Outstanding Recorded Investment	Pre-Modification Weighted Average Rate	Pre-Modification Weighted Average Term (in Months)	Post-Modification Outstanding Recorded Investment	Post-Modification Weighted Average Rate	Post-Modification Weighted Average Term (in Months)
Mortgage	72	$ 9,558	6.00%	347	$ 9,284	4.69%	462
Commercial	13	8,675	5.53%	63	8,676	5.95%	120
Consumer	67	739	13.63%	74	813	11.12%	67

Quarter Ended September 30, 2015 (Dollars in thousands)	Number of contracts	Pre-Modification Outstanding Recorded Investment	Pre-Modification Weighted Average Rate	Pre-Modification Weighted Average Term (in Months)	Post-Modification Outstanding Recorded Investment	Post-Modification Weighted Average Rate	Post-Modification Weighted Average Term (in Months)
Mortgage	30	$ 3,846	6.34%	338	$ 3,992	4.45%	180
Commercial	3	1,001	6.50%	12	8,511	3.19%	12
Consumer	27	170	12.41%	70	400	12.32%	52

Nine-Month Period Ended September 30, 2015 (Dollars in thousands)	Number of contracts	Pre-Modification Outstanding Recorded Investment	Pre-Modification Weighted Average Rate	Pre-Modification Weighted Average Term (in Months)	Post-Modification Outstanding Recorded Investment	Post-Modification Weighted Average Rate	Post-Modification Weighted Average Term (in Months)
Mortgage	127	$ 15,455	5.07%	346	$ 15,586	4.21%	306

Commercial	7	5,534	6.77%	67	13,045	4.52%	57
Consumer	59	567	13.87%	71	840	13.33%	60
Auto	1	64	12.95%	72	65	12.95%	72

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following table presents troubled-debt restructurings for which there was a payment default during the twelve-month periods ended September 30, 2016 and 2015:

	Twelve-Month Period Ended September 30,			
	2016		2015	
	Number of Contracts	Recorded Investment	Number of Contracts	Recorded Investment
	(Dollars in thousands)			
Mortgage	23	$ 3,437	49	$ 5,396
Commercial	2	$ 157	-	$ -
Consumer	7	$ 68	8	$ 177
Auto	-	$ -	1	$ 64

Credit Quality Indicators

The Company categorizes originated and other loans and acquired loans accounted for under ASC 310-20 into risk categories based on relevant information about the ability of borrowers to service their debt, such as economic conditions, portfolio risk characteristics, prior loss experience, and the results of periodic credit reviews of individual loans.

The Company uses the following definitions for risk ratings:

Pass: Loans classified as “pass” have a well-defined primary source of repayment very likely to be sufficient, with no apparent risk, strong financial position, minimal operating risk, profitability, liquidity and capitalization better than industry standards.

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 institution’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 institution 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, questionable and improbable.

Loss: Loans classified as “loss” are considered uncollectible and of such little value that their continuance as bankable assets is not warranted. This classification does not mean that the asset has absolutely no recovery or salvage value, but rather that it is not practical or desirable to defer writing off this worthless loan even though partial recovery may be effected in the future.

Loans not meeting the criteria above that are analyzed individually as part of the above described process are considered to be pass rated loans.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

As of September 30, 2016 and December 31, 2015, and based on the most recent analysis performed, the risk category of gross originated and other loans and BBVAPR acquired loans accounted for under ASC 310-20 subject to risk rating by class of loans is as follows:

	September 30, 2016					
		Risk Ratings				
	Balance Outstanding	Pass	Special Mention	Substandard	Doubtful	Individually Measured for Impairment
	(In thousands)					
Commercial - originated and other loans held for investment						
Commercial secured by real estate:						
Corporate	$ 240,458	$ 225,559	$ 14,899	$ -	$ -	$ -
Institutional	28,760	25,745	-	-	-	3,015
Middle market	236,813	200,191	23,628	517	-	12,477
Retail	248,549	224,865	6,486	4,435	-	12,763
Floor plan	2,793	1,824	-	-	-	969
Real estate	15,783	15,783	-	-	-	-
	773,156	693,967	45,013	4,952	-	29,224
Other commercial and industrial:						
Corporate	126,325	126,325	-	-	-	-
Institutional	174,833	172,749	239	-	-	1,845
Middle market	86,699	80,606	4,582	161	-	1,350
Retail	73,945	68,670	863	1,328	-	3,084
Floor plan	32,219	27,396	3,876	81	-	866
	494,021	475,746	9,560	1,570	-	7,145
Total	1,267,177	1,169,713	54,573	6,522	-	36,369
Commercial - acquired loans (under ASC 310-20)						
Commercial secured by real estate:						
Retail	150	-	-	150	-	-
Floor plan	2,482	1,899	356	-	-	227
	2,632	1,899	356	150	-	227
Other commercial and industrial:						
Retail	3,120	3,096	-	24	-	-
Floor plan	3	-	-	-	-	3
	3,123	3,096	-	24	-	3
Total	5,755	4,995	356	174	-	230
Total	**$ 1,272,932**	**$ 1,174,708**	**$ 54,929**	**$ 6,696**	**$ -**	**$ 36,599**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	December 31, 2015 Risk Ratings					
	Balance Outstanding	Pass	Special Mention	Substandard	Doubtful	Individually Measured for Impairment
	(In thousands)					
Commercial - originated and other loans held for investment						
Commercial secured by real estate:						
Corporate	$ 227,557	$ 212,410	$ 15,147	$ -	$ -	$ -
Institutional	33,807	25,907	-	-	-	7,900
Middle market	206,948	181,916	9,697	-	-	15,335
Retail	241,090	217,836	7,936	5,097	-	10,221
Floor plan	2,892	2,892	-	-	-	-
Real estate	16,662	16,662	-	-	-	-
	728,956	657,623	32,780	5,097	-	33,456
Other commercial and industrial:						
Corporate	108,582	100,826	-	-	-	7,756
Institutional	380,985	190,695	-	-	-	190,290
Middle market	107,313	97,288	8,052	-	-	1,973
Retail	77,797	73,757	1,076	1,184	-	1,780
Floor plan	38,016	35,862	2,115	-	-	39
	712,693	498,428	11,243	1,184	-	201,838
Total	1,441,649	1,156,051	44,023	6,281	-	235,294
Commercial - acquired loans						
(under ASC 310-20)						
Commercial secured by real estate:						
Retail	228	-	-	228	-	-
Floor plan	2,889	602	1,820	-	-	467
	3,117	602	1,820	228	-	467
Other commercial and industrial:						
Retail	3,724	3,637	-	87	-	-
Floor plan	616	609	-	-	-	7
	4,340	4,246	-	87	-	7
Total	7,457	4,848	1,820	315	-	474
Total	**$ 1,449,106**	**$ 1,160,899**	**$ 45,843**	**$ 6,596**	**$ -**	**$ 235,768**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

At September 30, 2016 and December 31, 2015, the Company had outstanding credit facilities held for investment of approximately $202.4 million and $415.4 million, respectively, granted to the Puerto Rico government, including its instrumentalities, public corporations and municipalities, included within the portfolios of originated and other loans and acquired BBVAPR loans accounted for under ASC 310-30. A substantial portion of the Company's credit exposure to Puerto Rico's government consists of collateralized loans or obligations that have a specific source of income or revenues identified for their repayment. Approximately $191.2 million of these loans are general obligations of municipalities secured by *ad valorem* taxation, without limitation as to rate or amount, on all taxable property within the issuing municipalities. The good faith, credit and unlimited taxing power of each issuing municipality are pledged for the payment of its general obligations.

At September 30, 2016, we had approximately $11.2 million of credit facilities to central government and public corporations of the Commonwealth, consisting of a participation in a loan to the Puerto Rico Housing Finance Authority ("PRHFA") with an outstanding balance of $10.9 million to be repaid from abandoned or unclaimed funds at financial institutions that revert to the government under a Puerto Rico escheat law. The loan to PRHFA defaulted on an annual principal payment in the third quarter of 2016.

The outstanding balance of credit facilities to the central government and public corporations decreased by $200.8 million during 2016 mainly as a result of the sale of the PREPA fuel line of credit which had an outstanding balance of $190.3 million at December 31, 2015. At September 30, 2016, this fuel line of credit was reported as other loans held for sale, at fair value. The sale settled on October 7, 2016.

OFG BANCORP

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

For residential and consumer loan classes, the Company evaluates credit quality based on the delinquency status of the loan. As of September 30, 2016 and December 31, 2015, and based on the most recent analysis performed, the risk category of gross originated and other loans and acquired BBVAPR loans accounted for under ASC 310-20 not subject to risk rating by class of loans is as follows:

	September 30, 2016							
			Delinquency					
	Balance Outstanding	0-29 days	30-59 days	60-89 days	90-119 days	120-364 days	365+ days	Individually Measured for Impairment
	(In thousands)							
Originated and other loans and leases held for investment								
Mortgage								
Traditional (by origination year)								
Up to the year 2002	$ 52,446	$ 46,884	$ -	$ 1,607	$ 304	$ 1,296	$ 1,646	$ 709
Years 2003 and 2004	92,909	81,218	-	4,003	1,492	1,806	2,442	1,948
Year 2005	50,682	44,294	123	1,810	790	910	1,797	958
Year 2006	71,939	58,195	231	3,380	955	1,283	4,173	3,722
Years 2007, 2008 and 2009	80,847	64,798	171	1,779	863	2,212	7,068	3,956
Years 2010, 2011, 2012 2013	143,436	131,227	292	2,398	717	809	3,954	4,039
Years 2014, 2015 and 2016	104,416	102,788	-	430	244	447	460	47
	596,675	529,404	817	15,407	5,365	8,763	21,540	15,379
Non-traditional	24,339	19,036	-	301	-	1,904	3,098	-
Loss mitigation program	104,416	17,991	2,086	1,598	1,150	1,233	3,394	76,964
	725,430	566,431	2,903	17,306	6,515	11,900	28,032	92,343
Home equity secured personal loans	339	339	-	-	-	-	-	-
GNMA's buy-back option program	9,598	-	-	-	1,872	4,065	3,661	-
	735,367	**566,770**	**2,903**	**17,306**	**8,387**	**15,965**	**31,693**	**92,343**
Consumer								
Credit cards	25,464	24,204	486	264	251	259	-	-
Overdrafts	196	178	12	3	2	1	-	-
	2,292	2,199	38	18	21	13	3	-

Unsecured personal lines of credit								
Unsecured personal loans	234,995	230,259	2,154	1,657	889	36	-	-
Cash collateral personal loans	15,719	15,525	162	2	30	-	-	-
	278,666	**272,365**	**2,852**	**1,944**	**1,193**	**309**	**3**	**-**
Auto and Leasing	**730,589**	**656,880**	**46,564**	**18,738**	**6,015**	**2,392**	**-**	**-**
	1,744,622	**1,496,015**	**52,319**	**37,988**	**15,595**	**18,666**	**31,696**	**92,343**
Acquired loans (accounted for under ASC 310-20)								
Consumer								
Credit cards	31,363	29,452	827	443	238	403	-	-
Personal loans	2,852	2,679	95	15	22	41	-	-
	34,215	**32,131**	**922**	**458**	**260**	**444**	**-**	**-**
Auto	**64,393**	**57,725**	**4,321**	**1,608**	**588**	**151**	**-**	**-**
	98,608	**89,856**	**5,243**	**2,066**	**848**	**595**	**-**	**-**
Total	**$ 1,843,230**	**$ 1,585,871**	**$ 57,562**	**$ 40,054**	**$ 16,443**	**$ 19,261**	**$ 31,696**	**$ 92,343**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	December 31, 2015							
	Delinquency							
	Balance Outstanding	0-29 days	30-59 days	60-89 days	90-119 days	120-364 days	365+ days	Individually Measured for Impairment
	(In thousands)							
Originated and other loans and leases held for investment								
Mortgage								
Traditional (by origination year)								
Up to the year 2002	$ 57,789	$ 50,912	$ 82	$ 2,218	$ 530	$ 1,504	$ 1,858	$ 685
Years 2003 and 2004	99,446	87,060	251	4,867	1,261	1,353	2,921	1,733
Year 2005	54,221	47,197	79	2,553	292	1,068	2,189	843
Year 2006	78,403	63,659	318	2,878	1,168	1,895	4,871	3,614
Years 2007, 2008 and 2009	91,546	71,439	170	1,665	685	2,972	10,725	3,890
Years 2010, 2011, 2012 2013	150,744	134,945	569	1,611	434	1,982	6,737	4,466
Year 2014 and 2015	85,856	85,128	-	65	148	281	234	-
	618,005	540,340	1,469	15,857	4,518	11,055	29,535	15,231
Non-traditional	29,552	23,497	-	977	552	2,621	1,905	-
Loss mitigation program	101,916	16,031	4,173	1,977	727	1,728	2,538	74,742
	749,473	579,868	5,642	18,811	5,797	15,404	33,978	89,973
Home equity secured personal loans	410	346	-	-	-	64	-	-
GNMA's buy-back option program	7,945	-	-	-	1,593	3,578	2,774	-
	757,828	**580,214**	**5,642**	**18,811**	**7,390**	**19,046**	**36,752**	**89,973**
Consumer								
Credit cards	22,766	21,766	449	182	179	190	-	-
Overdrafts	190	166	24	-	-	-	-	-
Unsecured personal lines of credit	2,244	2,125	74	-	17	28	-	-
Unsecured personal loans	201,156	197,339	2,083	1,107	621	6	-	-
Cash collateral personal loans	16,594	16,450	125	17	2	-	-	-
	242,950	**237,846**	**2,755**	**1,306**	**819**	**224**	**-**	**-**
Auto and Leasing	**669,163**	**590,482**	**53,549**	**16,839**	**5,708**	**2,585**	**-**	**-**

	1,669,941	**1,408,542**	**61,946**	**36,956**	**13,917**	**21,855**	**36,752**	**89,973**
Acquired loans (accounted for under ASC 310-20)								
Consumer								
Credit cards	35,217	33,414	930	384	186	303	-	-
Personal loans	3,168	3,079	14	29	1	45	-	-
	38,385	**36,493**	**944**	**413**	**187**	**348**	**-**	**-**
Auto	**106,911**	**96,247**	**7,553**	**2,279**	**623**	**209**	**-**	**-**
	145,296	**132,740**	**8,497**	**2,692**	**810**	**557**	**-**	**-**
Total	**$ 1,815,237**	**$ 1,541,282**	**$ 70,443**	**$ 39,648**	**$ 14,727**	**$ 22,412**	**$ 36,752**	**$ 89,973**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 5 – ALLOWANCE FOR LOAN AND LEASE LOSSES

The composition of the Company's allowance for loan and lease losses at September 30, 2016 and December 31, 2015 was as follows:

	September 30, 2016	December 31, 2015
	(In thousands)	
Allowance for loans and lease losses on non-acquired loans:		
Originated and other loans and leases held for investment:		
Mortgage	$ 18,527	$ 18,352
Commercial	12,307	64,791
Consumer	12,289	11,197
Auto and leasing	19,002	18,261
Unallocated	43	25
Total allowance for originated and other loans and lease losses	**62,168**	**112,626**
Acquired loans:		
Acquired BBVAPR loans:		
Accounted for under ASC 310-20 (Loans with revolving feature and/or acquired at a premium)		
Commercial	18	26
Consumer	2,946	3,429
Auto	1,249	2,087
	4,213	**5,542**
Accounted for under ASC 310-30 (Loans acquired with deteriorated credit quality, including those by analogy) (a)		
Mortgage	2,664	1,762
Commercial	21,998	21,161
Auto	5,157	2,862
	29,819	**25,785**
Total allowance for acquired BBVAPR loans and lease losses	**34,032**	**31,327**
Acquired Eurobank loans: (a)		
Loans secured by 1-4 family residential properties	12,268	22,570
Commercial and other construction	10,544	67,365
Consumer	-	243
Total allowance for acquired Eurobank loan and lease losses (a)	**22,812**	**90,178**
Total allowance for loan and lease losses (a)	**$ 119,012**	**$ 234,131**

(a) A portion of the allowance for loan and lease losses associated with purchased credit impaired loans was de-recognized due to the revision in the de-recognition policy for these loans during the second quarter of 2016 .

The Company maintains an allowance for loan and lease losses at a level that management considers adequate to provide for probable losses based upon an evaluation of known and inherent risks. The Company's allowance for loan and lease losses policy provides for a detailed quarterly analysis of probable losses. The analysis includes a review of historical loan loss experience, value of underlying collateral, current economic conditions, financial condition of borrowers and other pertinent factors. While management uses available information in estimating probable loan losses, future additions to the allowance may be required based on factors beyond the Company's control. We also maintain an allowance for loan losses on acquired loans when: (i) for loans accounted for under ASC 310-30, there is deterioration in credit quality subsequent to acquisition, and (ii) for loans accounted for under ASC 310-20, the inherent losses in the loans exceed the remaining credit discount recorded at the time of acquisition.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Effective June 30, 2016, pursuant to supervisory direction, the Company revised its purchase credit impaired policy for all loans accounted for under ASC 310-30. Under the revised policy, the Company writes-off the loan's recorded investment and derecognizes the associated allowance for loan and lease losses for loans that exit the pools. The revised policy was implemented prospectively due to the immaterial impact of retrospective adoption. Prior to June 30, 2016, the pool's carrying value and allowance was determined by discounting expected cash flows at the pool's effective yield. The allowance for loan and lease losses was maintained until all of the loans in the pool were paid off or charged-off. During the nine-month period ended September 30, 2016, the Company de-recognized $8.9 million and $73.1 million in the recorded investment balance and associated allowance for loans that had exited the pools for acquired BBVAPR loans and acquired Eurobank loans, respectively, with no impact to the provision for loan and lease losses.

Allowance for Originated and Other Loan and Lease Losses Held for Investment

The following tables present the activity in our allowance for loan and lease losses and the related recorded investment of the originated and other loans held for investment by segment for the periods indicated:

	Quarter Ended September 30, 2016					
	Mortgage	Commercial	Consumer	Auto and Leasing	Unallocated	Tota
	(In thousands)					
Allowance for loan and lease losses for originated and other loans:						
Balance at beginning of period	$ 18,537	$ 63,144	$ 11,771	$ 19,259	$ 101	$ 112,
Charge-offs	(1,656)	(56,700)	(3,173)	(7,804)	-	(69,3
Recoveries	21	93	120	3,747	-	3,
Provision (recapture) for originated and other loans and lease losses	1,625	5,770	3,571	3,800	(58)	14,
Balance at end of period	**$ 18,527**	**$ 12,307**	**$ 12,289**	**$ 19,002**	**$ 43**	**$ 62,**

	Nine-Month Period Ended September 30, 2016					
	Mortgage	Commercial	Consumer	Auto and Leasing	Unallocated	Tota
	(In thousands)					
Allowance for loan and lease losses for originated and other loans:						
Balance at beginning of period	$ 18,352	$ 64,791	$ 11,197	$ 18,261	$ 25	$ 112,
Charge-offs	(4,692)	(58,544)	(8,310)	(24,267)	-	(95,8
Recoveries	204	407	355	9,969	-	10,
Provision for originated and	4,663	5,653	9,047	15,039	18	34,

other loans and lease losses						
Balance at end of period	**$ 18,527**	**$ 12,307**	**$ 12,289**	**$ 19,002**	**$ 43**	**$ 62,**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	September 30, 2016					
	Mortgage	Commercial	Consumer	Auto and Leasing	Unallocated	T
	(In thousands)					
Allowance for loan and lease losses on originated and other loans:						
Ending allowance balance attributable to loans:						
Individually evaluated for impairment	$ 8,725	$ 5,572	$ -	$ -	$ -	$
Collectively evaluated for impairment	9,802	6,735	12,289	19,002	43	
Total ending allowance balance	**$ 18,527**	**$ 12,307**	**$ 12,289**	**$ 19,002**	**$ 43**	**$**
Loans:						
Individually evaluated for impairment	$ 92,343	$ 36,369	$ -	$ -	$ -	$ 1
Collectively evaluated for impairment	643,024	1,230,808	278,666	730,589	-	2,8
Total ending loan balance	**$ 735,367**	**$ 1,267,177**	**$ 278,666**	**$ 730,589**	**$ -**	**$ 3,0**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Quarter Ended September 30, 2015					
	Mortgage	Commercial	Consumer	Auto and Leasing	Unallocated	Tota
	(In thousands)					
Allowance for loan and lease losses for originated and other loans:						
Balance at beginning of period	$ 18,076	$ 34,779	$ 10,464	$ 15,064	$ 606	$ 78,9
Charge-offs	(1,058)	(828)	(2,471)	(8,510)	-	(12,8
Recoveries	270	63	186	3,251	-	3,7
Provision (recapture) for originated and other loans and lease losses	4	1,510	2,637	6,869	(561)	10,4
Balance at end of period	**$ 17,292**	**$ 35,524**	**$ 10,816**	**$ 16,674**	**$ 45**	**$ 80,3**

	Nine-Month Period Ended September 30, 2015					
	Mortgage	Commercial	Consumer	Auto and Leasing	Unallocated	Total
	(In thousands)					
Allowance for loan and lease losses for originated and other loans:						
Balance at beginning of year	$ 19,679	$ 8,432	$ 9,072	$ 14,255	$ 1	$ 51,4
Charge-offs	(3,829)	(2,317)	(6,456)	(24,307)	-	(36,90
Recoveries	338	372	729	10,060	-	11,4
Provision for originated and other loans and lease losses	1,104	29,037	7,471	16,666	44	54,3
Balance at end of year	**$ 17,292**	**$ 35,524**	**$ 10,816**	**$ 16,674**	**$ 45**	**$ 80,3**

	December 31, 2015					
	Mortgage	Commercial	Consumer	Auto and Leasing	Unallocated	T
	(In thousands)					
Allowance for loan and lease losses on originated and other loans:						
Ending allowance balance attributable to loans:						
Individually evaluated for impairment	$ 9,233	$ 55,947	$ -	$ -	$ -	$
Collectively evaluated for impairment	9,119	8,844	11,197	18,261	25	
Total ending allowance balance	**$ 18,352**	**$ 64,791**	**$ 11,197**	**$ 18,261**	**$ 25**	**$ 1**
Loans:						
Individually evaluated for impairment	$ 89,973	$ 235,294	$ -	$ -	$ -	$ 3
Collectively evaluated for impairment	667,855	1,206,355	242,950	669,163	-	2,7
Total ending loan balance	**$ 757,828**	**$ 1,441,649**	**$ 242,950**	**$ 669,163**	**$ -**	**$ 3,1**

During the third quarter of 2016, the Company entered into an agreement to sell its outstanding participation in the PREPA line of credit. As a result of this transaction, the Company recognized a $56.2 million charge-off and a $2.9 million provision for loan and lease losses during the quarter ended September 30, 2016.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Allowance for BBVAPR Acquired Loan Losses

Loans accounted for under ASC 310-20 (Loans with revolving feature and/or acquired at a premium)

The following tables present the activity in our allowance for loan losses and related recorded investment of the associated loans in our BBVAPR acquired loan portfolio, excluding loans accounted for under ASC 310-30, for the periods indicated:

	Quarter Ended September 30, 2016				
	Commercial	**Consumer**	**Auto**	**Unallocated**	**Total**
	(In thousands)				
Allowance for loan and lease losses for acquired BBVAPR loans accounted for under ASC 310-20:					
Balance at beginning of period	$ 21	$ 3,002	$ 1,464	$ -	$ 4,487
Charge-offs	(2)	(889)	(475)	-	(1,366)
Recoveries	16	67	461	-	544
Provision (recapture) for acquired BBVAPR loan and lease losses accounted for under ASC 310-20	(17)	766	(201)	-	548
Balance at end of period	**$ 18**	**$ 2,946**	**$ 1,249**	**$ -**	**$ 4,213**

	Nine-Month Period Ended September 30, 2016				
	Commercial	**Consumer**	**Auto**	**Unallocated**	**Total**
	(In thousands)				
Allowance for loan and lease losses for acquired BBVAPR loans accounted for under ASC 310-20:					
Balance at beginning of year	$ 26	$ 3,429	$ 2,087	$ -	$ 5,542
Charge-offs	(21)	(2,714)	(1,783)	-	(4,518)
Recoveries	56	236	1,505	-	1,797
Provision (recapture) for acquired BBVAPR	(43)	1,995	(560)	-	1,392

loan and lease losses accounted for under ASC 310-20										
Balance at end of year	**$**	**18**	**$**	**2,946**	**$**	**1,249**	**$**	**-**	**$**	**4,213**

	September 30, 2016									
	Commercial		**Consumer**		**Auto**		**Unallocated**		**Total**	
	(In thousands)									
Allowance for loan and lease losses for acquired BBVAPR loans accounted for under ASC 310-20:										
Ending allowance balance attributable to loans:										
Collectively evaluated for impairment	$	18	$	2,946	$	1,249	$	-	$	4,213
Total ending allowance balance	**$**	**18**	**$**	**2,946**	**$**	**1,249**	**$**	**-**	**$**	**4,213**
Loans:										
Collectively evaluated for impairment		5,755		34,215		64,393		-		104,363
Total ending loan balance	**$**	**5,755**	**$**	**34,215**	**$**	**64,393**	**$**	**-**	**$**	**104,363**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Quarter Ended September 30, 2015				
	Commercial	**Consumer**	**Auto**	**Unallocated**	**Total**
			(In thousands)		
Allowance for loan and lease losses for acquired BBVAPR loans accounted for under ASC 310-20:					
Balance at beginning of period	$ 54	$ 2,616	$ 2,859	$ -	$ 5,529
Charge-offs	(22)	(1,103)	(1,150)	-	(2,275)
Recoveries	7	59	502	-	568
Provision (recapture) for acquired loan and lease losses accounted for under ASC 310-20	(17)	1,485	183	-	1,651
Balance at end of period	**$ 22**	**$ 3,057**	**$ 2,394**	**$ -**	**$ 5,473**

	Nine-Month Period Ended September 30, 2015				
	Commercial	**Consumer**	**Auto**	**Unallocated**	**Total**
			(In thousands)		
Allowance for loan and lease losses for acquired BBVAPR loans accounted for under ASC 310-20:					
Balance at beginning of year	$ 65	$ 1,211	$ 3,321	$ -	$ 4,597
Charge-offs	(38)	(3,789)	(3,454)	-	(7,281)
Recoveries	24	622	1,574	-	2,220
Provision (recapture) for acquired loan and lease losses accounted for under ASC 310-20	(29)	5,013	953	-	5,937
Balance at end of period	**$ 22**	**$ 3,057**	**$ 2,394**	**$ -**	**$ 5,473**

	December 31, 2015				
	Commercial	**Consumer**	**Auto**	**Unallocated**	**Total**
			(In thousands)		
Allowance for loan and lease losses for acquired BBVAPR loans accounted for under ASC 310-20:					

Ending allowance balance attributable										
to loans:										
Collectively evaluated for impairment	$	26	$	3,429	$	2,087	$	-	$	5,542
Total ending allowance balance	**$**	**26**	**$**	**3,429**	**$**	**2,087**	**$**	**-**	**$**	**5,542**
Loans:										
Individually evaluated for impairment	$	474	$	-	$	-	$	-	$	474
Collectively evaluated for impairment		6,983		38,385		106,911		-		152,279
Total ending loan balance	**$**	**7,457**	**$**	**38,385**	**$**	**106,911**	**$**	**-**	**$**	**152,753**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Loans Accounted for under ASC 310-30 (including those accounted for under ASC 310-30 by analogy)

The following tables present the activity in our allowance for loan losses and related recorded investment of the acquired BBVAPR loan portfolio accounted for under ASC 310-30, for the periods indicated:

	Quarter Ended September 30, 2016				
	Mortgage	Commercial	Consumer (In thousands)	Auto	Total
Allowance for loan and lease losses for acquired BBVAPR loans accounted for under ASC 310-30:					
Balance at beginning of period	$ 1,585	$ 15,863	$ -	$ 5,353	$ 22,801
Provision for BBVAPR loans and lease losses accounted for under ASC 310-30	1,079	6,324	-	-	7,403
Allowance de-recognition (a)	-	(189)	-	(196)	(385)
Balance at end of period	**$ 2,664**	**$ 21,998**	**$ -**	**$ 5,157**	**$ 29,819**

(a) A portion of the allowance for loan and lease losses associated with purchased credit impaired loans was de-recognized due to the revision in the de-recognition policy for these loans during the second quarter of 2016.

	Nine-Month Period Ended September 30, 2016				
	Mortgage	Commercial	Consumer (In thousands)	Auto	Total
Allowance for loan and lease losses for acquired BBVAPR loans accounted for under ASC 310-30:					
Balance at beginning of period	$ 1,678	$ 21,245	$ -	$ 2,862	$ 25,785
Provision for BBVAPR loans and lease losses accounted for under ASC 310-30	1,000	9,552	-	2,693	13,245
Loan pools fully charged-off	(14)	(66)	-	(202)	(282)
Allowance de-recognition (a)	-	(8,733)	-	(196)	(8,929)
Balance at end of period	**$ 2,664**	**$ 21,998**	**$ -**	**$ 5,157**	**$ 29,819**

(a) A portion of the allowance for loan and lease losses associated with purchased credit impaired loans was de-recognized due to the revision in the de-recognition policy for these loans during the second quarter of 2016.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Quarter Ended September 30, 2015				
	Mortgage	Commercial	Consumer (In thousands)	Auto	Total
Allowance for loan and lease losses for acquired BBVAPR loans accounted for under ASC 310-30:					
Balance at beginning of period	$ 473	$ 14,940	$ 84	$ 2,862	$ 18,359
Provision for acquired BBVAPR loans and lease losses accounted for under ASC 310-30	-	5,979	-	-	5,979
Loan pools fully charged-off	-	(4,352)	-	-	(4,352)
Balance at end of period	**$ 473**	**$ 16,567**	**$ 84**	**$ 2,862**	**$ 19,986**

	Nine-Month Period Ended September 30, 2015				
	Mortgage	Commercial	Consumer (In thousands)	Auto	Total
Allowance for loan and lease losses for acquired BBVAPR loans accounted for under ASC 310-30:					
Balance at beginning of period	$ -	$ 13,476	$ 5	$ -	$ 13,481
Provision for acquired BBVAPR loans and lease losses accounted for under ASC 310-30	473	7,443	79	2,862	10,857
Loan pools fully charged-off	-	(4,352)	-	-	(4,352)
Balance at end of period	**$ 473**	**$ 16,567**	**$ 84**	**$ 2,862**	**$ 19,986**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Allowance for Acquired Eurobank Loan Losses

For loans accounted for under ASC 310-30, as part of the evaluation of actual versus expected cash flows, the Company assesses on a quarterly basis the credit quality of these loans based on delinquency, severity factors and risk ratings, among other assumptions. Migration and credit quality trends are assessed at the pool level, by comparing information from the latest evaluation period through the end of the reporting period.

The changes in the allowance for loan and lease losses on acquired Eurobank loans for the quarters and nine-month periods ended September 30, 2016 and 2015 were as follows:

	Quarter Ended September 30, 2016			
	Loans Secured by 1-4 Family Residential Properties	**Commercial and Construction**	**Consumer**	**Total**
		(In thousands)		
Allowance for loan and lease losses for acquired Eurobank loans:				
Balance at beginning of period	$ 11,016	$ 11,096	$ 4	$ 22,116
Provision (recapture) for acquired Eurobank loans and lease losses, net	893	(74)	-	819
FDIC shared-loss portion of provision for covered loan and lease losses, net	818	-	-	818
Allowance de-recognition (a)	(459)	(478)	(4)	(941)
Balance at end of period	**$ 12,268**	**$ 10,544**	**$ -**	**$ 22,812**

(a) A portion of the allowance for loan and lease losses associated with purchased credit impaired loans was de-recognized due to the revision in the de-recognition policy for these loans during the second quarter of 2016.

	Nine-Month Period Ended September 30, 2016			
	Loans Secured by 1-4 Family Residential Properties	**Commercial and Construction**	**Consumer**	**Total**
		(In thousands)		

Allowance for loan and lease losses for acquired Eurobank loans:				
Balance at beginning of period	$ 22,570	$ 67,365	$ 243	$ 90,178
Provision (recapture) for acquired Eurobank loans and lease losses, net	1,077	1,585	(7)	2,655
FDIC shared-loss portion of provision for covered loan and lease losses, net	3,213	-	-	3,213
Loan pools fully charged-off	-	(134)	-	(134)
Allowance de-recognition (a)	(14,592)	(58,272)	(236)	(73,100)
Balance at end of year	**$ 12,268**	**$ 10,544**	**$ -**	**$ 22,812**

(a) A portion of the allowance for loan and lease losses associated with purchased credit impaired loans was de-recognized due to the revision in the de-recognition policy for these loans during the second quarter of 2016.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Quarter Ended September 30, 2015			
	Mortgage	Commercial and Construction	Consumer	Total
	(In thousands)			
Allowance for loan and lease losses for acquired Eurobank loans:				
Balance at beginning of period	$ 17,593	$ 53,470	$ 389	$ 71,452
Provision for Eurobank loans and lease losses, net	15,813	17,398	279	33,490
Loans pools fully charged-off	(721)	(13,588)	(301)	(14,610)
Balance at end of period	**$ 32,685**	**$ 57,280**	**$ 367**	**$ 90,332**

	Nine-Month Period Ended September 30, 2015			
	Mortgage	Commercial and Construction	Consumer	Total
	(In thousands)			
Allowance for loan and lease losses for Eurobank loans:				
Balance at beginning of year	$ 15,522	$ 48,334	$ 389	$ 64,245
Provision for Eurobank loans and lease losses, net	17,779	20,136	279	38,194
FDIC shared-loss portion of provision for covered loan and lease losses, net	105	2,398	-	2,503
Loans pools fully charged-off	(721)	(13,588)	(301)	(14,610)
Balance at end of year	**$ 32,685**	**$ 57,280**	**$ 367**	**$ 90,332**

The FDIC shared-loss portion of provision for acquired Eurobank loans and lease losses, net, represents the credit impairment losses to be covered under the FDIC loss-share agreement which is increasing the FDIC loss-share indemnification asset.

The FDIC loss sharing obligation, related to commercial and other-non single family acquired Eurobank loans expired on June 30, 2015. The coverage for the single family residential loans will expire on June 30, 2020. The remaining covered loans are included as part of acquired Eurobank loans under the name "loans secured by 1-4 family residential properties." At September 30, 2016 and December 31, 2015, allowance for loan losses on loans covered by the FDIC shared-loss agreement amounted to $12.3 million and $22.6 million, respectively. The provision for covered loan and lease losses for the quarters ended September 30, 2016 and 2015 was $893 thousand and $15.8 million, respectively. The provision for covered loan and lease losses for the nine-month periods ended September 30, 2016 and 2015 was $1.1 million and $20.5 million, respectively.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 6- FDIC INDEMNIFICATION ASSET, TRUE-UP PAYMENT OBLIGATION, AND FDIC SHARED-LOSS EXPENSE

In connection with the FDIC-assisted acquisition, the Bank and the FDIC entered into shared-loss agreements pursuant to which the FDIC covers a substantial portion of any losses on loans (and related unfunded loan commitments), foreclosed real estate and other repossessed properties covered by the agreements.

The acquired loans, foreclosed real estate, and other repossessed properties subject to the shared-loss agreements are collectively referred to as “covered assets.” Under the terms of the shared-loss agreements, the FDIC absorbs 80% of losses and shares in 80% of loss recoveries on covered assets. The term of the shared-loss agreement covering single family residential mortgage loans is ten years with respect to losses and loss recoveries, while the term of the shared-loss agreement covering commercial loans is five years with respect to losses and eight years with respect to loss recoveries, from the end of the quarter of the acquisition. The coverage under the commercial shared-loss agreement expired on June 30, 2015. The shared-loss agreements also provide for certain costs directly related to the collection and preservation of covered assets to be reimbursed at an 80% level. The FDIC indemnification asset represents the portion of estimated losses covered by the shared-loss agreements between the Bank and the FDIC.

The following table presents the activity in the FDIC indemnification asset and true-up payment obligation for the quarters and nine-month periods ended September 30, 2016 and 2015:

	Quarter Ended September 30,		Nine-Month Period Ended September 30,	
	2016	2015	2016	2015
	(In thousands)			
<u>**FDIC indemnification asset:**</u>				
Balance at beginning of period	$ 18,426	$ 22,704	$ 22,599	$ 97,378
Shared-loss agreements reimbursements from the FDIC	(87)	-	(824)	(17,171)
Shared-loss agreements reimbursements expected from the FDIC	-	-	-	(20,917)
Increase in expected credit losses to be covered under shared-loss agreements, net	818	-	3,213	2,503
FDIC indemnification asset expense	(1,910)	(1,215)	(6,179)	(35,948)
Net expenses (reimbursed) incurred under shared-loss agreement	(577)	1,406	(2,139)	(2,950)
Balance at end of period	**$ 16,670**	**$ 22,895**	**$ 16,670**	**$ 22,895**
<u>**True-up payment obligation:**</u>				
Balance at beginning of period	$ 25,771	$ 23,577	$ 24,658	$ 21,981
Change in true-up payment obligation	508	864	1,621	2,460
Balance at end of period	**$ 26,279**	**$ 24,441**	**$ 26,279**	**$ 24,441**

The FDIC shared-loss expense bears an inverse relationship with a change in the yield of covered loan pools in accordance with ASC 310-30. ASC 310-30 dictates that such pools should be subject to increases in their yield when the present value of the expected cash flows is higher than the pool's carrying balance. When the increases in cash flow expectations are driven by reductions in the expected credit losses, the Bank recognizes that such losses are no longer expected to be collected from the FDIC. Accordingly, the Bank reduces the FDIC indemnification asset by amortizing the reduction in expected collections throughout the remaining life of the underlying pools. This amortization is recognized in the FDIC shared-loss expense account.

The underlying factors that caused an increase in the expected cash flows and resulting reduction in projected losses are derived from the pool-level cash flow forecasts. Credit loss assumptions used to develop each pool-level cash flow forecast are based on the behavior of defaults, recoveries and losses of the corresponding pool of covered loans.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The FDIC indemnification asset shared-loss expense for the quarters ended September 30, 2016 and 2015 amounted to $1.9 million and $1.2 million, respectively. The expense for the nine-month periods ended September 30, 2016 and 2015 amounted to of $6.2 million and $35.9 million, respectively. The FDIC loss-share coverage for the commercial loans was in effect until June 30, 2015. Accordingly, the Company amortized the remaining portion of the FDIC indemnification asset attributable to non-single family loans at the close of the second quarter of 2015. At September 30, 2016 and December 31, 2015, the FDIC indemnification asset reflects only the balance for single family residential mortgage loans.

The Company has owed payments to the FDIC for the recovery of prior claims for non-single family loans. At September 30, 2016, the liability for these payments amounted to $278 thousand and is recorded in other liabilities in the consolidated statements of financial condition until cash is paid to the FDIC. There was no liability at September 30, 2015.

Also in connection with the FDIC-assisted acquisition, the Bank agreed to make a true-up payment, also known as clawback liability or clawback provision, to the FDIC on the date that is 45 days following the last day (such day, the "True-Up Measurement Date") of the final shared-loss month, or upon the final disposition of all covered assets under the shared-loss agreements in the event losses thereunder fail to reach expected levels. Under the shared-loss agreements, the Bank will pay to the FDIC 50% of the excess, if any, of: (i) 20% of the Intrinsic Loss Estimate of $906.0 million (or $181.2 million) (as determined by the FDIC) less (ii) the sum of: (A) 25% of the asset discount (per bid) (or $227.5 million); plus (B) 25% of the cumulative shared-loss payments (defined as the aggregate of all of the payments made or payable to the Bank minus the aggregate of all of the payments made or payable to the FDIC); plus (C) the sum of the period servicing amounts for every consecutive twelve-month period prior to and ending on the True-Up Measurement Date in respect of each of the shared-loss agreements during which the shared-loss provisions of the applicable shared-loss agreement is in effect (defined as the product of the simple average of the principal amount of shared-loss loans and shared-loss assets at the beginning and end of such period times 1%). The estimated liability is included within accrued expenses and other liabilities in the unaudited consolidated statements of financial condition.

This true-up payment obligation may increase if actual and expected losses decline. The Company measures the true-up payment obligation at fair value. The changes in fair value are included as a change in true-up payment obligation within the FDIC shared-loss expense, net, in the unaudited consolidated statements of operations.

The following table provides the fair value and the undiscounted amount of the true-up payment obligation at September 30, 2016 and December 31, 2015:

	September 30, 2016	December 31, 2015

		(In thousands)		
Carrying amount (fair value)	$	26,279	$	24,658
Undiscounted amount	$	33,661	$	34,956

In connection with the FDIC-assisted acquisition, the Company recognized an FDIC shared-loss expense, net, in the unaudited consolidated statements of operations, which consists of the following for the quarters and nine-month periods ended September 30, 2016 and 2015:

	Quarter Ended September 30,				Nine-Month Period Ended September 30,			
	2016		2015		2016		2015	
	(In thousands)				(In thousands)			
FDIC indemnification asset expense	$	1,910	$	1,215	$	6,179	$	35,948
Change in true-up payment obligation		508		864		1,621		2,460
Reimbursement to FDIC for recoveries		878		-		2,945		-
Total FDIC shared-loss expense, net	**$**	**3,296**	**$**	**2,079**	**$**	**10,745**	**$**	**38,408**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 7 — DERIVATIVES

The following table presents the Company's derivative assets and liabilities at September 30, 2016 and December 31, 2015:

	September 30, 2016	December 31, 2015
	(In thousands)	
Derivative assets:		
Interest rate swaps not designated as hedges	$ 1,481	$ 1,819
Interest rate caps	22	32
Options tied to S&P 500 Index	-	1,170
Other	-	4
	$ 1,503	**$ 3,025**
Derivative liabilities:		
Interest rate swaps designated as cash flow hedges	$ 2,803	$ 4,307
Interest rate swaps not designated as hedges	1,481	1,819
Interest rate caps	22	32
Other	-	4
	$ 4,306	**$ 6,162**

Interest Rate Swaps

The Company enters into interest rate swap contracts to hedge the variability of future interest cash flows of forecasted wholesale borrowings attributable to changes in a predetermined variable index rate. The interest rate swaps effectively fix the Company's interest payments on an amount of forecasted interest expense attributable to the variable index rate corresponding to the swap notional stated rate. These swaps are designated as cash flow hedges for the forecasted wholesale borrowing transactions, are properly documented as such, and therefore, qualify for cash flow hedge accounting. Any gain or loss associated with the effective portion of the cash flow hedges is recognized in other comprehensive income (loss) and is subsequently reclassified into operations in the period during which the hedged forecasted transactions affect earnings. Changes in the fair value of these derivatives are recorded in accumulated other comprehensive income to the extent there is no significant ineffectiveness in the cash flow hedging relationships. Currently, the Company does not expect to reclassify any amount included in other comprehensive income (loss) related to these interest rate swaps to operations in the next twelve months.

The following table shows a summary of these swaps and their terms at September 30, 2016:

Type		Notional Amount (In thousands)	Fixed Rate	Variable Rate Index	Trade Date	Settlement Date	Maturity Date
Interest Rate Swaps	**$**	**36,938**	2.4210%	1-Month LIBOR	07/03/13	07/03/13	08/01/23

An accumulated unrealized loss of $2.8 million and $4.3 million was recognized in accumulated other comprehensive income related to the valuation of these swaps at September 30, 2016 and December 31, 2015, respectively, and the related liability is being reflected in the accompanying unaudited consolidated statements of financial condition.

At September 30, 2016 and December 31, 2015, interest rate swaps not designated as hedging instruments that were offered to clients represented an asset of $1.5 million and $1.8 million, respectively, and were included as part of derivative assets in the unaudited consolidated statements of financial position. The credit risk to these clients stemming from these derivatives, if any, is not material. At September 30, 2016 and December 31, 2015, interest rate swaps not designated as hedging instruments that are the mirror-images of the derivatives offered to clients represented a liability of $1.5 million and $1.8 million, respectively, and were included as part of derivative liabilities in the unaudited consolidated statements of financial condition.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following table shows a summary of these interest rate swaps not designated as hedging instruments and their terms at September 30, 2016:

Type	Notional Amount (In thousands)	Fixed Rate	Variable Rate Index	Settlement Date	Maturity Date
Interest Rate Swaps - Derivatives Offered to Clients	**$ 12,500**	5.5050%	1-Month LIBOR	04/11/09	04/11/19
Interest Rate Swaps - Mirror Image Derivatives	**$ 12,500**	5.5050%	1-Month LIBOR	04/11/09	04/11/19

Interest Rate Caps

The Company has entered into interest rate cap transactions with various clients with floating-rate debt who wish to protect their financial results against increases in interest rates. In these cases, the Company simultaneously enters into mirror-image interest rate cap transactions with financial counterparties. None of these cap transactions qualify for hedge accounting, and therefore, they are marked to market through earnings. As of September 30, 2016 and December 31, 2015, the outstanding total notional amount of interest rate caps was $124.4 million and $109.8 million, respectively. At September 30, 2016 and December 31, 2015, the interest rate caps sold to clients represented a liability of $22 thousand and $32 thousand, respectively, and were included as part of derivative liabilities in the unaudited consolidated statements of financial condition. At September 30, 2016 and December 31, 2015, the interest rate caps purchased as mirror-images represented an asset of $22 thousand and $32 thousand, respectively, and were included as part of derivative assets in the unaudited consolidated statements of financial condition.

Options Tied to Standard & Poor's 500 Stock Market Index

In the past, the Company offered its customers certificates of deposit with an option tied to the performance of the S&P 500 Index. The Company used option agreements with major broker-dealers to manage its exposure to changes in this index. Under the terms of the option agreements, the Company received the average increase in the month-end value of the index in exchange for a fixed premium. The changes in fair value of the option agreements used to manage the exposure in the stock market in the certificates of deposit were recorded in earnings. At September 30, 2016 there were no transactions outstanding. At December 31, 2015, the purchased options used to manage exposure to the S&P 500 Index on stock indexed deposits represented an asset of $1.2 million (notional amount of $3.4 million), and the options sold to customers embedded in the certificates of deposit and recorded as deposits in the unaudited consolidated statements of financial condition, represented a liability of $1.1 million (notional amount of $3.2 million).

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 8 — ACCRUED INTEREST RECEIVABLE AND OTHER ASSETS

Accrued interest receivable at September 30, 2016 and December 31, 2015 consists of the following:

	September 30, 2016	December 31, 2015
	(In thousands)	
Loans, excluding acquired loans	$ 14,644	$ 16,020
Investments	3,322	4,617
	$ 17,966	**$ 20,637**

Other assets at September 30, 2016 and December 31, 2015 consist of the following:

	September 30, 2016	December 31, 2015
	(In thousands)	
Prepaid expenses	19,514	11,762
Other repossessed assets	3,449	6,226
Core deposit and customer relationship intangibles	6,579	7,838
Mortgage tax credits	6,277	6,277
Investment in Statutory Trust	1,083	1,083
Accounts receivable and other assets	49,733	42,786
	$ 86,635	**$ 75,972**

Prepaid expenses amounting to $19.5 million and $11.8 million at September 30, 2016 and December 31, 2015, respectively, include prepaid municipal, property and income taxes aggregating to $14.1 million and $7.0 million, respectively.

In connection with the FDIC-assisted acquisition and the BBVAPR Acquisition, the Company recorded a core deposit intangible representing the value of checking and savings deposits acquired. At September 30, 2016 and December 31, 2015 this core deposit intangible amounted to $4.5 million and $5.3 million, respectively. In addition, the Company recorded a customer relationship intangible representing the value of customer relationships acquired with the acquisition of the securities broker-dealer and insurance agency in the BBVAPR Acquisition. At September 30, 2016 and December 31, 2015 this customer relationship intangible amounted to $2.1 million and $2.5 million, respectively.

Other repossessed assets totaled \$3.4 million at September 30, 2016 and \$6.2 million at December 31, 2015, include repossessed automobiles amounting to \$3.1 million and \$5.5 million, respectively, which are recorded at their net realizable value.

At September 30, 2016 and December 31, 2015, mortgage tax credits for the Company totaled \$6.3 million for both periods. These tax credits do not have an expiration date.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 9— DEPOSITS AND RELATED INTEREST

Total deposits, including related accrued interest payable, as of September 30, 2016 and December 31, 2015 consists of the following:

		September 30, 2016		December 31, 2015
		(In thousands)		
Non-interest bearing demand deposits	$	818,153	$	762,009
Interest-bearing savings and demand deposits		2,312,885		2,208,180
Individual retirement accounts		267,955		268,799
Retail certificates of deposit		549,945		441,998
Institutional certificates of deposit		224,672		253,791
Total core deposits		**4,173,610**		**3,934,777**
Brokered deposits		581,161		782,974
Total deposits	$	**4,754,771**	$	**4,717,751**

Brokered deposits include $515.9 million in certificates of deposits and $65.3 million in money market accounts at September 30, 2016, and $711.4 million in certificates of deposits and $71.6 million in money market accounts at December 31, 2015.

The weighted average interest rate of the Company’s deposits was 0.62% and 0.57% at September 30, 2016 and December 31, 2015, respectively. Interest expense for the quarters and nine-month periods ended September 30, 2016 and 2015 was as follows:

	Quarter Ended September 30,				Nine-Month Period Ended September 30,			
	2016		2015		2016		2015	
	(In thousands)				(In thousands)			
Demand and savings deposits	$	3,035	$	2,987	$	9,061	$	9,469
Certificates of deposit		4,296		3,664		12,761		10,890
	$	**7,331**	**$**	**6,651**	**$**	**21,822**	**$**	**20,359**

At September 30, 2016 and December 31, 2015, demand and interest-bearing deposits and certificates of deposit included deposits of the Puerto Rico Cash & Money Market Fund, Inc., which amounted to $114.8 million and $103.7 million, respectively, with a weighted average rate of 0.77% for both periods, and were collateralized with investment securities with a fair value of $87.4 million and $81.6 million, respectively.

At September 30, 2016 and December 31, 2015, time deposits in denominations of $250 thousand or higher, excluding accrued interest and unamortized discounts, amounted to $371.3 million and $376.8 million, respectively. Such amounts include public fund time deposits from various Puerto Rico government municipalities, agencies, and corporations of $9.2 million and $7.6 million at a weighted average rate of 0.45% and 0.49% at September 30, 2016 and December 31, 2015, respectively.

At September 30, 2016 and December 31, 2015, total public fund deposits from various Puerto Rico government municipalities, agencies, and corporations amounted to $165.0 million and $99.0 million, respectively. These public funds were collateralized with commercial loans amounting to $209.3 million and $410.9 million at September 30, 2016 and December 31, 2015, respectively.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Excluding accrued interest of $1.5 million and unamortized deposit discount in the amount of $72 thousand at September 30, 2016, and accrued interest of $1.5 million, unamortized deposit discount of $311 thousand and equity indexed options of $1.1 million at December 31, 2015, the scheduled maturities of certificates of deposit are as follows:

	September 30, 2016	December 31, 2015
	(In thousands)	
Within one year:		
Three (3) months or less	$ 197,615	$ 474,051
Over 3 months through 1 year	592,382	501,551
	789,997	**975,602**
Over 1 through 2 years	514,665	454,906
Over 2 through 3 years	165,838	176,406
Over 3 through 4 years	42,569	32,396
Over 4 through 5 years	43,816	33,715
	$ 1,556,885	**$ 1,673,025**

The table of scheduled maturities of certificates of deposits above includes brokered-deposits and individual retirement accounts.

The aggregate amount of overdrafts in demand deposit accounts that were reclassified to loans amounted to $780 thousand as of September 30, 2016 and $1.5 million as of December 31, 2015.

NOTE 10 — BORROWINGS AND RELATED INTEREST

Securities Sold under Agreements to Repurchase

At September 30, 2016, securities underlying agreements to repurchase were delivered to, and are being held by, the counterparties with whom the repurchase agreements were transacted. The counterparties have agreed to resell to the Company the same or similar securities at the maturity of these agreements.

At September 30, 2016 and December 31, 2015, securities sold under agreements to repurchase (classified by counterparty), excluding accrued interest in the amount of $1.6 million and $2.2 million, respectively, were as follows:

	September 30, 2016		December 31, 2015	
	Borrowing Balance	Fair Value of Underlying Collateral	Borrowing Balance	Fair Value of Underlying Collateral
	(In thousands)			
Federal Home Loan Bank of NY	42,135	44,883	-	-
JP Morgan Chase Bank NA	$ 212,500	$ 231,967	$ 262,500	$ 283,483
Credit Suisse Securities (USA) LLC	402,000	429,111	670,000	737,887
Total	**$ 656,635**	**$ 705,961**	**$ 932,500**	**$ 1,021,370**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following table shows a summary of the Company's repurchase agreements and their terms, excluding accrued interest in the amount of $1.6 million, at September 30, 2016:

Year of Maturity		Borrowing Balance (In thousands)	Weighted-Average Coupon	Settlement Date	Maturity Date
2016	$	21,635	0.570%	09/20/16	10/07/16
		20,500	0.510%	09/30/16	10/07/16
		170,000	1.500%	12/06/12	12/08/16
2017		232,000	4.780%	3/2/2007	3/2/2017
2018		212,500	1.420%	12/10/2012	04/29/18
	$	**656,635**	**2.57%**		

A repurchase agreement in the original amount of $500 million with an original term of ten years, maturing on March 2, 2017, was modified in February 2016 to terminate, before maturity, $268.0 million of this repurchase agreement at a cost of $12.0 million, included as a loss on early extinguishment of debt in the unaudited statements of operations. The remaining balance of this repurchase agreement was $232.0 million at September 30, 2016.

The following table presents the repurchase liability associated with the repurchase agreement transactions (excluding accrued interest) by maturity. Also, it includes the carrying value and approximate market value of collateral (excluding accrued interest) at September 30, 2016 and December 31, 2015. There was no cash collateral at September 30, 2016 and December 31, 2015.

	September 30, 2016										
				Market Value of Underlying Collateral							
	Repurchase Liability		Weighted Average Rate	FNMA and FHLMC Certificates		GNMA Certificates		US Treasury Treasury Notes		Total	
	(Dollars in thousands)										
Less than 90 days	$	212,135	1.31%	$	197,936	$	437	$	23,817	$	222,190
Over 90 days	$	444,500	3.17%	$	481,455	$	1,115	$	1,201	$	483,771
Total	**$**	**656,635**	**2.57%**	**$**	**679,391**	**$**	**1,552**	**$**	**25,018**	**$**	**705,961**

December 31, 2015

Market Value of Underlying Collateral

	Repurchase Liability	Weighted Average Rate	FNMA and FHLMC Certificates	GNMA Certificates	US Treasury Treasury Notes	Total
			(Dollars in thousands)			
Less than 90 days	$ 30,000	0.70%	$ 31,961	$ -	$ -	$ 31,961
Over 90 days	902,500	3.18%	974,698	2,131	12,580	989,409
Total	**$ 932,500**	**3.10%**	**$ 1,006,659**	**$ 2,131**	**$ 12,580**	**$ 1,021,370**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Advances from the Federal Home Loan Bank of New York

Advances are received from the Federal Home Loan Bank of New York (the "FHLB-NY") under an agreement whereby the Company is required to maintain a minimum amount of qualifying collateral with a fair value of at least 110% of the outstanding advances. At September 30, 2016 and December 31, 2015, these advances were secured by mortgage and commercial loans amounting to $1.5 billion and $1.3 billion, respectively. Also, at September 30, 2016 and December 31, 2015, the Company had an additional borrowing capacity with the FHLB-NY of $1.1 billion and $770.6 million, respectively. At September 30, 2016 and December 31, 2015, the weighted average remaining maturity of FHLB's advances was 12.5 months and 6.3 months, respectively. The original terms of these advances ranges between one month and seven years, and the FHLB-NY does not have the right to exercise put options at par on any advances outstanding as of September 30, 2016.

The following table shows a summary of these advances and their terms, excluding accrued interest in the amount of $293 thousand, at September 30, 2016:

Year of Maturity		Borrowing Balance	Weighted-Average Coupon	Settlement Date	Maturity Date
		(In thousands)			
2016	$	36,938	0.57%	9/1/2016	10/3/2016
2017		4,091	1.24%	4/3/2012	4/3/2017
2018		30,000	2.19%	1/16/2013	1/16/2018
		25,000	2.18%	1/16/2013	1/16/2018
		55,000			
2020		9,623	2.59%	7/19/2013	7/20/2020
	$	**105,652**	**1.61%**		

All of the advances referred to above with maturity dates up to the date of this report were renewed as one-month short-term advances.

Subordinated Capital Notes

Outstanding subordinated capital notes amounted to $36.1 million and $102.6 million at September 30, 2016 and December 31, 2015, respectively. On September 29, 2016, the Company repaid $67.0 million of subordinated capital notes at maturity.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 11 – OFFSETTING OF FINANCIAL ASSETS AND LIABILITIES

The Company's derivatives are subject to agreements which allow a right of set-off with each respective counterparty. In addition, the Company's securities purchased under agreements to resell and securities sold under agreements to repurchase have a right of set-off with the respective counterparty under the supplemental terms of the master repurchase agreements. In an event of default, each party has a right of set-off against the other party for amounts owed in the related agreements and any other amount or obligation owed in respect of any other agreement or transaction between them. Security collateral posted to open and maintain a master netting agreement with a counterparty, in the form of cash and securities, may from time to time be segregated in an account at a third-party custodian pursuant to a an account control agreement.

The following table presents the potential effect of rights of set-off associated with the Company's recognized financial assets and liabilities at September 30, 2016 and December 31, 2015:

	September 30, 2016					
				Gross Amounts Not Offset in the Statement of Financial Condition		
	Gross Amount of Recognized Assets	Gross Amounts Offset in the Statement of Financial Condition	Net Amount of Assets Presented in Statement of Financial Condition	Financial Instruments	Cash Collateral Received	Net Amount
	(In thousands)					
Derivatives	$ 1,503	$ -	$ 1,503	$ 2,005	$ -	$ (502)

	December 31, 2015				
				Gross Amounts Not Offset in the Statement of Financial Condition	
	Gross Amount	Gross Amounts Offset in the Statement of	Net amount of Assets Presented in Statement		Cash

	of Recognized Assets		Financial Condition		of Financial Condition		Financial Instruments		Collateral Received		Net Amount
					(In thousands)						
Derivatives	$	3,025	$	-	$	3,025	$	2,000	$	-	$	1,025

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

September 30, 2016

	Gross Amount of Recognized Liabilities	Gross Amounts Offset in the Statement of Financial Condition	Net Amount of Liabilities Presented in Statement of Financial Condition	Gross Amounts Not Offset in the Statement of Financial Condition: Financial Instruments	Gross Amounts Not Offset in the Statement of Financial Condition: Cash Collateral Provided	Net Amount
	(In thousands)					
Derivatives	$ 4,306	$ -	$ 4,306	$ -	$ 1,980	$ 2,326
Securities sold under agreements to repurchase	656,635	-	656,635	705,961	-	(49,326)
Total	**$ 660,941**	**$ -**	**$ 660,941**	**$ 705,961**	**$ 1,980**	**$ (47,000)**

December 31, 2015

	Gross Amount of Recognized Liabilities	Gross Amounts Offset in the Statement of Financial Condition	Net Amount of Liabilities Presented in Statement of Financial Condition	Gross Amounts Not Offset in the Statement of Financial Condition: Financial Instruments	Gross Amounts Not Offset in the Statement of Financial Condition: Cash Collateral Provided	Net Amount
	(In thousands)					
Derivatives	$ 7,257	$ -	$ 7,257	$ -	$ 1,980	$ 5,277
Securities sold under agreements to repurchase	932,500	-	932,500	1,021,370	-	(88,870)
Total	**$ 939,757**	**$ -**	**$ 939,757**	**$ 1,021,370**	**$ 1,980**	**$ (83,593)**

NOTE 12 — RELATED PARTY TRANSACTIONS

The Bank grants loans to its directors, executive officers and certain related individuals or organizations in the ordinary course of business. These loans are offered at the same terms as loans to unrelated third parties. The activity and balance of these loans for the quarters and nine-month periods ended September 30, 2016 and 2015 was as follows:

	Quarter Ended September 30,		Nine-Month Period Ended September 30,	
	2016	2015	2016	2015
	(In thousands)		(In thousands)	
Balance at the beginning of year	$ 30,696	$ 33,318	$ 31,475	$ 27,011
New loans and disbursements	225	5,866	727	13,489
Repayments	(2,376)	(7,450)	(3,657)	(8,766)
Balance at the end of period	**$ 28,545**	**$ 31,734**	**$ 28,545**	**$ 31,734**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 13 — INCOME TAXES

At September 30, 2016 and December 31, 2015, the Company's net deferred tax asset amounted to $131.1 million and $145.9 million, respectively. In assessing the realizability of the deferred tax asset, management considers whether it is more likely than not that some portion or the entire deferred tax asset will not be realized. The ultimate realization of the deferred tax asset is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. Based upon the level of historical taxable income and projections for future taxable income over the periods in which the deferred tax asset are deductible, management believes it is more likely than not that the Company will realize the deferred tax asset, net of any existing valuation allowances recorded at September 30, 2016 and December 31, 2015. The amount of the deferred tax asset that is considered realizable could be reduced in the near term if estimates of future taxable income during the carry forward period are reduced.

At September 30, 2016 and December 31, 2015 OIB, the Bank's international banking entity subsidiary, had $117 thousand and $141 thousand, respectively, in income tax effect of unrecognized gain on available-for-sale securities included in other comprehensive income. Following the change in OIB's applicable tax rate from 5% to 0% as a result of a Puerto Rico law adopted in 2011, this remaining tax balance will flow through income as these securities are repaid or sold in future periods. During the quarters ended September 30, 2016 and 2015, $9 thousand and $11 thousand, respectively, related to this residual tax effect from OIB was reclassified from accumulated other comprehensive income into income tax provision. During the nine-month periods ended September 30, 2016 and 2015, $24 thousand and $33 thousand, respectively, related to this residual tax effect from OIB was reclassified from accumulated other comprehensive income into income tax provision.

The Company classifies unrecognized tax benefits in other liabilities. These gross unrecognized tax benefits would affect the effective tax rate if realized. The balance of unrecognized tax benefits was $2.0 million at September 30, 2016 and $2.2 million at December 31, 2015. The Company had accrued $112 thousand at September 30, 2016 and $175 thousand at December 31, 2015 for the payment of interest and penalties relating to unrecognized tax benefits. During the quarter ended September 30, 2016, the Company increased unrecognized tax benefits by $1.1 million and released $1.3 million due to the expiration of the statute of limitations.

Income tax expense for the quarters ended September 30, 2016 and 2015 was $3.6 million and $562 thousand, respectively. Income tax expense for the nine-month periods ended September 30, 2016 and 2015 was $15.1 million and $2.3 million, respectively.

NOTE 14 — REGULATORY CAPITAL REQUIREMENTS

Regulatory Capital Requirements

The Company (on a consolidated basis) and the Bank are subject to various regulatory capital requirements administered by federal and Puerto Rico 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 effect on the Company's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Bank must meet specific capital guidelines that involve quantitative measures of their assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Pursuant to the Dodd-Frank Act, federal banking regulators have adopted new capital rules that became effective January 1, 2015 for the Company and the Bank (subject to certain phase-in periods through January 1, 2019) and that replaced their general risk-based capital rules, advanced approaches rule, market risk rule, and leverage rules. Among other matters, the new capital rules: (i) introduce a new capital measure called "Common Equity Tier 1" ("CET1") and related regulatory capital ratio of CET1 to risk-weighted assets; (ii) specify that Tier 1 capital consists of CET1 and "Additional Tier 1 capital" instruments meeting certain revised requirements; (iii) mandate that most deductions/adjustments to regulatory capital measures be made to CET1 and not to the other components of capital; and (iv) expand the scope of the deductions from and adjustments to capital as compared to prior regulations. The new capital rules prescribe a new standardized approach for risk weightings that expand the risk-weighting categories from the current four Basel I-derived categories (0%, 20%, 50% and 100%) to a larger and more risk-sensitive number of categories, depending on the nature of the assets, and resulting in higher risk weights for a variety of asset classes.

Pursuant to the new capital rules, the minimum capital ratios requirements as of January 1, 2015 are as follows:

4.5% CET1 to risk-weighted assets;

6.0% Tier 1 capital (that is, CET1 *plus* Additional Tier 1 capital) to risk-weighted assets;

8.0% Total capital (that is, Tier 1 capital *plus* Tier 2 capital) to risk-weighted assets; and

4.0% Tier 1 capital to average consolidated assets as reported on consolidated financial statements (known as the "leverage ratio").

As of September 30, 2016 and December 31, 2015, the Company and the Bank met all capital adequacy requirements to which they are subject. As of September 30, 2016 and December 31, 2015, the Bank is "well capitalized" under the regulatory framework for prompt corrective action. To be categorized as "well capitalized," an institution must maintain minimum CET1 risk-based, Tier 1 risk-based, total risk-based, and Tier 1 leverage ratios as set forth in the tables presented below.

The New Capital Rules also introduce a new 2.5% "capital conservation buffer", composed entirely of CET1, on top of the three minimum risk-weighted asset ratios. The capital conservation buffer is designed to absorb losses during periods of economic stress. Banking institutions with a ratio of CET1 to risk-weighted assets above the minimum but below the capital conservation buffer will face constraints on dividends, equity repurchases and compensation based on the amount of the shortfall. Thus, when fully phased-in on January 1, 2019, the Company and the Bank will be required to maintain such an additional capital conservation buffer of 2.5% of CET1, effectively resulting in minimum ratios of (i) CET1 to risk-weighted assets of at least 7%, (ii) Tier 1 capital to risk-weighted assets of at least 8.5%, and (iii) Total capital to risk-weighted assets of at least 10.5%. The implementation of the capital conservation buffer began on January 1, 2016 at the 0.625% level and increase by 0.625% on each subsequent January 1, until it reaches 2.5% on January 1, 2019. At September 30, 2016 the Company and the Bank met the capital buffer requirement.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The Company's and the Bank's actual capital amounts and ratios as of September 30, 2016 and December 31, 2015 are as follows:

	Actual		Minimum Capital Requirement		Minimum to be Well Capitalized	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(Dollars in thousands)			
Company Ratios						
As of September 30, 2016						
Total capital to risk-weighted assets	$ 860,581	**18.71%**	$ 367,907	**8.00%**	$ 459,884	**10.00%**
Tier 1 capital to risk-weighted assets	$ 801,882	**17.44%**	$ 275,930	**6.00%**	$ 367,907	**8.00%**
Common equity tier 1 capital to risk-weighted assets	$ 612,792	**13.32%**	$ 206,948	**4.50%**	$ 298,924	**6.50%**
Tier 1 capital to average total assets	$ 801,882	**12.35%**	$ 259,711	**4.00%**	$ 324,639	**5.00%**
As of December 31, 2015						
Total capital to risk-weighted assets	$ 846,748	**17.29%**	$ 391,723	**8.00%**	$ 489,654	**10.00%**
Tier 1 capital to risk-weighted assets	$ 782,912	**15.99%**	$ 293,792	**6.00%**	$ 391,723	**8.00%**
Common equity tier 1 capital to risk-weighted assets	$ 594,482	**12.14%**	$ 220,344	**4.50%**	$ 318,275	**6.50%**
Tier 1 capital to average total assets	$ 782,912	**11.18%**	$ 280,009	**4.00%**	$ 350,011	**5.00%**

	Actual		Minimum Capital Requirement		Minimum to be Well Capitalized	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(Dollars in thousands)			
Bank Ratios						
As of September 30, 2016						
Total capital to risk-weighted assets	$ 841,599	**18.33%**	$ 367,256	**8.00%**	$ 459,070	**10.00%**
Tier 1 capital to risk-weighted assets	$ 783,151	**17.06%**	$ 275,442	**6.00%**	$ 367,256	**8.00%**
Common equity tier 1 capital to risk-weighted assets	$ 783,151	**17.06%**	$ 206,582	**4.50%**	$ 298,396	**6.50%**
Tier 1 capital to average total assets	$ 783,151	**12.11%**	$ 258,600	**4.00%**	$ 323,250	**5.00%**
As of December 31, 2015						
Total capital to risk-weighted assets	$ 815,458	**16.70%**	$ 390,688	**8.00%**	$ 488,360	**10.00%**
Tier 1 capital to risk-weighted assets	$ 751,886	**15.40%**	$ 293,016	**6.00%**	$ 390,688	**8.00%**
Common equity tier 1 capital to risk-weighted assets	$ 751,886	**15.40%**	$ 219,762	**4.50%**	$ 317,434	**6.50%**
Tier 1 capital to average total assets	$ 751,886	**10.80%**	$ 278,399	**4.00%**	$ 347,999	**5.00%**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 15 – STOCKHOLDERS' EQUITY

Additional Paid-in Capital

Additional paid-in capital represents contributed capital in excess of par value of common and preferred stock net of the costs of issuance. As of September 30, 2016 and December 31, 2015 accumulated issuance costs charged against additional paid-in capital amounted to $13.6 million and $10.1 million for preferred and common stock, respectively.

Legal Surplus

The Puerto Rico Banking Act requires that a minimum of 10% of the Bank's net income for the year be transferred to a reserve fund until such fund (legal surplus) equals the total paid-in capital on common and preferred stock. At September 30, 2016 and December 31, 2015, the Bank's legal surplus amounted to $74.8 million and $70.4 million, respectively. The amount transferred to the legal surplus account is not available for the payment of dividends to shareholders.

Treasury Stock

Under the Company's current stock repurchase program it is authorized to purchase in the open market up to $70 million of its outstanding shares of common stock, of which approximately $7.7 million of authority remains. The shares of common stock repurchased are to be held by the Company as treasury shares. There were no repurchases during the nine-month period ended September 30, 2016. During the nine-month period ended September 30, 2015, the Company purchased 803,985 shares under this program for a total of $8.9 million at an average price of $11.10 per share.

The number of shares that may yet be purchased under the $70 million program is estimated at 764,674 and was calculated by dividing the remaining balance of $7.7 million by $10.11 (closing price of the Company common stock at September 30, 2016). The Company did not purchase any shares of its common stock during the nine-month period ended September 30, 2016 and 2015, other than through its publicly announced stock purchase program.

The activity in connection with common shares held in treasury by the Company for the nine-month periods ended September 30, 2016 and 2015 is set forth below:

	Nine-Month Period Ended September 30,			
	2016		2015	
	Shares	Dollar Amount	Shares	Dollar Amount
	(In thousands, except shares data)			
Beginning of period	8,757,960	$ 105,379	8,012,254	$ 97,070
Common shares used upon lapse of restricted stock units	(45,810)	(505)	(58,279)	(641)
Common shares repurchased as part of the stock repurchase program	-	-	803,985	8,950
End of period	**8,712,150**	**$ 104,874**	**8,757,960**	**$ 105,379**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 16 - ACCUMULATED OTHER COMPREHENSIVE INCOME

Accumulated other comprehensive income, net of income tax, as of September 30, 2016 and December 31, 2015 consisted of:

	September 30, 2016	December 31, 2015
	(In thousands)	
Unrealized gain on securities available-for-sale which are not other-than-temporarily impaired	$ 18,689	$ 22,044
Unrealized gain on securities available-for-sale which are other-than-temporarily impaired	-	(3,196)
Income tax effect of unrealized gain on securities available-for-sale	(1,136)	(1,924)
Net unrealized gain on securities available-for-sale which are not other-than-temporarily impaired, net of tax	17,553	16,924
Unrealized loss on cash flow hedges	(2,803)	(4,307)
Income tax effect of unrealized loss on cash flow hedges	1,094	1,380
Net unrealized loss on cash flow hedges	(1,709)	(2,927)
Accumulated other comprehensive income, net of taxes	**$ 15,844**	**$ 13,997**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following table presents changes in accumulated other comprehensive income by component, net of taxes, for the quarters and nine-month periods ended September 30, 2016 and 2015:

	Quarter		
	2016		
	Net unrealized gains on securities available-for-sale	**Net unrealized loss on cash flow hedges**	**Accu o compr in**
Beginning balance	$ 18,085	$ (2,280)	$ 1
Other comprehensive income (loss) before reclassifications	(469)	(144)	
Other-than-temporary impairment amount reclassified from accumulated other comprehensive income	-	-	
Amounts reclassified out of accumulated other comprehensive (loss) income	(63)	715	
Other comprehensive income (loss)	(532)	571	
Ending balance	**$ 17,553**	**$ (1,709)**	**$ 1**

	Nine-Month I		
	2016		
	Net unrealized gains on securities available-for-sale	**Net unrealized loss on cash flow hedges**	**Accu o compr in (**
Beginning balance	$ 16,924	$ (2,927)	$ 1
Other comprehensive (loss) before reclassifications	(1,732)	(2,550)	(4
Other-than-temporary impairment amount reclassified from accumulated other comprehensive income	2,557	-	
Amounts reclassified out of accumulated other comprehensive income (loss)	(196)	3,768	
Other comprehensive income (loss)	629	1,218	
Ending balance	**$ 17,553**	**$ (1,709)**	**$ 1**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following table presents reclassifications out of accumulated other comprehensive income for the quarters and nine-month periods ended September 30, 2016 and 2015:

	Amount reclassified out of accumulated other comprehensive income Quarter Ended September 30, 2016	2015	Affected Line Item in Consolidated Statement of Operations
	(In thousands)		
Cash flow hedges:			
Interest-rate contracts	$ 664	$ 1,622	Net interest expense
Tax effect from increase in capital gains tax rate	51	(75)	Income tax expense
Available-for-sale securities:			
Residual tax effect from OIB's change in applicable tax rate	9	11	Income tax expense
Other-than-temporary impairment losses on available for sale securities realized during the period	-	(246)	Net impairment losses recognized in
Tax effect from increase in capital gains tax rate	(72)	130	Income tax expense
	$ 652	**$ 1,442**	

	Amount reclassified out of accumulated other comprehensive income Nine-Month Period Ended September 30, 2016	2015	Affected Line Item in Consolidated Statement of Operations
	(In thousands)		
Cash flow hedges:			
Interest-rate contracts	$ 3,468	$ 4,842	Net interest expense
Tax effect from increase in capital gains tax rate	300	(224)	Income tax expense
Available-for-sale securities:			
Residual tax effect from OIB's change in applicable tax rate	24	33	Income tax expense
Other-than-temporary impairment losses on available for sale securities	-	(246)	Net impairment losses recognized in
Tax effect from increase in capital gains tax rate	(220)	387	Income tax expense
	$ 3,572	**$ 4,792**	

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 17 – EARNINGS (LOSS) PER COMMON SHARE

The calculation of earnings (loss) per common share for the quarters and nine-month periods ended September 30, 2016 and 2015 is as follows:

	Quarter Ended September 30,		Nine-Month Period Ende September 3	
	2016	2015	2016	201
	(In thousands, except per share data)		(In thousand except per sha data)	
Net income (loss)	$ 15,120	$ 4,569	$ 43,630	$ (1,5
Less: Dividends on preferred stock				
Non-convertible preferred stock (Series A, B, and D)	(1,627)	(1,627)	(4,883)	(4,8
Convertible preferred stock (Series C)	(1,838)	(1,838)	(5,513)	(5,5
Income (loss) available to common shareholders	**$ 11,655**	**$ 1,104**	**$ 33,234**	**$(11,9**
Effect of assumed conversion of the convertible preferred stock	1,838	1,838	5,513	5,
Income (loss) available to common shareholders assuming conversion	$ **13,493**	$ **2,942**	$ **38,747**	$ **(6,4**
Weighted average common shares and share equivalents:				
Average common shares outstanding	43,926	43,929	43,913	44,
Effect of dilutive securities:				
Average potential common shares-options	47	46	40	
Average potential common shares-assuming conversion of convertible preferred stock	7,138	7,171	7,138	7,
Total weighted average common shares outstanding and equivalents	**51,111**	**51,146**	**51,091**	**51,**
Earnings (loss) per common share - basic	**$ 0.27**	**$ 0.03**	**$ 0.76**	**$ (0**
Earnings (loss) per common share - diluted	**$ 0.26**	**$ 0.03**	**$ 0.76**	**$ (0**

In computing diluted earnings (loss) per common share, the 84,000 shares of convertible preferred stock, which remain outstanding at September 30, 2016, with a conversion rate, subject to certain conditions, of 86.4225 shares of common stock per share, were included as average potential common shares from the date they were issued and outstanding. Moreover, in computing diluted earnings (loss) per common share, the dividends declared during the quarters ended September 30, 2016 and 2015 on the convertible preferred stock were added back as income available to common shareholders.

For the quarters ended September 30, 2016 and 2015, weighted-average stock options with an anti-dilutive effect on earnings (loss) per share not included in the calculation amounted to 927,069 and 973,200, respectively. For the nine-month periods ended September 30, 2016 and 2015, weighted-average stock options with an anti-dilutive effect on earnings (loss) per share not included in the calculation amounted to 957,670 and 648,563, respectively.

NOTE 18 – GUARANTEES

At September 30, 2016, the unamortized balance of the obligations undertaken in issuing the guarantees under standby letters of credit represented a liability of $2.4 million (December 31, 2015 - $14.7 million).

As a result of the BBVAPR Acquisition, the Company assumed a liability for residential mortgage loans sold subject to credit recourse pursuant to FNMA's residential mortgage loan sales and securitization programs. At September 30, 2016 and December 31, 2015, the unpaid principal balance of residential mortgage loans sold subject to credit recourse was $20.4 million and $22.4 million, respectively.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following table shows the changes in the Company's liability for estimated losses from these credit recourse agreements, included in the unaudited consolidated statements of financial condition during the quarters and nine-month periods ended September 30, 2016 and 2015.

	Quarter Ended September 30,		Nine-Month Period Ended September 30,	
	2016	2015	2016	2015
	(In thousands)		(In thousands)	
Balance at beginning of period	$ 162	$ 289	$ 439	$ 927
Net (charge-offs/terminations) recoveries	29	140	(248)	(498)
Balance at end of period	**$ 191**	**$ 429**	**$ 191**	**$ 429**

The estimated losses to be absorbed under the credit recourse arrangements were recorded as a liability when the credit recourse was assumed, and are updated on a quarterly basis. The expected loss, which represents the amount expected to be lost on a given loan, considers the probability of default and loss severity. The probability of default represents the probability that a loan in good standing would become 120 days delinquent, in which case the Company is obligated to repurchase the loan. The recourse obligation will be fully extinguished before the end of 2017.

If a borrower defaults, pursuant to the credit recourse provided, the Company is required to repurchase the loan or reimburse the third party investor for the incurred loss. The maximum potential amount of future payments that the Company would be required to make under the recourse arrangements is equivalent to the total outstanding balance of the residential mortgage loans serviced with recourse and interest, if applicable. During the quarter and nine-month period ended September 30, 2016, the Company repurchased approximately $133 thousand and $421 thousand, respectively of unpaid principal balance in mortgage loans subject to the credit recourse provisions. During the quarter and nine-month period ended September 30, 2015, the Company repurchased approximately $165 thousand and $3.4 million, respectively of unpaid principal balance in mortgage loans subject to the credit recourse provisions. If a borrower defaults, the Company has rights to the underlying collateral securing the mortgage loan. The Company suffers losses on these mortgage loans when the proceeds from a foreclosure sale of the collateral property are less than the outstanding principal balance of the loan, any uncollected interest advanced, and the costs of holding and disposing the related property. At September 30, 2016, the Company's liability for estimated credit losses related to loans sold with credit recourse amounted to $191 thousand (December 31, 2015– $439 thousand).

When the Company sells or securitizes mortgage loans, it generally makes customary representations and warranties regarding the characteristics of the loans sold. The Company's mortgage operations division groups conforming mortgage loans into pools which are exchanged for FNMA and GNMA mortgage-backed securities that are generally sold to private investors, or are sold directly to FNMA or other private investors for cash. As required under such mortgage backed securities programs, quality review procedures are performed by the Company to ensure that asset guideline qualifications are met. To the extent the loans do not meet specified characteristics, the Company may be required to repurchase such loans or indemnify for losses and bear any subsequent loss related to the loans. During the quarter and nine-month period ended September 30, 2016, the Company repurchased $791 thousand and $3.1 million, respectively, of unpaid principal balance in mortgage loans, excluding mortgage loans subject to credit recourse provisions referred to above. During the quarter and nine-month period ended September 30, 2015, the Company repurchased $7.7 million and $19.5 million, respectively, of unpaid principal balance in mortgage loans, excluding mortgage loans subject to credit recourse provisions referred to above.

During the quarter and nine-month period ended September 30, 2016, the Company recognized $202 thousand and $313 thousand, respectively, in losses from the repurchase of residential mortgage loans sold subject to credit recourse, and $208 thousand and $1.0 million, respectively, in losses from the repurchase of residential mortgage loans as a result of breaches of the customary representations and warranties. During the quarter and nine -month period ended September 30, 2015, the Company recognized $418 thousand and $1.0 million, respectively, in losses from the repurchase of residential mortgage loans sold subject to credit recourse, and $500 thousand and $2.0 million, respectively, in losses from the repurchase of residential mortgage loans as a result of breaches of the customary representations and warranties.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Servicing agreements relating to the mortgage-backed securities programs of FNMA and GNMA, and to mortgage loans sold or serviced to certain other investors, including the Federal Home Loan Mortgage Corporation ("FHLMC"), require the Company to advance funds to make scheduled payments of principal, interest, taxes and insurance, if such payments have not been received from the borrowers. At September 30, 2016, the Company serviced $752.5 million in mortgage loans for third-parties. The Company generally recovers funds advanced pursuant to these arrangements from the mortgage owner, from liquidation proceeds when the mortgage loan is foreclosed or, in the case of FHA/VA loans, under the applicable FHA and VA insurance and guarantees programs. However, in the meantime, the Company must absorb the cost of the funds it advances during the time the advance is outstanding. The Company must also bear the costs of attempting to collect on delinquent and defaulted mortgage loans. In addition, if a defaulted loan is not cured, the mortgage loan would be canceled as part of the foreclosure proceedings and the Company would not receive any future servicing income with respect to that loan. At September 30, 2016, the outstanding balance of funds advanced by the Company under such mortgage loan servicing agreements was approximately $330 thousand (December 31, 2015 - $301 thousand). To the extent the mortgage loans underlying the Company's servicing portfolio experience increased delinquencies, the Company would be required to dedicate additional cash resources to comply with its obligation to advance funds as well as incur additional administrative costs related to increases in collection efforts.

NOTE 19— COMMITMENTS AND CONTINGENCIES

Loan Commitments

In the normal course of business, the Company becomes a party to credit-related financial instruments with off-balance-sheet risk to meet the financing needs of its customers. These financial instruments include commitments to extend credit, standby and commercial letters of credit, and financial guarantees. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amounts recognized in the consolidated statements of financial condition. The contract or notional amount of those instruments reflects the extent of the Company's involvement in particular types of financial instruments.

The Company's exposure to credit losses in the event of nonperformance by the counterparty to the financial instrument for commitments to extend credit, including commitments under credit card arrangements, and commercial letters of credit is represented by the contractual notional amounts of those instruments, which do not necessarily represent the amounts potentially subject to risk. In addition, the measurement of the risks associated with these instruments is meaningful only when all related and offsetting transactions are identified. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

Credit-related financial instruments at September 30, 2016 and December 31, 2015 were as follows:

	September 30, 2016	December 31, 2015

		(In thousands)		
Commitments to extend credit	$	516,134	$	456,720
Commercial letters of credit		1,386		1,508

Commitments to extend credit represent 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. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if it is deemed necessary by the Company upon the extension of credit, is based on management's credit evaluation of the counterparty.

At September 30, 2016 and December 31, 2015, commitments to extend credit consisted mainly of undisbursed available amounts on commercial lines of credit, construction loans, and revolving credit card arrangements. Since many of the unused commitments are expected to expire unused or be only partially used, the total amount of these unused commitments does not necessarily represent future cash requirements. These lines of credit had a reserve of $667 thousand at both September 30, 2016 and December 31, 2015.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Commercial letters of credit are issued or confirmed to guarantee payment of customers' payables or receivables in short-term international trade transactions. Generally, drafts will be drawn when the underlying transaction is consummated as intended. However, the short-term nature of this instrument serves to mitigate the risk associated with these contracts.

The summary of instruments that are considered financial guarantees in accordance with the authoritative guidance related to guarantor's accounting and disclosure requirements for guarantees, including indirect guarantees of indebtedness of others, at September 30, 2016 and December 31, 2015, is as follows:

	September 30, 2016	December 31, 2015
	(In thousands)	
Standby letters of credit and financial guarantees	$ 4,809	$ 14,656
Loans sold with recourse	20,394	22,374

Standby letters of credit and financial guarantees are written conditional commitments issued by the Company to guarantee the payment and/or performance of a customer to a third party ("beneficiary"). If the customer fails to comply with the agreement, the beneficiary may draw on the standby letter of credit or financial guarantee as a remedy. The amount of credit risk involved in issuing letters of credit in the event of nonperformance is the face amount of the letter of credit or financial guarantee. These guarantees are primarily issued to support public and private borrowing arrangements, including commercial paper, bond financing, and similar transactions. The amount of collateral obtained, if it is deemed necessary by the Company upon extension of credit, is based on management's credit evaluation of the customer.

Lease Commitments

The Company has entered into various operating lease agreements for branch facilities and administrative offices. Rent expense for the quarters ended September 30, 2016 and 2015, amounted to $2.0 million and $2.3 million, respectively. For the nine-month periods ended September 30, 2016 and 2015, rent expense amounted to $6.5 million and $7.0 million, respectively, and is included in the "occupancy and equipment" caption in the unaudited consolidated statements of operations. Future rental commitments under leases in effect at September 30, 2016 exclusive of taxes, insurance, and maintenance expenses payable by the Company, are summarized as follows:

Year Ending December 31,	Minimum Rent (In thousands)
2016	$ 1,864
2017	7,051
2018	6,512

2019		6,471
2020		5,744
Thereafter		12,563
	$	**40,205**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Contingencies

The Company and its subsidiaries are defendants in a number of legal proceedings incidental to their business. In the ordinary course of business, the Company and its subsidiaries are also subject to governmental and regulatory examinations. Certain subsidiaries of the Company, including the Bank (and its subsidiary OIB), Oriental Financial Services, and Oriental Insurance, are subject to regulation by various U.S., Puerto Rico and other regulators.

The Company seeks to resolve all litigation and regulatory matters in the manner management believes is in the best interests of the Company and its shareholders, and contests allegations of liability or wrongdoing and, where applicable, the amount of damages or scope of any penalties or other relief sought as appropriate in each pending matter.

Subject to the accounting and disclosure framework under the provisions of ASC 450, it is the opinion of the Company's management, based on current knowledge and after taking into account its current legal accruals, that the eventual outcome of all matters would not be likely to have a material adverse effect on the consolidated statements of financial condition of the Company. Nonetheless, given the substantial or indeterminate amounts sought in certain of these matters, and the inherent unpredictability of such matters, an adverse outcome in certain of these matters could, from time to time, have a material adverse effect on the Company's consolidated results of operations or cash flows in particular quarterly or annual periods. The Company has evaluated all litigation and regulatory matters where the likelihood of a potential loss is deemed reasonably possible. The Company has determined that the estimate of the reasonably possible loss is not significant.

NOTE 20 - FAIR VALUE OF FINANCIAL INSTRUMENTS

The Company follows the fair value measurement framework under GAAP.

Fair Value Measurement

The fair value measurement framework defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. This framework also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

Money market investments

The fair value of money market investments is based on the carrying amounts reflected in the unaudited consolidated statements of financial condition as these are reasonable estimates of fair value given the short-term nature of the instruments.

Investment securities

The fair value of investment securities is based on quoted market prices, when available, or market prices provided by Interactive Data Corporation ("IDC"), an independent, well-recognized pricing company. Such securities are classified as Level 1 or Level 2 depending on the basis for determining fair value. If listed prices or quotes are not available, fair value is based upon externally developed models that use both observable and unobservable inputs depending on the market activity of the instrument, and such securities are classified as Level 3. At September 30, 2016 and December 31, 2015, the Company did not have investment securities classified as Level 3.

Derivative instruments

The fair value of the interest rate swaps is largely a function of the financial market's expectations regarding the future direction of interest rates. Accordingly, current market values are not necessarily indicative of the future impact of derivative instruments on earnings. This will depend, for the most part, on the shape of the yield curve, the level of interest rates, as well as the expectations for rates in the future. The fair value of most of these derivative instruments is based on observable market parameters, which include discounting the instruments' cash flows using the U.S. dollar LIBOR-based discount rates, and also applying yield curves that account for the industry sector and the credit rating of the counterparty and/or the Company.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Certain other derivative instruments with limited market activity are valued using externally developed models that consider unobservable market parameters. Based on their valuation methodology, derivative instruments are classified as Level 2 or Level 3. In the past, the Company offered its customers certificates of deposit with an option tied to the performance of the S&P Index and used equity indexed option agreements with major broker-dealers to manage its exposure to changes in this index. Their fair value was obtained through the use of an external based valuation that was thoroughly evaluated and adopted by management as its measurement tool for these options. The payoff of these options was linked to the average value of the S&P Index on a specific set of dates during the life of the option. The methodology used an average rate option or a cash-settled option whose payoff was based on the difference between the expected average value of the S&P Index during the remaining life of the option and the strike price at inception. The assumptions, which were uncertain and required a degree of judgment, included primarily S&P Index volatility, forward interest rate projections, estimated index dividend payout, and leverage. At September 30, 2016 there were no transaction outstanding.

Servicing assets

Servicing assets do not trade in an active market with readily observable prices. Servicing assets are priced using a discounted cash flow model. The valuation model considers servicing fees, portfolio characteristics, prepayment assumptions, delinquency rates, late charges, other ancillary revenues, cost to service and other economic factors. Due to the unobservable nature of certain valuation inputs, the servicing rights are classified as Level 3.

Impaired Loans

Impaired loans are carried at the present value of expected future cash flows using the loan's existing rate in a discounted cash flow calculation, or the fair value of the collateral if the loan is collateral-dependent. Expected cash flows are based on internal inputs reflecting expected default rates on contractual cash flows. This method of estimating fair value does not incorporate the exit-price concept of fair value described in Accounting Standards Codification ("ASC") 820-10 and would generally result in a higher value than the exit-price approach. For loans measured using the estimated fair value of collateral less costs to sell, fair value is generally determined based on the fair value of the collateral, which is derived from appraisals that take into consideration prices in observed transactions involving similar assets in similar locations, in accordance with the provisions of ASC 310-10-35 less disposition costs. Currently, the associated loans considered impaired are classified as Level 3.

Foreclosed real estate

Foreclosed real estate includes real estate properties securing residential mortgage and commercial loans. The fair value of foreclosed real estate may be determined using an external appraisal, broker price option or an internal valuation. These foreclosed assets are classified as Level 3 given certain internal adjustments that may be made to external appraisals.

Other repossessed assets

Other repossessed assets include repossessed automobiles. The fair value of the repossessed automobiles may be determined using internal valuation and an external appraisal. These repossessed assets are classified as Level 3 given certain internal adjustments that may be made to external appraisals.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Assets and liabilities measured at fair value on a recurring and non-recurring basis are summarized below:

	September 30, 2016 Fair Value Measurements			
	Level 1	Level 2	Level 3	Total
	(In thousands)			
Recurring fair value measurements:				
Investment securities available-for-sale	$ -	$ 642,683	$ -	$ 642,683
Trading securities	-	380	-	380
Money market investments	5,460	-	-	5,460
Derivative assets	-	1,503	-	1,503
Servicing assets	-	-	8,393	8,393
Derivative liabilities	-	(4,306)	-	(4,306)
	$ 5,460	**$ 640,260**	**$ 8,393**	**$ 654,113**
Non-recurring fair value measurements:				
Impaired commercial loans	$ -	$ -	$ 36,601	$ 36,601
Foreclosed real estate	-	-	45,740	45,740
Other repossessed assets	-	-	3,449	3,449
	$ -	**$ -**	**$ 85,790**	**$ 85,790**

	December 31, 2015 Fair Value Measurements			
	Level 1	Level 2	Level 3	Total
	(In thousands)			
Recurring fair value measurements:				
Investment securities available-for-sale	$ -	$ 974,609	$ -	$ 974,609
Trading securities	-	288	-	288
Money market investments	4,699	-	-	4,699
Derivative assets	-	1,853	1,172	3,025
Servicing assets	-	-	7,455	7,455
Derivative liabilities	-	(6,162)	(1,095)	(7,257)
	$ 4,699	**$ 970,588**	**$ 7,532**	**$ 982,819**
Non-recurring fair value measurements:				
Impaired commercial loans	$ -	$ -	$ 235,767	$ 235,767
Foreclosed real estate	-	-	58,176	58,176
Other repossessed assets	-	-	6,226	6,226
	$ -	**$ -**	**$ 300,169**	**$ 300,169**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The table below presents a reconciliation of all assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the quarters and nine-month periods ended September 30, 2016 and 2015:

	Quarter Ended September 30, 2016			
Level 3 Instruments Only	**Derivative asset (S&P Purchased Options)**	**Servicing assets**	**Derivative liability (S&P Embedded Options)**	**Total**
Balance at beginning of period	$ 187	$ 7,932	$ (181)	$ 7,938
Gains (losses) included in earnings	(187)	-	181	(6)
New instruments acquired	-	466	-	466
Principal repayments	-	(123)	(1)	(124)
Amortization	-	-	1	1
Changes in fair value of servicing assets	-	118	-	118
Balance at end of period	$ **-**	$ **8,393**	$ **-**	$ **8,393**

	Nine-Month Period Ended September 30, 2016			
Level 3 Instruments Only	**Derivative asset (S&P Purchased Options)**	**Servicing assets**	**Derivative liability (S&P Embedded Options)**	**Total**
Balance at beginning of period	$ 1,170	$ 7,455	$ (1,095)	$ 7,530
Gains (losses) included in earnings	(1,170)	-	1,067	(103)
New instruments acquired	-	1,740	-	1,740
Principal repayments	-	(347)	-	(347)
Amortization	-	-	28	28
Changes in fair value of servicing assets	-	(455)	-	(455)
Balance at end of period	$ **-**	$ **8,393**	$ **-**	$ **8,393**

	Quarter Ended September 30, 2015			
Level 3 Instruments Only	**Derivative asset (S&P Purchased Options)**	**Servicing assets**	**Derivative liability (S&P Embedded Options)**	**Total**
Balance at beginning of period	$ 2,138	$ 5,791	$ (2,044)	$ 5,885
(Losses) gains included in earnings	(1,023)	-	972	(51)
New instruments acquired	-	748	-	748
Changes due to payments on loans	-	(242)	-	(242)

Amortization		-		-		31		31
Changes in fair value of servicing assets		-		166		-		166
Balance at end of period	$	**1,115**	$	**6,463**	$	**(1,041)**	$	**6,537**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Nine-Month Period Ended September 30, 2015			
Level 3 Instruments Only	**Derivative asset (S&P Purchased Options)**	**Servicing assets**	**Derivative liability (S&P Embedded Options)**	**Total**
Balance at beginning of period	$ 5,555	$ 13,992	$ (5,477)	$ 14,070
(Losses) gains included in earnings	(4,440)	-	4,271	(169)
Sale of mortgage servicing rights held-for-sale	-	(6,985)	-	(6,985)
Changes due to payments on loans	-	(974)	-	(974)
New instruments acquired	-	2,808	-	2,808
Amortization	-	-	165	165
Changes in fair value related to price of MSRs held for sale	-	(2,716)	-	(2,716)
Changes in fair value of servicing assets	-	338	-	338
Balance at end of period	**$ 1,115**	**$ 6,463**	**$ (1,041)**	**$ 6,537**

During the quarters and nine-month periods ended September 30, 2016 and 2015, there were purchases and sales of assets and liabilities measured at fair value on a recurring basis. There were no transfers into or out of Level 1 and Level 2 fair value measurements during such periods.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The table below presents quantitative information for all assets and liabilities measured at fair value on a recurring and non-recurring basis using significant unobservable inputs (Level 3) at September 30, 2016:

	September 30, 2016				
	Fair Value (In thousands)		Valuation Technique	Unobservable Input	Range
Servicing assets	$	8,393	Cash flow valuation	Constant prepayment rate	5.18% - 10.49%
				Discount rate	10.00% - 12.00%
Collateral dependant impaired loans	$	23,759	Fair value of property or collateral	Appraised value less disposition costs	29.20% - 46.20%
Non-collateral dependant impaired loans	$	12,840	Cash flow valuation	Discount rate	4.25%-10.50%
Foreclosed real estate	$	45,740	Fair value of property or collateral	Appraised value less disposition costs	29.20% - 46.20%
Other repossessed assets	$	3,449	Fair value of property or collateral	Appraised value less disposition costs	29.20% - 46.20%

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Information about Sensitivity to Changes in Significant Unobservable Inputs

Derivative asset (S&P Purchased Options) – The significant unobservable inputs used in the fair value measurement of the Company's derivative assets related to S&P purchased options are implied option volatility and counterparty credit risk. Significant changes in any of those inputs in isolation would result in a significantly different fair value measurement. Generally, a change in the assumption used for implied option volatility is not necessarily accompanied by directionally similar or opposite changes in the assumption used for counterparty credit risk.

Servicing assets – The significant unobservable inputs used in the fair value measurement of the Company's servicing assets are constant prepayment rates and discount rates. Changes in one factor may result in changes in another (for example, increases in market interest rates may result in lower prepayments), which may magnify or offset the sensitivities. Mortgage banking activities, a component of total banking and financial service revenue in the consolidated statements of operations, include the changes from period to period in the fair value of the mortgage loan servicing rights, which may result from changes in the valuation model inputs or assumptions (principally reflecting changes in discount rates and prepayment speed assumptions) and other changes, including changes due to collection/realization of expected cash flows.

Derivative liability (S&P Embedded Options) – The significant unobservable inputs used in the fair value measurement of the Company's derivative liability related to S&P purchased options were implied option volatility and counterparty credit risk. Significant changes in any of those inputs in isolation would result in a significantly different fair value measurement. Generally, a change in the assumption used for implied option volatility is not necessarily accompanied by directionally similar or opposite changes in the assumption used for counterparty credit risk.

Fair Value of Financial Instruments

The information about the estimated fair value of financial instruments required by GAAP is presented hereunder. The aggregate fair value amounts presented do not necessarily represent management's estimate of the underlying value of the Company.

The estimated fair value is subjective in nature, involves uncertainties and matters of significant judgment and, therefore, cannot be determined with precision. Changes in assumptions could affect these fair value estimates. The fair value estimates do not take into consideration the value of future business and the value of assets and liabilities that are not financial instruments. Other significant tangible and intangible assets that are not considered financial instruments are the value of long-term customer relationships of retail deposits, and premises and equipment.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The estimated fair value and carrying value of the Company's financial instruments at September 30, 2016 and December 31, 2015 is as follows:

	September 30, 2016		December 31, 2015	
	Fair Value	Carrying Value	Fair Value	Carrying Value
	(In thousands)			
Level 1				
Financial Assets:				
Cash and cash equivalents	$ 509,265	$ 509,265	$ 536,709	$ 536,709
Restricted cash	3,030	3,030		